

CHAPTER I

INTRODUCTION

Title of Dissertation

FOREIGN AID AS A TOOL OF FOREIGN POLICY – JAPAN'S OFFICIAL DEVELOPMENT ASSISTANCE (ODA) POLICY IN CHINA

Introduction

Foreign aid has always been used as an instrument to achieve political aim, especially by the developed nations. A major goal of foreign aid governed by donors' interests is to distribute payments, positive incentives or downright bribes among recipient countries. Such rewards are extended when the recipient countries abide by basic rules of international relations, such as securing a good economic and political environment for trade and foreign investment as well as protection of democracy and human rights. Donors can use their financial contributions to 'buy' favorable attitudes and good behavior from recipient countries. On the other hand, foreign aid suspension can constitute a negative incentive. Suspensions of foreign aid clearly indicate objections by donors against conduct, policies or regimes of recipient countries. Such negative stimulus can range from a mild sign of disapproval to outright coercion to change the behavior of the recipient.

This study concentrates on foreign aid, namely Japan's Official Development Assistance (ODA) to China from 1978 to 2003.

Japan has become increasingly involved in providing economic assistance for the development of less-developed countries. Since 1989, Japan has been the world's biggest donor of ODA in absolute terms. In 2000, Japan's ODA constituted 25.2 per

cent of total ODA of Development Assistance Committee (DAC) countries' contributions totalling US\$53,504 million.¹

In addition, Japanese aid emphasizes heavily on Asia. In 1998, 62.4 per cent of all bilateral aid went to Asia, 63.2 per cent in 1999 and 54.8 per cent in 2000.² Asian countries received the main part of their aid in the form of loans, receiving a total of 91.5 per cent of all the loan aid. The top recipient on a cumulative basis was Indonesia. China has a much shorter history of receiving aid but is quickly catching up and was the largest recipient during much of the 1990s.

An ODA programme to the People's Republic of China commenced after the declaration of an open-door policy and Prime Minister Ohira Masayoshi's visit to China in 1979. Since that time ODA has grown enormously. Between 1982 and 1986, China was the single largest recipient of ODA from Japan. The incident at Tiananmen Square in 1989 led to a temporary cessation of ODA, but aid was soon resumed, Japan being the first nation to restore friendly relations with China. In August 1989, it lifted the freeze on ongoing projects and in October that year the World Bank resumed its lending to China for humanitarian aid. After that, Japan extended aid in the form of grants, and in July 1990 it announced that all aid would gradually be resumed. Soon after that other industrialized countries followed. Since then China has remained as one of the major, if not the top, recipients of Japanese aid.

Since Japan provided ODA to China in 1979, China has received four economic assistance tranches worth US\$19 billion from Japan. Most of the funds were used for China's infrastructure development.

¹ Development Assistance Committee (DAC), press release, 2001

² White Paper on Japan's Official Development Assistance (ODA) 2001, pp.91

Nevertheless, according to the Ministry of Finance of Japan, it might cut ODA funds for other countries by postponing until fiscal 2005 the implementation of some ODA-funded projects, and the Japanese Government is expected to reduce low-interest yen loans to China, which constitute the major pillar of Japan's assistance to the country by about 20 per cent. This was to divert part of Japan's fund assistance to Iraqi's reconstruction; hence its plans to trim ODA to other countries to achieve what is expected to be a small-scale overall reduction in conjunction with overall Japan's ODA cut in the fiscal 2004 budget for the fifth straight year.³

However, according to some commentators, the Japanese Government cut its ODA to China – which could possibly be an indirect result of China's successful manned space mission in early November 2003, which reflected on China's economic advancement. While Japan's ODA to China would decline to US\$8 billion, Japan's ODA to India would increase by 20 per cent. *The India Times* reported that India would replace China as the biggest recipient of Japan's ODA since the financial year of 2004.⁴ Some political analysts believed that Japan's ODA to India was originally allocated to China. Even though the Ministry of Foreign Affairs of Japan emphasized that Japan does not intend to 'fight with' China, some Japanese media pointed out that Japan's ODA increment to India has a hidden agenda, which is to contain China.

³ "China loans face 20 per cent cut as part of overall ODA reduction", *The Japan Times*, 4 November 2003

⁴ "Japan cuts its ODA to China to RM3 billion as China's successful manned space mission has reflected China's economic achievement", *The Oriental Daily, Malaysia*, 5 November 2003

Objective of the Study

This dissertation deals with Japan's ODA policy in China. It aims to study Japan's ODA purely as a form of aid from Japan in helping China's domestic development, or Japan's ODA as an instrument of Japan's foreign policy in order to influence or pressure the Government of China in Japan's national interests.

This research also means to give an overall picture of Japan's foreign policy, particularly on China in order to find out whether Japan's foreign aid policy has been utilized as a tool in implementing the goals of its foreign policy.

Indeed, the paper wishes to examine the historical cases that have shown Japan's utilization of ODA in intervening China's domestic policy as well as foreign policy.

It is the writer's intention to examine the influence of Japan's foreign policy in its ODA to China. Is Japan's ODA primed to serve Japanese diplomacy and security plans better?

Theoretical Approach

For the writer's purposes, the most relevant theory is the donor-oriented or international relations theory (John White, 1974, The Politics of Foreign Aid, London, p.128). The donor-oriented theory believes that donors pursue other objectives in their aid programmes besides the promotion of economic development. The donor-oriented theory also argues that the promotion of the welfare of poor countries is ultimately in the rich countries' interest. However, the rich countries' long-term interest in the welfare of poor countries might be both political and economic. In political terms, the rich countries might be interested in stability. On the basis of an assumption that hunger breeds discontent, and that discontent breeds instability, they might see the

promotion of economic development as the means of preserving the political status quo. In economic terms, the rich countries might be interested in a world economy organized on the principles of comparative advantage and the international division of labour, helping the rich to specialize in what they do best.

The donor-oriented theory, therefore, is likely to fall back on the more conventional and much more convincing identification of specific foreign policy objectives which the donors pursue, such as the maintenance of military alliances or trading and investment relationships.

Research Methodology

Both qualitative and quantitative methods were applied in this dissertation study.

Also, this study was conducted through a combination of primary and secondary research. The historical method of organizing the material is mainly used because the writer believes in order to understand the Japan's ODA policy in China and its impact in influencing Chinese Government it is necessary to trace its historical development.

Because the study covered the period from 1978 to 2003, there are available enough sources, particularly within Japan and China, to come up with the conclusion. The sources on which this study is based fall roughly into four categories: (1) Japan's ODA Annual Reports published by Japan International Cooperation Agency (JICA); (2) Japan's Foreign Policy White Books; (3) Academic books, journals and articles from the US, China, the U.K. as well as Japan on Foreign Aid, by focusing on Japan's foreign policy and its foreign aid policy in Asia; (4) Global trends and international affairs concerning international security issues.

Recent discussions were conducted with Japanese diplomats, academicians in universities, as well as think-tanks at home and abroad.

Definition of Key Concepts

According to John White (The Politics of Foreign Aid, London, 1974), the term “Foreign Aid” can only be properly applied to actions taken by people or institutions in one country towards people in institutions in another country which help, or are at least intended to help, the latter.

“A tool of foreign policy” means an instrument of the foreign policy of the donor country in influencing the recipient country. Economic sanction, democracy, aid, propaganda as well as unconventional warfare have been utilized as tools of foreign policy by states in dealing with other countries.

The Development Assistance Committee (DAC) has defined “Official Development Assistance” as all flows to less-developed countries and multilateral institutions provided by official agencies which meet the following tests:

- a. “They are administered with the promotion of the economic development and welfare of developing countries as their main objective; and
- b. Their financial terms are intended to be concessional in character.

DAC has excluded from these flows official and private gifts of, or loans for the purchase of, military supplies and official grants to private individuals resident in the developing countries, such as pensions, unless they are part of technical assistance or relief programmes.

Generally, of various forms of economic assistance provided to developing countries, ODA is that made by governments with concessionary elements in terms of lower interest rates and longer repayment periods than in the case of loans; it contains the so-called “grant element”. The grant element is 100 percent in the case of grant aid, while it is zero per cent in the case of a loan with a commercial interest rate. In between, the grant element is calculated by the margin of concessionality compared to commercial loan conditions. In any case, aid cannot be labeled ODA unless the grant element is over 25 per cent. Government aid that is outside the scope of ODA is called “other official flows” (OOF).

In Japan, ODA is provided through the Japan International Cooperation Agency (JICA) and the Overseas Economic Cooperation Fund (OECF), while OOF goes through the Export-import (EXIM) Bank of Japan. However, in April 1999, the Japan Export-import Bank (JEXIM) and the ECF were merged to form the Japan Bank for International Cooperation (JBIC). ODA accounts, formerly OECF operations, and non-ODA accounts, formerly JEXIM operations, are kept separate.

There are two types of ODA, namely technical cooperation and financial assistance. In technical cooperation, Japan receives trainees, dispatches experts, provides equipment, conducts feasibility studies, and dispatches Youth Cooperation Units. In terms of financial assistance, Japan provides both grant aid that does not require repayment and yen loans that require repayment under concessionary conditions. Grant aid is provided from tax revenues, while ODA loans or yen loans are provided from the Fiscal Investment and Loan Programme (FILP), using monies from postal savings and pension funds.

In addition to bilateral ODA, Japan also provides multilateral aid through multilateral development agencies such as the United Nations Development Programme (UNDP). Japan also provides contributions and subscriptions to international organizations such as the United Nations, the World Bank, and the Asia Development Bank, which are categorized as multilateral grants.

Nature and Use of Literature on the Subject: A Critique

The importance of donor interests, rather than recipient needs, dominates discussion of the motivation of foreign aid given by major donors. Schraeder, Hook and Taylor (Schraeder, Peter J., Steven W. Hook and Bruce Taylor, 1998, Clarifying the Foreign Aid Puzzle: A Comparison of American, Japanese, French and Swedish Aid Flows'. World Politics 50 (January): pp. 294-323) analyzed four aid donors – the US, Japan, France and Sweden – during the Cold War and confirmed that donors' economic, security and cultural interests had dominated their aid allocation decisions. Although statistics show that the proportion of tied aid within Japan's overall foreign aid has significantly decreased in the 1990s, some authors argue that Japanese foreign aid is still strongly influenced by Japanese business interests. The corporatist nature of the Japanese state, with the notoriously close ties between government and big business, has linked Japanese foreign aid closely with Japanese business interests. The 'request basis' modality of Japan's foreign aid itself has enabled Japanese corporations operating in recipient countries to influence the types and allocations of Japanese foreign aid. Of course, such relationship also increases the influence of big business in Japan's aid policy-making.

If a single donor government is sufficiently important to a certain developing country, or concentrates its aid on a few major recipients, it may be able to exercise significant

influence over these recipients. A classic study by Hirschman (Hirschman, Albert, 1945, National Power and the Structure of Foreign Trade, Berkeley and Los Angeles: University of California Press) illustrates how a concentration of trade among a few Eastern European countries with Germany in the inter-war period enhanced German influence and power over them. In the case of foreign aid, the US enjoyed similar power from the 1950s through the 1960s. Baldwin (Baldwin, David A., 1985, Economic Statecraft, Princeton, N.J.: Princetown University Press) analyses US economic sanctions and argues that foreign aid serves as a tool of US economic statecraft. Although some critics deny that foreign aid and its suspension are effective policy tools, Baldwin asserts that such a conclusion is too premature unless the outcomes of alternative policy options are comprehensively analyzed and compared.

According to Hewitt and Killick (Hewitt, Adrian P. and Tony Killick. 1996. 'Bilateral Aid Conditionality and Policy Leverage', In Foreign Aid Towards the Year 2000: Experience and Challenges, ed. Olav Stokke. EADI Book Series no. 18, London: Frank Cass), aid suspension and aid conditionality have often been used to pursue the economic and political objectives of donors, effective or not. Stokke (Stokke, Olav. 1996. 'Foreign Aid: What Now?' in Foreign Aid towards the Year 2000: Experience and Challenges, ed. Olav Stokke, EADI Book Series No. 18. London: Frank Cass) notes that the 'second generation' of aid conditionality often aims at political reforms. Foreign aid policy is not only concerned with financial or technical resource transfer, but also targets cultural concepts and values, such as democracy and human rights, that Western aid donors would like to promote. However, Stokke observes that donors are far more likely to use aid as a policy tool with small aid recipients than with major aid recipients such as China or India.

Actually, many donor countries have legal provisions governing foreign aid. Where conditions for aid eligibility are seriously and repeatedly violated by recipient governments, aid donors can individually or collectively react and suspend payments. Many non-democratic African countries, including Kenya, have been deprived of aid until they implement democratic reforms. Repeated aid suspension by most Development Assistance Committee (DAC) donors has been a factor leading the Kenyan government to amend its constitution to allow multiparty elections. Malawi also faced suspension of non-humanitarian aid by its donors in May of 1992, and this pressure accelerated Malawi's democratization process, leading to elections in 1994.

A recent study by Long (Long, William J., 1999, Nonproliferation as a Goal of Japanese Foreign Assistance, *Asian Survey* 39: pp. 328-347) concluded that Japan's aid policy has recently begun to show increasing assertiveness in pursuing its security interests vis-à-vis aid recipient countries. Although Hewitt and Kililck (1996: 139) are correct to state that the Japanese Government is still reluctant to move into aid conditionality, some observe an increasing proactive stance in Japan's use of foreign aid as a tool of statecraft.

Two influences on foreign aid as economic statecraft require attention. The first of these is the interaction and convergence of aid-giving behavior among major donors. Collaboration among donors can enhance the impact of foreign aid policies in influencing recipient behavior (Martin, Lisa, 1992, Coercive Cooperation: Explaining Multilateral Economic Sanctions, Princeton, N.J.: Princeton University Press). Some cases where a group of donors has frozen aid flows to anti-democratic governments in developing countries show how the convergence of aid policy may stem from conscious and structured co-operation among donors. Many developing countries are quite

vulnerable to these orchestrated suspensions of aid (Cusak, Thomas R. and Joyce P. Kaufman, 1994, The Evolution of Western Foreign Aid Programmes: pp. 12-14). International bodies such as the Organization for Economic Co-operation and Development (OECD) and its affiliate, the DAC, are among consultative bodies on aid providing for peer pressure on policy co-ordination. Convergence may also facilitate and be facilitated by an 'aid regime' that evolves around a core of aid norms.

The second influence is domestic public opinion. This can be a critical factor, particularly when a foreign aid preference reflects domestic pressure, such as the farm lobby for US food aid or the construction industry for Japanese infrastructure aid. In such cases, the suspension of aid may incur political costs arising from the opposition of these influential domestic actors against governments' actions. Hence suspension of aid, particularly to a major aid recipient, demonstrates a strong commitment to a particular outcome or value on the part of the donor government (Martin, Lisa, 1993, Credibility, Costs, and Institutions: Cooperation on Economic Sanctions, *World Politics* 45 (April): pp. 415-416).

The potential for foreign aid as a tool of Japan's economic statecraft exists. The Japanese Government, as the largest aid donor in the ten years from 1989 to 1998, is in a position to impose penalties – not only economic but also political – on its aid recipients. More research is needed on how that power is exercised.

Organization of Chapters

Chapter I	: Introduction
Chapter II	: Japan's Foreign Policy towards China
Chapter III	: Japan's ODA Policy towards China
Chapter IV	: The Politics of Aid in Japan's ODA Policy towards China
Chapter V	: Conclusion

Chapter II studies Japan's foreign policy towards China. It also tries to provide a general idea about Sino-Japanese relationship by dividing into five periods, which are 1895-1911, 1911-1927, 1927-1936, 1937-1945, and post-1945.

Chapter III examines Japan's ODA policy towards China as well as Japan's ODA relationship with China since 1978.

Chapter IV studies how ODA was utilized as a tool of Japan's foreign policy in pressuring the Chinese Government and influencing China's domestic politics. The chapter provides two suspension cases of Japan's ODA in China, following the Tianamen Square Incident in 1989, and China's nuclear testing in 1995, in illustrating that the Japanese Government has established extension and suspension of its foreign aid as a multi-use foreign policy tool, as the country became the top aid donor in the world in the 1990s.

Chapter V aims to analyze the level of successfulness of Japan's ODA in China in supplementing Japan's foreign policy as a tool of bargaining card. It looks at carefully how Japan's ODA has affected government to government relationship.