

## JAPANESE AID

*Japan claims an aid 'outlay' of over \$10 bn in 1989, having spent a record \$9.1bn in foreign aid in 1988 when it came near to becoming the world's largest aid donor — the USA's official development assistance (oda) totalled \$10.1bn. Japan has managed to double its aid on average every five years since it became a member of the Development Assistance Committee of the OECD and is likely to have overtaken the USA when 1989 donor calculations are released by the DAC in summer 1990. Japan's aid disbursements in 1988 rose by 22.5% in dollar terms (8.6% in yen) and Japan is currently committed to doubling its aid again in five years under a fourth medium-term aid plan for 1988-92.*

*Starting with the origins of Japanese aid, this Briefing Paper analyses the volume and direction of the programme. It then considers the role aid plays in Japan's foreign policy and the special features of Japan's aid administration. It concludes by looking at the future directions Japanese aid policy can take.*

### Stage-by-stage history

It is essential to an understanding of Japan's future aid role to appreciate how aid policy has evolved. Japan joined the OECD only in 1964 and is still repaying some World Bank loans even today, but has been an aid donor in the conventional sense from the 1950s (with DAC founder-membership in 1961). Some Japanese scholars and analysts see Japan's role in the Greater East Asian Co-prosperity sphere in the 1930s as development assistance, but it is safer to see the evolution of Japan's present donor role in five post-war stages:

1. **War reparations**, starting in the 1950s. Over \$1.2bn of government funds were transferred in damages to Burma, Philippines, Indonesia and Vietnam. About \$738m was also given in loans under the same scheme. China was excluded on political grounds while India waived war reparations in favour of development credits. Japanese business leaders played a key role in negotiating the reparation arrangements, ahead of the Ministry of Finance, this setting an early pattern for Japan's oda at its origin. Japan's Eximbank had been established in 1952.

2. **Trade promotion through tied yen credits**. In 1958 Japan extended its first yen credit to India. This was seen as a new vehicle for penetrating Asian markets with Japanese plant and material, but also to stimulate resource flows in both directions. Levels of concessionality were low, and tying absolute, but this was justified on the grounds that Japan herself had barely recovered economically — in 1958 her per capita income was \$280 -closer to that of India than to the OECD donors. Japan had also joined the Colombo Plan (1956) and so participated in technical assistance early on.

3. **Aid as part of an Asian strategy**. In the 1960s, the yen credits to Asia blossomed. Japan extended assistance to South Korea and Taiwan, and helped create the regional bank, the Asian Development Bank, in 1966. Japan wanted to provide the headquarters of the ADB but the USA insisted that this be established in Manila. As well as making sound economic sense at the time, the Asian aid push was also part of a 'good neighbour' strategy. Political sensitivity arising from Japan's role in war and occupation remained delicate, and a generous aid policy to Asian countries offered without any overt attempt at intervening in domestic political processes was part of this overall strategy. The OECF (for credits) and a technical assistance agency (OTCA) were established for this period. The JOCV (volunteers) scheme came a little later and JICA, the present technical assistance agency, was not established until 1974; unrequited grant aid, as opposed to reparations, was a relatively new phenomenon.

4. **The beginning of global assistance**. By the 1970s, Japan's GNP had overtaken that of Britain and Germany to become a major economic power. Encouraged by the USA towards more 'burden sharing', Japan began to expand oda rapidly, to contribute more fully to international organisations and to shift from a near-exclusive geographic focus on Asia to initiating small programmes

in Africa and Latin America. This geographical dispersion was also a reaction to Middle East tension and oil supply difficulties after 1973. The bilateral programme was nevertheless still 85% Asia-based at the end of the 1970s. Nixon's overture to Beijing led the way to a China oda programme which was later to become Japan's largest.

5. **Surplus recycling**. Recognising that if Japan's massive current account surplus (\$80bn in 1987) were to be simply recycled according to market mechanisms, it would be attracted to the most buoyant economic areas — mainly in rich countries — Japan took steps in the 1980s to enhance its role in intervening in the world economy, notably by boosting oda and supporting recycling, debt relief and (as of March 1989) debt reduction measures. New initiatives are awaited: despite four medium-term oda target programmes and, in 1989, a major debt recycling programme (partly oda), Japan's policy so far has been essentially reactive. Moreover, according to the DAC, Japan still received \$871m interest in oda in 1987, far more than any other donor: an indication of the extent to which Japan's development assistance is still loan-based and seen as latently remunerative.

It is easier to date the beginning of a stage than to specify its end. Of the five stages, only war reparations has fully ended. Present bilateral oda is still dominated by yen credits. The Asian focus remains. Japan's role of global responsibility may not yet be commensurate with the reality of her being the leading surplus nation and supplier of oda. Many observers would cite the emergence of 'strategic aid' as a phenomenon which cuts across the above categories. This would be linked to the arguments about 'burden-sharing', combining aid and defence expenditures, and would give pride of place to security rather than development assistance. This approach is particularly relevant to an analysis of the evolving US-Japanese alliance, in which oda policies are used in a trade-off for alleged 'shortcomings' in other areas.

### Volume

Japan's aid programme is about four times as large as Britain's (\$2.6bn/£1.5bn in 1988). Both countries currently devote 0.32% of GNP to official development assistance. This is below the DAC average of 0.36% in 1988 (Japan supplies 18.4% of OECD aid but accounts for 21.6% of its gross economic output): it is well ahead of the US position (0.21% of GNP) but below the average for EC Members (0.5%).

In terms of total net Japanese financial flows to developing countries (\$20.4bn in 1987), aid has risen to take a half-share as new private sector lending and direct foreign investment has fallen or stagnated. Thus, not only has aid spending grown, but official aid policy has become increasingly important vis-à-vis private sector initiatives in developing countries when measured on a net current basis.

Table 1. Aid disbursements<sup>a</sup>, 1988: Selected donors

	\$m	% of GNP	Change <sup>b</sup> 1982/3-1987/8 (%)	Untied Share 1986 (%)
USA	10,141	0.21	-0.1	54.3
Japan	9,134	0.32	5.4	71.0
France <sup>c</sup>	4,777	0.50	3.5	49.1
W Germany	4,731	0.39	-1.7	71.1
UK	2,645	0.32	-1.3	43.0

a Net official development assistance

b Annual average change over period.

c Excluding DOM-TOM

Source: Development Assistance Committee, OECD, Paris 1989, except final column which derives from earlier DAC reports.

## Country distribution

Starting as a pronounced Asian aid donor, Japan has recently adopted a broader development assistance strategy and has developed a presence in Africa and Latin America too. Japan is already the biggest bilateral aid donor in twenty-nine countries, not merely the Far Eastern and SE Asian developing countries, but also Kenya, Zambia, Ghana and even Nigeria. Overall,

**Table 2: Major Bilateral Aid Recipients, 1988**

	\$m	%
Asia	4,039	62.8
Indonesia	985	15.3
China	671	10.5
Philippines	535	8.3
Thailand	361	5.6
Bangladesh	342	5.3
Pakistan	302	4.7
India	173	2.8
Africa	884	13.8
Middle East	584	9.1
Latin America	399	6.2
Other	522	8.1
Total	6,425	100.0

Source: Morgan Guaranty World Financial Markets

Japanese bilateral aid to sub-Saharan Africa now ranks fourth after France, Italy and Germany, and ahead of USA and UK.

Japan is the largest contributor to the Asian Development Bank and has challenged the UK for the second ranking which is due in the IMF. A reranking arranged in 1990 will place Japan second, Germany third and the UK fourth with France. Japan is already second in the World Bank on the strength of her IDA contributions, is the leading contributor to the African Development Bank, and has played a key role in recycling funds to debt-distressed Latin American countries, effectively underpinning the USA's Brady initiative.

Such has been the expansion of the aid programme that the new programmes in Africa and Latin America have made relatively little impression on the proportion going towards Asia. As Table 2 shows, the seven leading recipients of Japanese bilateral aid are all Asian, and around two-thirds of the overall programme will continue to be allocated there (Asia took 65% in 1987). Absorptive capacity in other parts of the developing world, given Japan's present administrative guidelines, is such that the overall balance cannot be greatly altered. There also remain strong foreign policy pressures to ensure a dominant aid position in Asia. Challenged in January 1990 during a South-East Asia tour that Japan's promises of support for East European reforms might be at the expense of the established foreign aid budget, foreign minister Taro Nakayama put on record

'Our ODA (development assistance) to the Asia-Pacific will not be adversely affected by our assistance to Hungary and Poland. This is never going to be affected. I am here to make this clear.'

The Asian aid focus is also maintained for commercial and strategic reasons. Table 3 shows Asia is the leading developing country region for direct foreign investment. The importance of this regional focus for aid too is seen most clearly in the case of People's Republic of China, Japan's second largest aid recipient. All Japanese aid was suspended immediately after the 4 June

**Table 3. Direct foreign investment<sup>a</sup> by region**

	\$m
North America	75,091
Europe	30,164
Asia	32,227
Latin America & Caribbean (excluding Panama and Cayman Islands)	13,674
Oceania	9,315
Middle East	3,338
Africa (excluding Liberia)	946
TOTAL, including money centres excluded above	186,356

a Capital value (as of 31 March 1989)

Source: Ministry of Finance

Tiananmen massacres. But by 17 August, the Foreign Ministry was already announcing a limited resumption. It cannot afford to let such a large programme lapse.

## Terms and sectoral emphasis

Japan's aid still remains predominantly a loan programme: until recently outright grants were rare. The aid programme's grant element (75%) is below that of all other DAC donors save Austria, and well below the UK (99%) and Sweden (100%). Its sectoral breakdown continues to show greatest interest in transport infrastructure and energy installations (Table 4), although the influence of multilateral commitments under programme aid and support for new technical assistance initiatives based on transfers of Japanese management is now beginning to alter this pattern.

**Table 4. Sectoral Distribution of Bilateral oda Commitments, 1987. (\$m)**

	Grants	Loans	Total
Economic infrastructure (Transport, communications energy ...)	289	3,324	3,614
Production (Agriculture, industry, trade ...)	685	422	1,108
Social Services (Education, health, water, planning ...)	753	276	1,029
Multisector	103	—	103
Programme Aid	—	1,048	1,048
Debt Reorganisation	49	67	116
Food and Emergency Aid	96	—	96
(Donor) Administrative Costs	214	—	214
Support for NGOs	2	—	2
TOTAL (inc other):	2,205	5,137	7,342

Source: Ministry of Foreign Affairs, 1989

## Aid's role in Japan's foreign policy

Japan has no tradition of giving away official aid to poorer countries overseas: the motivation for breaking out of centuries of isolation and later dominating Korea and Manchuria bears little relation to the current concept of development assistance. Japan cannot call on the equivalent of (for the UK) the Colonial Development and Welfare Acts to justify its overseas aid: nor was it like the western OECD nations a direct participant in Marshall Aid, from which the DAC system of aid coordination developed. Concepts of Christian charity (which underpin at least the unofficial side of Western aid donors) and the Moslem practice of alms-giving (relevant for most of the OPEC donors) are foreign to Japanese society.

Nor is there an active 'development lobby': the leading non-governmental organisations are creatures of individual ministries, or else tend to have their roots in Buddhist spiritualism. Shintoism itself is nationalistic not internationalist. There is little to compare with the scale and scope of, say, Oxfam, although the Ministry of Foreign Affairs lists over 200 development NGOs.

Foreign aid is still a very foreign concept for most Japanese. A pertinent sign is that the normal Japanese term for aid, 'enjo' (or 'Kaiatsu enjo' = development assistance), is hardly ever used. In discussions and publications in Japanese the foreign concept-acronym 'oda' will be customarily used. Recently the phrase 'keizai kyoryoku' has been used more to convey the concept of cooperation with equal but poorer and needier foreign partners in development.

The aid programme has grown as a response to global economic and security issues. In particular, Japan uses aid spending creatively to defuse other problems troubling the US-Japan security alliance like trade (too much of it), defence (not enough), technology (too advanced), tax base (too narrow) and so on. Japan's current account surplus (\$80bn in 1988 but now declining) and in particular its trade surplus with the USA (around \$50bn) are seen as the main points of friction. So long as the government

can say that it is, additionally, pulling increased weight as an aid donor, the relationship with the USA can be sweetened. Successive US administrations have regarded their own foreign aid as part of a seamless web extending into defence and security so for Japan it has been reasonable to respond to US encouragement towards a greater regional and international security role by referring to the (US-drafted) constitution of Japan which proscribes military activity overseas and by offering increased aid instead. Many Japanese officials still maintain that Japan supplies only 'request aid': perhaps because this avoids charges of imperialism, Japanese foreign investors adopt the same posture. In contrast, the local critics of aid maintain that Japan runs an aid programme only to buy a seat at the top table of Western nations. Likely US reactions remain an important determinant of Japanese foreign policy and so of aid policy.

Until recently, Japan appeared happy to hide under US skirts on all the major international aid policy issues — adjustment and conditionality, debt relief, environmental protection, even aid tying and the non-aggressive use of mixed credits. As Japan emerges as the leading donor to individual countries and supplier of funding to international development and finance institutions, a clearer position on policy issues is emerging.

## Global economic management

For nearly \$10bn of concessional transfer, the Japanese government is doing more than just buying international respectability among third world nations and among its donor peers; it is necessarily adopting global responsibilities which require it to play an increasing role in bodies like the Bretton Woods institutions and wield influence over developing countries' economic policies, particularly those in debt difficulties, and whose contribution to global demand is important.

## Adjustment and conditionality

On the linkage between aid and policy reform, the normal Japanese line is not to impose or dictate policies abroad: this is in sharp contrast to the prevailing donor/creditor position in the 1980s. While being in favour of efficient use of resources, Japan is far less doctrinaire about matters such as state corporation divestiture, the use of market prices alone to stimulate producers, and the merits of raw material export dependence. The Japanese use development cooperation as a way of gaining global political influence and sustaining markets (for supply as well as demand). In short, Japan sees the genuine merits in 'policy dialogue'.

## Debt

On debt initiatives, the Japanese government has been generous in providing funds, given the relatively low exposure of Japanese banks (about 10% of total ldc exposure). A new \$65 bn recycling programme, over five years, mixing government aid loans with private sector effort was announced at the 1989 Paris Summit. This perhaps reflects Japan's recognition of the relative imbalance in the Bretton Woods payments settlement system, where only the deficit countries (other than the US) are penalised: Japan feels it can act with some magnanimity on debt relief as a substantial (but now declining) surplus country.

## Tied aid

Japan's aid is no longer so closely tied to domestic procurement (see Table 1). Significantly, Japan's \$500m contribution to the UN Special Fund for Africa is all untied (about \$200m of it is administered by the UK's Crown Agents, the rest by UNDP). Japan remains competitive on international markets and so has less interest than many other donors in perpetuating mixed credit competition, although lower interest rates on loans gives Japan an edge.

Low tying ratios do not necessarily mean that Japanese contractors do not win. GEC's success in winning a signalling contract in Thailand was the exception rather than the rule. But under pressure from other DAC members, Japan in 1989 agreed to untie some feasibility study and design contracts for aid projects: it was argued that awarding these to Japanese consultants made the ultimate project management and procurement award a Japanese fait accompli. In future, Japan may well want to move further into aid domains such as management and training, where Japan has hitherto been a reluctant partner due to language barriers, and away from the infrastructure contracting which still dominates the loan

programme and causes friction when contracts are awarded. In the past, Japan has been criticised for targeting particular sectors for aid — and then winning commercially too. In future 'human resources aid' to developing countries is likely to rise.

## Japan's aid administration

Although aid features so prominently in foreign policy, the programme is not run as in the UK by a part of the Foreign Office. There is no single aid ministry or agency in the lead, but four central ministries:

- the Ministry of Foreign Affairs (MOFA)
- the Ministry of Finance (MOF)
- the Ministry of International Trade and Industry (MITI)
- and the Economic Planning Agency (EPA)

In the earlier stages of Japan's aid growth, MITI's influence was predominant. Behind MITI stands the Keidanren, the association of Japanese big business (unlike Britain's CBI, for instance, small firms are not admitted) which in the past actively promoted aid-tying and export subsidisation but which is now adopting a more 'globally responsible' view of Japan's aid role and Japan's longer-term economic interests. MITI's purchase over the aid programme is now much reduced.

Japan is the only country to produce two separate aid White Papers. They combine policy statements with annual reporting, each employing a different approach. MITI produces 'The Present State and Problems of Japan's Economic Cooperation' while MOFA produces 'Japan's Official Development Assistance', both annually. An abbreviated version of the October 1989 MOFA White Paper is given in the box. (The MITI White Paper, in contrast, addresses the domestic industrial constituency more directly).

The Ministry of Finance determines public resource allocation policies and so constrains both the overall rise in the programme's spending and the aid establishment: the Japanese aid programme is administered by only 1503 staff, HQ and overseas — about the same number as employed on Britain's aid programme, half that of Germany and the USA.

The MOF role is crucial in times of political change. With the weakening of the yen and the uncertainties surrounding the 1990 Elections, the Fiscal 1991 aid budget was limited to an 8.2% increase (whereas public spending was to rise 9.7% overall): in the late 1980s, aid allocations consistently rose faster than public spending. MOF is the parent ministry controlling Japan's Eximbank and determines Japan's policies towards and within the Bretton Woods institutions and the Regional Development Banks.

The globalisation of aid policy (and the elevation of development assistance to a major plank of foreign policy) has raised the status of MOFA in aid decision-making. This is likely to continue, particularly with new programmes (and new public funding?) for Eastern Europe. MOFA's UN department controls all Japan's multilateral contributions other than those through the development banks and IMF. It is also the parent ministry for two technical assistance agencies — the Japan International Co-operation Agency (JICA) and the volunteer programme (JOCV). The greater the strategic role, the more MOFA will gain the upper hand in policy-making so long as the Ministry of Finance is not obliged — by 'aid fatigue' or revenue constraints — to curtail foreign aid allocations.

The EPA's limited role serves as a reminder that Japan still sets much store by planning, regulation, and interchange between the public and private sectors in promoting development. The EPA is also nominally responsible for the Overseas Economic Co-operation Fund, OECF (the yen loan agency).

Beyond the core group of four central ministries, there are about sixteen ministries which exert influence on aid. With its direct links to infrastructure contractors and suppliers, the Ministry of Construction is among the most influential of these.

## Aid and politics

Current Japanese aid policy has been a response to requirements of international politics. Yet from out outside it has traditionally been viewed as a MITI-driven vehicle for promoting 'Japan Inc'. Between these two contrasting tendencies is a harder truth. Aid policy has not been terribly important for Japan in the past, at best a method of smoothing relations with its major allies. The Japanese public has been more introverted than its European counterparts in matters concerning the Third World. Interest in

**Box: The 1989 White Paper on Aid from the Ministry of Foreign Affairs**

**1: Present state of oda:**

1988 disbursements reached \$9.13bn; capital flows to ldc's are decreasing but Japan is implementing capital recycling measures.

Japan is adopting a flexible approach to deal with the diversifying needs of ldc's: non-project assistance and local cost financing are instanced.

Japan provides assistance to 154 countries and regions 'and leaves no developing countries unaided'. Asia dominates but Japanese aid reaches all parts of the globe. Japan was the largest aid donor in 29 countries in 1987.

**2: Goals**

The fundamental principles are 'recognition of mutual dependence' and 'humanistic considerations'. Japan's heavy global responsibilities, including that of being 'the only major non-Western industrial nation', provide the reason for giving aid. The aid is intended to promote economic and social development; stability; and deeper ties with Japan. Evaluation reports show that Japan's aid is accomplishing its intended goals.

**3: New Policy Measures and Issues**

a. Volume and effort: Japan recognises its assistance as a percentage of GNP is below the DAC average and that 'further enhancement is necessary', not only of volume but also the grant share (among the lowest in the DAC) and — despite Japan's rate of untied assistance being 'already among the highest' — aid procurement-tying.

b. Country-by-country aid policy to be developed. Human resources to be a key area.

c. Coordination with other donors to be fostered by taking the lead, e.g. the aid plan to ease the Philippine debt burden, and flood defences for Bangladesh.

d. Participation is recognised as crucially important, hence the enhanced role for Japanese and developing country NGOs. MOFA instituted a subsidy system for NGO activities in 1989. Public sector aid and private sector effort should be increasingly combined: capital recycling measures are one example.

e. The biggest task Japan's ODA faces is 'increasing the number of workers to implement assistance'. All overseas operations of Japan's aid programme 'should be brought under the single umbrella of the Ministry of Foreign Affairs'.

(Derived from the official summary W-89-6 issued October 1989)

aid has been kindled at times when major scandals erupt (the Marcos payments are a recent case in point) but the programme still depends heavily on receiving requests rather than actively designing projects and prescribing initiatives.

Moreover, aid has been largely kept out of the party political domain. The Liberal Democratic Party has dominated Japanese politics for forty years, and in the February 1990 election retained an absolute majority (271 seats) in the Lower House of 512, although factions within the party are extremely important. The Japanese do not on the whole admire their politicians. Therefore taxpayers' aid money has to be insulated from factional political influence rather more than in European countries: bureaucrats are entrusted with this task which they execute as teamwork. This means there is an absence of political leadership which is now at odds with Japan's world position as a leading supplier of aid.

Japan supplied a former foreign minister, Saburo Okita, to the Brundtland Environment Commission — he had earlier been on the Pearson Commission on Aid — but such world-ranking figures are rare in Japanese politics. Domestically there is now more Parliamentary interest in aid shown by the opposition, who have never held power. While the Socialist Party has tended to see development assistance as part of a dependency paradigm, a foreign aid reform bill being promoted by Mrs Nakanishi of the small Komeito party in the Upper House (House of Councillors) advocates the creation of a single ministry — or failing that a sole

agency under the wing of MOFA — and a redirection of policy towards the sustained relief of poverty. These are areas which are likely to be debated in future.

**Future directions**

Japanese aid has expanded so vigorously that it is easy to assume that volume increases will continue. Yet if Japan encounters economic setbacks, the programme could be vulnerable: any spending programme which increases the tax burden is now highly sensitive, as the introduction of a 3% consumption tax in 1989 proved. Furthermore, there is no popular base in favour of foreign aid: whereas the Norwegians show national pride at being No 1 donor in terms of aid: GNP ratios, the Japanese are merely bemused at overtaking US aid. In the more pluralistic society that Japan is likely to become, aid policies may be questioned more openly. So far expansion has been maintained because the government and the big business establishment see the utility of a programme which deflects US pressures on trade and defence. Aid to developing countries may however peak at around \$10 — \$12 bn in real terms (especially if the yen weakens further).

New funding is likely to be raised for economic reconstruction programmes in Eastern Europe. Most of this will be private money. Japanese business is particularly keen on Hungary and Poland, and appears to be cautious elsewhere. There ought to be relatively little risk of diversion of oda funds to these countries: Japan, like Britain and France at present, has made it clear that existing aid recipients will not be made to suffer.

Improvements in aid quality are now overdue. International pressure is forcing Japan to recognise its aid programme is too heavily dominated by yen loans: in future there will be a switch towards grants. The promotion of rapid economic growth with assumed 'trickle-down' will however remain the objective — Japanese policy-makers are not supportive of a poverty-focused aid approach. More original contributions to resolving developing country debt problems can be expected: already it is Japanese, rather than US aid which is underpinning the Brady Plan for Mexico.

Greater international confidence in aid-giving will allow Japanese politicians and officials to challenge reigning orthodoxies on matters such as policy-based lending. Already a Japanese-chaired panel advising on future policies for the Asian Development Bank has recommended a 15% ceiling on policy-based lending. (The equivalent level in the World Bank is around 25%). Japan is much more comfortable with physical procurement than macroeconomic policy conditions: this view may carry more weight internationally in the 1990s as the lessons of the enhanced exposure of donors and creditors to policy-based lending sink in.

Lastly, although Japanese aid has suffered relatively fewer budgetary constraints than the programmes of Western (and recently OPEC) donors, although it is an Asian donor with an Asian focus and although its administrative structure and political control systems are sui generis, Japan's aid is not so different from the other thirty-to-forty year-old aid programmes on which it is modelled and with which it has developed. The present initiatives for co-operation between UK and Japanese aid reflect as much the fundamental similarities in approach as the complementary elements in the programmes' coverage. Japan's technology and management skills are however likely to offer new forms of co-operation and resource transfer in response to the growing needs for human resource and institutional development in the 1990s.

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