

Japanese Development Cooperation for China

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JAPAN AND THE People's Republic of China resolved a thorny issue concerning Official Development Assistance (ODA) on February 14, 1997, five days before the death of China's leader, Deng Xiaoping. Japanese Foreign Minister Ikeda Yukihiko met with Chinese Foreign Minister Qian Qichen in Singapore and explained Tokyo's decision to resume ODA for China. With the resumption, the bilateral relationship, which had deteriorated following a Chinese nuclear test on August 17, 1995, returned to normal. Although the news media did not highlight this resumption of aid, Japan's decision to delay some ODA for China for the first time since starting the provision in 1979 was monumental.

In 1995 and 1996, a series of events made the Japan-China relationship the worst it has been since normalization in 1972. China's nuclear test heightened Japan's traditional nuclear "allergy" and pacifism. Other incidents related to the Republic of China and the Senkaku (Diaoyu to the Chinese) Islands got tangled up with the nuclear testing issue.

China's nuclear test and Japan's reaction showed a new dimension in Japanese ODA policy toward China. At the time, Japan was concerned about ensuring the effectiveness of its ODA. The ODA Charter, adopted in 1992, stipulated that recipients' development of weapons of mass destruction be taken into account. Japan's decision to freeze ODA grants for China reflected a change toward paying more attention to noneconomic issues. This trend toward equating aid eligibility with noneconomic concerns was first observed among the Group of Seven (G-7) countries after the Tiananmen Square incident in 1989. At that time, G-7 economic sanctions against China were motivated by the crackdown on the democracy movement there.

Since then, China's dynamic economic growth and the rapid expansion of investment from Hong Kong and Taiwan have created the perception of a "Greater China" poised to become Asia's economic superpower. The concept of "Greater China" has become the basis for the argument against development aid for China. The country's environmental damage and population explosion are, on the other hand, compelling reasons to continue aid.

After World War II, the United States provided substantial strategic foreign aid to Japan so as to mold Japan into a bulwark against communism. During the cold war, the United States competed with China as both used foreign aid as

carrot-and-stick diplomacy to distinguish their allies from their enemies. In contrast, Japan has continued to increase its ODA for economic and humanitarian purposes, and in 1989 became the biggest ODA donor as the cold war neared its end.

Japan now faces questions that did not bother China or the United States during the cold war. Unlike these countries, Japan sees its ODA mainly as mutually beneficial economic aid that establishes a good environment in recipient countries for Japanese investors. Japan can now apply this policy to its ODA for China, but it must first answer these questions: Have Japanese political leaders, since the adoption of the ODA Charter, begun to use ODA as part of carrot-and-stick diplomacy? Is Japan's traditional goal of mutual economic benefit losing importance in the case of China? If not, what programs should be adopted for improving the welfare of the Chinese people and for realizing Japan's national interest? Can democracy or human rights be main issues of Japanese ODA diplomacy? Or will Japanese ODA for China be phased out as China continues to grow into the twenty-first century? These questions must be considered so Japan and China can realize a stable and peaceful relationship in the post-cold war era.

A mature international relationship should be built on common historical recognition and mutual understanding through human networks. ODA alone cannot build a strong relationship between two countries. Japan has been inclined to depend too much on the effects of development assistance for China as a means of strengthening the bilateral relationship. To become a global civilian power, Japan must review the historical role of its ODA policy and consider new dimensions.

This chapter begins with an examination of the historical characteristics of Japanese ODA and compares them with those of the United States and China. A review of Japanese ODA for China focuses on 1979–1995. Nuclear testing by China and Japan's response are examined as background for the recent trends in Japanese ODA. Then an overview of the U.S. approach to Chinese economic development highlights the activities of U.S. philanthropic foundations. This is followed by an introduction to the relationship between the World Bank and China. Finally, the future challenges for Japanese development cooperation with China and the implications for the China-Japan-U.S. relationship are discussed.

Historical Characteristics of ODA

The United States provided more than \$2 billion in humanitarian assistance and other foreign aid to Japan after World War II. However, as tensions among the major powers increased, the United States began using its foreign aid as a tool for cold war diplomacy. In 1954, it supplied Japan with abundant weapons

and food after the signing of the U.S.-Japan Security Treaty in order to speed Japan's reconstruction and build up its military capacity. This aid was explicitly aimed at enhancing the United States' strategic relationship with Japan. Although humanistic advocates in the United States created such aid concepts as the Basic Human Need (BHN) program, most of the country's foreign aid was designed to protect the Free World by strengthening economic and military ties with allies. Accordingly, the United States provided military aid to the Chinese Nationalists until the communists took over in 1949.

Chinese aid to Third World countries appears motivated by the same cold war strategy used by the United States. Although China had to struggle to develop its own economy, it sent many engineers to build railroads and airports in various countries, including Tanzania and Cambodia. China competed against its cold war rival the United States for expanded influence in Asia, Africa, and Latin America.

Japanese foreign aid has differed historically from aid provided by China and the United States. After its defeat in World War II, Japan had to pay reparations to the Philippines, Burma (now Myanmar), Indonesia, and other Asian countries. The Japanese government lacked capital for domestic reconstruction and tried to persuade these Asian countries to supply the raw materials for machines manufactured by Japanese enterprises. Japanese leaders such as Kishi Nobusuke, prime minister from 1950 to 1952, were concerned with the economic development of Southeast Asian countries because these were export markets for Japan. This postwar situation made Japanese policymakers regard ODA as economic cooperation rather than as a tool for strategic gains. For the remainder of the 1950s through 1970, however, Japan's concerns coincided with the United States' foreign aid strategy.

Although Japan and China normalized diplomatic relations in 1972, they did not agree on Japan's economic development support for China. This became an issue for the staff of the Ministry of Foreign Affairs in Tokyo (MOFA). Fujita Kimiro, a diplomat involved in policymaking for China at the time, recalled, "In the mid-1970s, we constantly talked with our Chinese counterparts about their willingness to accept Japanese ODA."¹ China, in accordance with its philosophy of self-sufficiency, showed no interest in Japanese ODA. When Deng Xiaoping decided to open China's economy, the United States strengthened its position vis-à-vis China by supporting the communist giant's membership in the International Bank for Reconstruction and Development (known as the World Bank) and the International Monetary Fund. China became a party to these organizations in 1980.

Japan also welcomed Deng's open-door policy. In December 1979, Prime Minister Ohira Masayoshi announced Japan would provide ODA in response to the Chinese government's request. This announcement marked a new era in China-Japan relations. Japanese corporations decided to jointly build up China's

steel industry using ODA funds. China's economic development was regarded in Japan not only as a promising business opportunity but also as a form of atonement for Japan's invasion of the country during the Pacific War. China had earlier renounced war reparations from Japan. In this sense, Japan's ODA lacked the strategic character evident in American foreign aid.

Since 1979, Japanese ODA has been a symbol of bilateral friendship with China. Several Japanese prime ministers visited Beijing bringing special five-year ODA programs for China. Sino-Japanese relations can be understood from various historical perspectives, such as the cultural legacy Japan inherited from China, the geographical proximity of the two countries, or the Imperial Army's invasion of China. Surely the development cooperation between the two countries has been a distinctive factor in shaping their modern history.

In the late 1970s, the United States and other Western countries adopted an engagement strategy to encourage China to be more involved in the international economic system. Throughout the 1980s and 1990s, the United States has continued to draw China into international society, except immediately after the Tiananmen Square incident. Japanese support for China has been in accordance with the long-term strategy of the United States. Development cooperation for China in the post-cold war period should be based on this engagement strategy.

Japan's ODA for China

When Japan started providing development assistance to China in 1979, Indonesia, Thailand, and Malaysia were the main recipients of Japanese ODA. To allay fears in these countries that their aid would be cut back, Ohira, in his announcement during a trip to Beijing that year of Japan's first yen loans to China, named three principles that his country would apply to aid to China. The first was that Japan's foreign aid program would give Southeast Asian countries highest priority.² At the time, Indonesia received the largest portion of Japan's ODA. China surpassed Indonesia in 1987 to become the leading recipient of Japanese ODA in terms of net disbursement of yen loans and has remained the leader since 1993 in total funds received.

Japanese ODA consists of yen loans, grant assistance, and technical cooperation. In 1994, Japan disbursed \$1,479.0 million in ODA funds to China, which amounted to 61.7 percent of Japan's total Chinese development assistance. The other major donors were Germany, \$300.0 million; Spain, \$153.1 million; France, \$97.7 million; and Australia, \$75.6 million. Among the multinational development banks, the International Development Association, an affiliate of the World Bank, ranked at the top after providing \$671.0 million in 1994, or more than 80 percent of the total from these banks.

In 1995, ODA for China reached \$1,380.2 million, which consisted of \$992.3 million in yen loans, \$304.8 million in technical cooperation, and \$83.1 million in grant assistance. The interest rate for the yen loans was 2.3 percent; that for loans pertaining to social infrastructure, especially the environment, was 2.1 percent. The payment period was thirty years, with a grace period of ten years.

Yen loans have formed the bulk of the development assistance received by China. From 1979 to 1995, Japan disbursed \$10,665.0 million to China. Of this, yen loans accounted for \$8,897.0 million. Yen loan projects have reached 190, of which 51.2 percent are transport projects, 19.1 percent electric power and gas, 7.7 percent commodity loans, 6.3 percent agriculture, 5.8 percent telecommunications, and 9.9 percent others.

Japanese development assistance for China increased throughout the 1980s and had the following characteristics:

Equality between partners. Although Japan became China's biggest donor, both countries wanted to behave as equal partners. The partnership has not been the traditional donor-recipient or superior-inferior arrangement that has often characterized relationships between the United States and its aid recipients.

Separation of economics and politics. China needed a huge inflow of financial resources and Japan expected to benefit from China's economic growth. The magnitude of the potential mutual benefits convinced Japan to provide financial and human resources without political conditions.

Concentration on infrastructure such as railroads and bridges. While both sides' favorite projects have gradually changed, Tokyo encouraged Beijing to focus on infrastructure projects as a way of advancing its open-door policy. Beijing agreed and selected projects mainly in coastal areas.

Recognition of bureaucrats' roles. While Japanese and Chinese politicians shaped long-term policy, bureaucrats in both countries designed and managed the development of cooperation projects.

These characteristics gradually changed in the late 1980s. After the Tiananmen Square incident resulted in economic sanctions by Western countries, Japan was forced to suspend its development assistance for China. This decision overturned the separation of economics from politics and added a political aspect to Japan's ODA policy. Public sentiment and pressure from citizens' groups for the first time influenced the Japanese policymaking process. Even after Tiananmen, Japan remained supportive of China's reform effort and took every opportunity at international gatherings such as the G-7 summits to convince the developed countries, the World Bank, and the Asian Development Bank to lift their sanctions against China in the interest of incorporating its economy into the international system. When Japan became the first country to resume ODA to China, it appeared as though aid policy had reverted to the old pattern of separation of economics and politics. But such was not the case.

In the mid-1980s, when the authoritarian regime in the Philippines toppled

and a series of business scandals related to then President Ferdinand Marcos came to light, opposition parties in Japan criticized the probable connection between corruption in the Marcos regime and the lack of transparency of Japan's ODA policy. The 1990 Gulf War provoked argument about the necessity of making clear Japan's philosophy or policy guidelines so as to discourage authoritarian regimes like Iraq from increasing military budgets. The Ministry of Foreign Affairs opposed an ODA bill introduced in the Diet, fearing that its hands would be tied diplomatically should the bill become law. In June 1992, the Kaifu administration announced the ODA Charter, which linked environmental protection and the development of nuclear weapons with aid eligibility.

In this way, ODA policy became tied to political and environmental conditions, and this new trend was crystallized in Japan's decision to freeze part of its ODA to China after that country's nuclear test in 1995. The period from 1989 to 1995 marked a transition in the character of Japan's ODA.

China's Nuclear Testing and Japan's ODA Policy

China conducted an underground nuclear test in the desert on August 17, 1995, two days after the fiftieth anniversary of the end of World War II. At that time, most Japanese were commemorating the loss of family and friends in the war and remembering the difficult postwar days. They were surprised and angry about the nuclear test.

Kono Yohei, minister of foreign affairs, struggled with both conservative and liberal Diet members who wanted to freeze ODA to China in response to the incident. The test was anticipated because China had announced its intent to continue nuclear tests until the final agreement on the Comprehensive Test Ban Treaty (CTBT), which was reached in September 1996. During the negotiations on the CTBT, the issue of nuclear testing attracted wide concern in Japan. For example, after France conducted a nuclear test at its territorial island in the South Pacific, some Diet members visited the test site to protest.

While the Liberal Democratic Party (LDP) did not formally protest the nuclear tests, most LDP members were angry. The New Frontier Party, the biggest opposition party, submitted a draft resolution demanding the halt of all ODA, including yen loans, for China. The Social Democratic Party and the New Party Sakigake also strongly protested and vowed to find suitable measures to reflect their anger.

All these politicians referred to the ODA Charter, which stipulates four principles for implementing the ODA program. One of the principles, which mentions assessing a country's development and production of weapons of mass destruction when considering the extension of aid can be interpreted as referring to the development of nuclear bombs.³ After it adopted the Charter, thus

intertwining ODA policy with the nuclear issue, the Japanese government repeatedly voiced its concern whenever China conducted a nuclear test.

After close consultation with the LDP and other parties, MOFA decided to freeze grant assistance to China on August 29, 1995. The decision was a compromise between the politicians and the bureaucrats, both of whom wanted to restore calm. That evening, Kono told the media, "Despite this decision, Japan will maintain its commitment to provide yen loans for China."

Japan could not easily cancel the yen loans, having pledged to provide China with ¥81 billion in 1991–1996. Furthermore, MOFA would need a lot of time to persuade its yen-loan policymaking partners, the Ministry of International Trade and Industry (MITI), the Ministry of Finance (MOF), and the Economic Planning Agency (EPA). Unlike the multiyear commitment of yen loans, MOFA determined grant assistance annually. The grant amount was considerably smaller than that of the yen loans, only ¥7 billion to ¥10 billion per year.

Despite Japan's decision to halt the grant portion of ODA, China continued to regard nuclear strategy and testing as the core of its defense policy. Ultimately, though, international pressure during the CTBT negotiations forced China to review its nuclear policy. On July 29, 1996, after conducting its forty-fifth nuclear test, the Chinese government announced it would stop testing.

China's change of policy allowed the Japanese government to consider the resumption of grants. The situation, however, worsened as other sensitive issues such as Taiwan and the Senkaku Islands blocked resumption. Politicians, particularly conservative members of the LDP, strongly resisted restarting the grants. As these issues became tangled together, political problems overshadowed development cooperation between Japan and China.

MOFA bureaucrats appeared paralyzed and unable to handle these issues. While Prime Minister Hashimoto Ryutaro pressed the other G-7 members to approve China's membership in the World Trade Organization (WTO), at home he could do nothing but wait for the politicians' anger to subside. Whenever the LDP's foreign affairs committee met, the voices of anti-China members criticizing MOFA for its ambiguous stance toward China were the loudest; pro-China politicians tended to refrain from voicing an opinion.

Internal political disputes are sometimes resolved by external circumstances. The foreign ministers of Japan and China were supposed to meet during the Asia Pacific Economic Cooperation (APEC) forum gathering in the Philippines in November 1996. Although MOFA tried to get approval to resume grants to China before APEC convened, the ruling LDP only agreed to send experts for the 1997 yen loan program. The planned dispatch of experts had been stalled since the summer of 1995. While MOFA had not admitted that the yen loans were in all practicality frozen because of the stalled dispatch of experts, it tried to play up the LDP's decision as a big step. One high-ranking official said,

"Today's decision is an important step toward improving the relationship between Japan and China."

It took nearly three months to normalize the bilateral relationship. At his New Year's press conference in 1997, Prime Minister Hashimoto stressed the importance of the year as the twentieth anniversary of the signing of the treaty for friendship and cooperation between Japan and China. Public concern in Japan at that time, however, had shifted from China to the hostage crisis at the Japanese Embassy in Peru and then to the famine in the Democratic People's Republic of Korea.

On February 13, 1997, one day before a scheduled meeting of the Japanese and Chinese foreign ministers in Singapore in conjunction with the Asia-Europe Meeting (ASEM), Hatakenaka Atushi, executive director of the Economic Cooperation Bureau of MOFA, attended a meeting of the special committee for external economic cooperation, one of the ODA-related committees in the LDP. Hatakenaka had tried to appease fellow politicians on the China issue since 1995. From his point of view, ODA was important for sustaining China's economic growth and open-door policy. Stubborn LDP politicians continued to cite the ODA Charter as one reason for their reluctance to support the pro-China policy of MOFA. This time, however, the LDP committee finally approved the resumption of grant assistance for China.

On February 14, 1997, when Japanese officials met their Chinese counterparts in Singapore and explained the decision to resume grants, journalists neglected this news and focused on the reports of a high-level government official who defected from North Korea.

New Trends in Japanese ODA Policy

The general characteristics of Japan's ODA policy probably cannot be wholly discerned from the Chinese nuclear testing issue. Now that China has discontinued its nuclear tests, the two countries are unlikely to confront a similar situation again. But the process of overcoming the impasse did clarify some new policy trends.

The first is the politicization of ODA policymaking. Historically, development assistance in other countries has had political overtones. In contrast, Japan has tried to avoid tying politics to development assistance for China. China's nuclear testing and the ODA Charter turned Japan's development assistance into a political dispute. Although Japanese bureaucrats tried to calm tempers, some politicians made the ruling LDP brandish ODA as a stick against China.

This situation becomes clearer when we compare the nuclear testing issue with the Tiananmen Square incident. When Japan decided to freeze its ODA for China, most politicians did not link ODA with the abuses in Tiananmen

Square. Politicians in Western countries first raised the issue of economic sanctions against China in retaliation for its military brutality, but in Japan bureaucrats dealt with this issue. As G-7 countries and international financial institutions argued for a coordinated response against China, Japanese government officials, including those at the Ministry of Finance, worked hard to adjust to the external situation.

China's nuclear testing, however, caused little concern among Western countries. Thus, the issue was contained within the Japan-China bilateral framework and allowed nationalistic Japanese politicians to lead the protest. They linked ODA with other political incidents of the moment and doubted the necessity for providing development assistance to an economic and military power. Government officials in Japan actually lost their motivation to resolve the problems. The most they could accomplish was to make the politicians consider the resumption of ODA when bilateral meetings were scheduled at multinational conferences such as APEC and ASEM.

The second trend is the emergence of nationalistic sentiment. Although a series of events similar to those in 1996 might not occur again, Japan was clearly annoyed at China. Nationalistic sentiment also seemed to prevail in China. A book titled *A China That Can Say No* and similar books became best-sellers in the same year.

These problems had been foreseen at the annual consultations between the two countries on ODA. At negotiations in 1994 for the fourth yen loan program to begin in fiscal 1996, the Japanese government had expressed interest in providing aid for China's social infrastructure and environmental problems, but there was no domestic support for a five-to-six-year commitment of ODA. Government officials explained that domestic fiscal constraints prevented them from committing long-term assistance only for China. Actually, though, some bureaucrats worried that making a long-term commitment would deprive Japan of an effective diplomatic card—ODA—that would give it some leverage in future Sino-Japanese relations. Finally, Japan agreed to support projects only for the three years 1996 through fiscal 1998. The remaining two years (1998–1999) will be determined later.

The third trend is the difficulty in measuring the effectiveness of Japan's ODA policy. Some observers say the ODA Charter has proven effective because China agreed to stop its nuclear testing after Japan froze its ODA. One can argue, however, that international pressure on China during the CTBT negotiations forced it to stop all nuclear tests. While high-ranking Chinese leaders such as Prime Minister Li Pin criticized Japan's ODA policy, it is difficult to identify the factors behind the Chinese decision to halt the tests. In fairness, most Japanese politicians, and even the bureaucrats, were not concerned about the linkage between ODA policy and the outcome of the policy. Even though a bilateral forum for discussing security issues exists, Japanese policymakers did not try to

start a dialogue with China about its nuclear tests. They only reacted to the situation, rather than acting to influence it.

This issue of whether ODA is effective also raises a question about the need for traditional development assistance for China. In the course of the nuclear debate, Japanese conservatives began to suspect the effectiveness of ODA-related projects and called for a reduction of the ODA budget. Economic growth in China's coastal areas cast doubt on the legitimacy of ODA in the late 1980s. People worldwide now tend to see China as becoming a military and economic power in the twenty-first century. It is therefore more difficult for Japan to justify substantial financial assistance for the same kind of infrastructure projects as it has supported in the past.

Japanese have begun to recognize the threat from such transnational issues as the population explosion, environmental degradation, and shortages of energy and food. For its fourth yen loan program, Japan selected projects that stressed environmental protection and development of China's hinterland.

U.S. Development Strategy for China

While the Japanese government regards development assistance for China as a main measure for promoting the bilateral relationship, the U.S. government has never shown a similar policy toward the present Chinese government. Because the Foreign Aid Act prevents the U.S. government from providing development assistance to communist countries, USAID has no official program in China except humanitarian assistance after natural disasters. The U.S. Environmental Protection Agency, however, provided technical assistance for manufacturing refrigerators in the late 1980s. This program, which was aimed at reducing emissions that damage the ozone layer, was terminated by the U.S. government because of a lack of funds. Other U.S. government agencies have implemented several programs, such as scholarships for students and cultural exchanges, in cooperation with private nonprofit organizations (NPOs).

These American NPOs, which include philanthropic foundations, think tanks, and project-oriented nongovernmental organizations (NGOs), have been active in China since the nineteenth century. Most of the NGOs have worked at the grass-roots level apparently motivated by missionary zeal. Some NPOs such as the Ford Foundation and the Asia Foundation have independently supported Chinese development and welfare.

The Ford Foundation has been involved in China since the 1950s. During 1952–1979, the Ford Foundation invested more than \$40 million to enhance understanding of China in the United States and in developing countries. The foundation also funded centers of Chinese studies at major U.S. universities, for national collections of Chinese-language library materials. After the

normalization of U.S.-China diplomatic relations, the Ford Foundation began a direct support program for academic and professional exchanges. The main participants were the Chinese Academy of Social Sciences and the Chinese Academy of Agricultural Sciences. During the 1980s, collaboration in China was broadened beyond these two academies to include universities and State Council and Ministry research institutes.

In January 1988, the Ford Foundation opened an office in Beijing and expanded its programs in economics, law, and international affairs. It decided not to freeze its programs after the Tiananmen Square incident when Western countries and Japan jointly imposed economic sanctions against China.

Programs in rural poverty and resources management as well as reproductive health were added in 1989–1990 in response to chronic poverty and persistent reproductive health problems. From January 1988 until September 1995, the Ford Foundation made grants totaling about \$50 million. At present, its efforts are mainly in four areas: rural poverty and resources; reproductive health; economic reform and its social consequences; and law, rights, and governance (Ford Foundation).

The Ford Foundation's activities have been widely accepted in China, particularly among Chinese intellectuals. Its long and stable commitment to Chinese academics deepened personal relationships among academics and broadened Westerners' knowledge of China. The Beijing office, located in the center of the city, enabled the foundation to enhance its contacts with governmental and grass-roots organizations, observe Chinese society, and encourage gradual social change.

The U.S. government has sought to encourage China to further open its economy and become a responsible member of the international community. China's market potential has become more attractive to big businesses. While the United States urges China to develop a market-driven economy and the two sometimes engage in serious trade disputes, at the same time the United States has sought to draw China closer to the international economic system through such multilateral approaches as APEC. APEC, at its ministerial meeting in Seoul in 1991, welcomed delegations from new members China, Taiwan, and Hong Kong. And at the 1993 APEC gathering in Seattle, U.S. President Bill Clinton held the first economic talks with Chinese President Jiang Zemin, in which they discussed ways to build an Asia Pacific community. Whereas Japanese diplomacy tends to rely on the country's economic power, APEC exemplifies the effectiveness of a capacity for diplomacy by its members' leaders and for setting an agenda, both of which Japan lacks.

The World Bank and China

The World Bank has played a key role in persuading Japan and other countries to provide financial assistance for China. China's negotiations with the World Bank and the IMF were initiated by Deng Xiaoping in the late 1970s. The United States has guided the World Bank as a main architect of the institutions that evolved from the United Nations Monetary and Financial Conference at Bretton Woods, New Hampshire, in July 1944. Japan, the second biggest financial contributor to the World Bank, has also encouraged the bank to support China. As a result, the World Bank and the IMF granted membership to China in 1980.

The World Bank increased its operations in China until 1989 when the U.S. government pressured the bank to stop its Chinese operations after the Tiananmen Square incident. Japan hesitated to follow the United States' lead. Since the bank resumed its Chinese activities in the early 1990s, its lending has rapidly increased. By 1992, China had become the biggest recipient of the World Bank's lending, followed by India, Indonesia, and Mexico.

According to the bank, China has shown the capability to implement bank-sponsored projects. The Chinese government has managed the projects well, from project selection to implementation and payment.

Recently, the United States has questioned the legitimacy of the bank's lending to China. The U.S. Congress has begun to doubt the effectiveness of the lending, citing the inefficiency of the bank's operations. Americans' perception of China's economic success and concern about their own government's budgetary constraints have also amplified suspicions of the bank's operations. In particular, the Chinese operations of the bank's soft-loan subsidiary, the International Development Association (IDA), aroused strong Congressional opposition in the summer of 1996.

The IDA, the so-called soft loan window of the World Bank, lends to the poorest countries. As part of the fiscal 1996 budget, the Clinton administration asked Congress to approve \$1.37 billion as the final installment of the U.S. government's third payment to IDA. This figure accounted for about half the total budget requested for multilateral aid. In the United States' tight budget situation, competition for funding became so intense that Congress responded negatively to the IDA payment. U.S. politicians criticized the World Bank as having a limited impact, supporting undesirable countries, placing too little emphasis on the needs of the poor, and being insensitive to the environmental consequences of its programs. They pointed out that the bank projected China's gross domestic product would surpass that of the United States early in the twenty-first century. The human rights issue was another concern of the U.S. Congress. The House of Representatives and the Senate decided to set the funding for IDA at around \$700 million, slightly more than half the proposed amount.

This raised questions about U.S. leadership and participation in upcoming negotiations on the IDA budget (Nowels 1996). It has been argued that China should lose its IDA recipient status in 1998. While Japan opposes this idea, the United States supports it. From the U.S. viewpoint, China should graduate from the IDA because of its economic strength.

Future Challenges

It was not a coincidence that Japan started its development assistance for China after China introduced a more open reform policy in 1979 under the leadership of Deng Xiaoping. During his era, development assistance was a linchpin for enhancing the relationship between China and Japan. Ironically, when Deng chose Jiang Zemin as his successor in 1989, political factors became involved in shaping development assistance policy. Although an open-door policy will be the only way to satisfy the Chinese people who are enjoying some economic benefits, Deng's death on February 19, 1997, raised uncertainty about future cooperation.

Of the future challenges for Japan, the first is to cultivate a new perception toward China. A Japanese government poll on China in October 1996 showed that more than half (51 percent) of the respondents answered, "I don't feel familiar with China." While around 70 percent felt some familiarity with China up to 1988, the figure dropped to 52 percent in 1989 and to 49 percent in 1996 (*Asahi Shimbun* 23 February 1997). These figures represent not only the bitter experiences of 1995–1996 but also the powerlessness of ODA to foster friendship between the two nations.

A better understanding of China might strongly shape Japan's ODA policy. When Japanese politicians showed their reluctance to provide development assistance for China, this reluctance reflected the Japanese people's dissatisfaction toward China in 1996. The existence of chronic poverty in China's hinterland even as the economic performance of coastal regions and the country's overall export performance are growing rapidly has raised doubts about the need for conventional development assistance.

Japan's second challenge is its fiscal situation. The ODA budget and the defense budget were regarded as sacred areas in the 1980s and were not reduced by MOF's screening process. Prime Minister Hashimoto, however, ordered a streamlining of all budget items, including ODA, in December 1996 to balance the budget until the twenty-first century. As a result, Japan's ODA budget for fiscal 1997 increased only 2.6 percent, the lowest rise ever.

Calls are being heard about reforming the special fiscal and investment accounts that are the major supply of funds for yen loans. Spurred by an anti-China sentiment, Japanese conservatives claimed ODA for China was not effective and demanded a reduction (Komori 1976).

The government decided in 1994 to merge the Overseas Economic Cooperation Fund (OECF), which implemented the yen loan projects, with the Japanese Export and Import Bank (EXIM Bank). While the OECF loans nearly ¥20 billion annually to China as ODA, the EXIM Bank lends more than ¥20 billion at low interest rates. Although the OECF operates under the ODA Charter, the EXIM Bank is free from such rigid principles. The EXIM Bank was therefore able to provide a preliminary export credit for the bidding by Japanese enterprises for the Three Gorges Dam project on the Yangtze River, potentially the world's largest hydroelectric dam. The full impact of the OECF-EXIM Bank merger is still unclear.

As for China, the gap between its status as a developing country and the worldwide perception of it as a rising economic power is a hindrance. While China has long performed an important political role as a permanent member of the UN Security Council, it has grown rapidly economically for the past two decades. As a result of China's growth and pressure from the United States, the IDA has considered terminating its financial aid for China until 1998. As direct private investment has increased, the share of ODA from Japan as well as multilateral assistance has been decreasing. China's foreign reserves surpassed a \$100 billion in October 1996.

True, parts of China are still struggling to overcome poverty and lack sufficient financial resources for public works projects. China stresses this difficult economic situation in negotiations with the WTO and APEC. While Japan has already shifted the focus of its ODA programs for China from economic infrastructure in the coastal regions to social infrastructure for the hinterland, Japan will gradually have more difficulty finding projects supported by Japanese people and policymakers. The MOFA is considering environmental programs, which would appeal to people throughout Japan.

Several sensitive issues still separate Japan and China, such as recognition of war crimes, territorial disputes, and chemical contamination. Among these issues, war reparations have overshadowed ODA policy. China relinquished its claims to reparations in 1972 when it normalized relations with Japan. However, when Japan protested China's nuclear testing, some Chinese politicians echoed the general perception that Japan's ODA is a form of war reparations. Nationalistic sentiment amplifies this and may cause another mutual perception gap.

From the Chinese perspective, an academic suggested that to alleviate the complex feelings between the two countries Japan should consider providing huge financial grants to China. These grants would be the last of Japan's development assistance to China and would put an end to the reparations issue. He argued that both countries could then make a fresh start in the twenty-first century.

Currently, the fourth five-year yen loan program for China has been in place since fiscal 1996, and assistance in the first three years totals ¥58 billion. The

Japanese government will discuss the remaining two years in fiscal 1998. MOFA officials are now paying more attention to environmental projects that can be expected to earn public support; they show little interest in programs that would start at the beginning of twenty-first century.

Conclusion

Japan's development assistance for China has been expected to enhance the friendship between the two countries. However, in view of events in the mid-1990s, such has not been the case.

Inevitably, Japanese ODA policy has taken on a new political dimension, which reflects the adoption of the ODA Charter. More important, the Japanese people have become more concerned about social values such as a good environment, a democratic system, and a peaceful civilized society. The increase of environmental programs funded by Japanese ODA reflects this concern.

The Chinese government appears to understand these desires of the Japanese people. China has focused on environmental programs in the first three years of the present five-year ODA program. This exemplifies positive interaction and mutual understanding between the two countries.

The social and economic changes in China and Japan, however, require Japan to seek a more sophisticated approach to realizing its people's desires through its ODA. Cold war era strategic foreign aid cannot work between Japan and China. Even if Japan dared to use its ODA as a diplomatic stick, nobody expects a big country such as China to take orders from a smaller neighbor.

Instead of orders, close consultations and dialogue should be the basis of bilateral relations. In this sense, Japan and China must gain deep knowledge about each other's politics, economics, and culture. To enhance mutual understanding and personal contact, various exchange programs that include students, academics, and future leaders should be expanded using ODA. The economic significance of ODA will decrease in the twenty-first century because of an increase in private trade and investment. ODA, however, should underpin relations between Japan and China.

New players working for development cooperation have emerged, and these players have contributed to the increase of contacts between Japan and China at the grass-roots level. Notably, China has increased its contacts with multinational organizations, local governments, and international NPOs. While the Chinese government of its own accord began to be more involved in the work of new multinational organizations such as APEC and the Asian Development Bank, China's contacts with local governments and international NPOs were initiated mainly from the Japanese side. In general, these contacts were welcomed in China.

Many local governments in Japan have built upon their experiences through exchange programs with their Chinese counterparts to expand programs into development cooperation. Kita-Kyushu City in western Japan, for example, has worked on air and water pollution with Dairen, a Chinese coastal city. The local government of Hiroshima Prefecture began a joint project with Shichan Province to tackle air pollution. The shift from exchange to cooperation symbolizes deepening interaction at the grass-roots level between the two countries.

Japanese NPOs have also become interested in programs with Chinese counterparts. In February 1997, GAP (Group Action Planning for International Philanthropy) held an international meeting attended by many NPOs from Southeast Asia and China. These Chinese NPOs have worked on environmental issues, women's rights, and international exchanges. These contacts can strengthen mutual understanding and create an authentic friendship and cooperation in the twenty-first century.

Endnotes

1. Personal interview with Fujita Kimiro, governor of the Japan International Cooperation Agency, October 1996.
2. The two other principles were that Japan would not dominate the Chinese market and would coordinate aid to China with Western countries and that Japan would never provide military assistance to China. See Ro (1996, 103).
3. The three other principles stipulate that development should be pursued in tandem with environmental conservation; that ODA should not be used for military purposes; and that efforts in the recipient country to promote democratization, introduce a market-oriented economy, and protect basic human rights be assessed.

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