

Japan's ODA at a Crossroads: Striving for a New Vision

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Japanese foreign aid policy is at a crossroads. First, a decade of prolonged economic recession has forced the government to cut Japan's foreign aid budget (Official Development Assistance, or ODA) – once regarded as sacred – by 0.2 percent in FY2000, 3.0 percent in FY2001, 10.3 percent in FY2002, and 5.8 percent in FY2003, in yen terms. For the first time in ten years, the US replaced Japan as top donor in 2001. Stark budget realities are requiring Japan to strategically prioritize its aid in order to maintain ODA's effectiveness.

Second, Japan does not wholly accept the mainstream thinking by Western aid community¹ about development. Japan continues to believe that East Asian development experience, which is widely regarded as a "success story," and to which Japan itself made significant contribution through aid, trade and investment, has also been a good model.

Moreover, the September 11 tragedy prompted a major shift in the Bush Administration's foreign policy and also strongly affected the thinking of the entire aid community – poverty alleviation through foreign aid is now considered to be another tool in fighting terrorism. As a direct result, the US and the EU

aspire to boost aid to levels² unimaginable just two years ago.

Budgetary pressures at home and shifting motivations for increased foreign aid by other countries have created a sense of urgency in Japanese development experts and officials. Some innovative efforts, both within and outside the government, have emerged in a means to move away from the traditional reactive mode and to project Japan's own ideas more strongly in the global arena.

Global Development Trends

Current thinking in the global development community has four major features, with which Japan feels considerable unease.

- The combination of a drive to reduce poverty and a neo-liberal economic framework – under this regime, public actions are justified only in direct pro-poor targeting and/or macro-economic management. Consequently, the contents of the growth strategies, including industrial promotion and infrastructure development, are often superficially treated or simply ignored.
- Re-direction of ODA to the poorest countries, assuming that middle-income countries

have access to private capital and thus do not need ODA.

- An increase in grant components and the reduction of concessional loans.
- Aid harmonization in favor of non-project aid and pooled funding, and the marginalization of project aid.

Strategic convergence rather than diversity is epitomized in the two currently dominant aid policies: the Poverty Reduction Strategy Paper (PRSP) initiated by the World Bank in late 1999 and the United Nations Development Goals adopted in 2001. Both regard poverty reduction as the ultimate goal of development and contend that aid must be evaluated mainly by the contribution to this goal.

Furthermore, it is argued that the polarization of developing countries where some countries perform well and others remain stagnant—some even call it the "Africanization of global poverty"³—provides a strong case for concentrating ODA on the poorest countries, particularly those in Sub-Saharan Africa, with increased grant components with no obligation to repay⁴. Since many Sub-Saharan African countries are highly aid-dependent under the proliferation of donors and projects, there is a call for reducing "transaction costs"

associated with multiplicity of aid to lift administrative burdens from recipient countries⁵. Now, donors are encouraged to harmonize or even completely unify their aid disbursement procedures.

Indeed, the UK has announced its intention to phase out specific project aid in favor of budget support and common basket funding. These initiatives are a European reaction to the disappointing records of African development in the past and the latest desperate attempt to meet the African challenge.

Japan's Development Vision

By sharp contrast, the East Asian development experience strongly affects the Japanese approach to development aid. Japan's ODA intends to support the industrialization of latecomer countries and has the following features:

- Geographical concentration in Asia [Figure 1]
- High priority on infrastructure development [Figure 2]
- A broad aid menu, including loans [Figure 3]

FIGURE 1 TOP 5 DONORS: REGIONAL DISTRIBUTION OF ODA 2000-2001

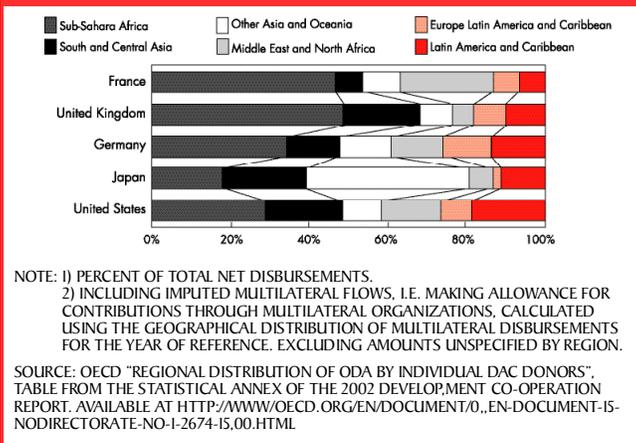


FIGURE 2 TOP 5 DONORS: SECTORAL SPENDING 2000-2001

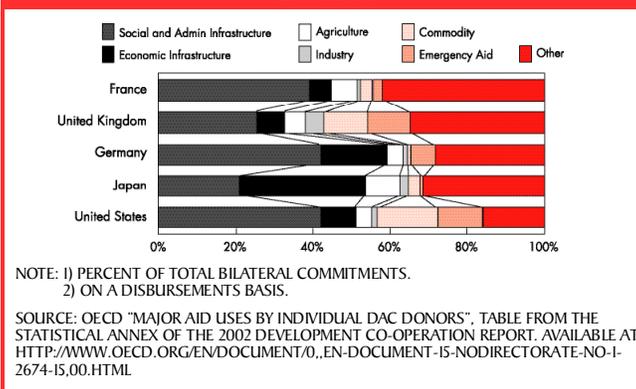
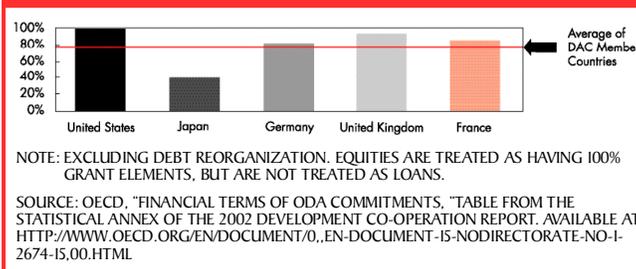


FIGURE 3 TOP 5 DONORS: GRANT SHARE OF BILATERAL ODA 2000-2001 AVERAGE



Two historic factors make Japan's aid and development vision quite distinctive from those of other donors. First, Japan is the only non-

Western donor with a history of early and successful industrialization. Furthermore, many Japanese personally experienced the post-WWII destruction and poverty that were gradually overcome by hard work. Japan's success in strengthening its manufacturing base contributed in turn to the trade-and investment-driven development and poverty reduction in the rest of East Asia.

Second, Japan's postwar decision to abandon military force pushed ODA to play a special role in diplomacy. Indeed, ODA has been the principal means by which Japan contributed to globally shared goals and addressed specific external needs, such as war reparation payment in the 1950s, trade promotion in the 1960s, securing imported energy and raw materials in the 1970s, and the "recycling" of the trade surplus in the 1980s.

These factors heavily influence the way development visions are

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shaped and the kind of relationship that Japan wishes to foster with developing countries through aid. Japan embraces the following latecomer perspectives that are unlikely to emerge from the West.

- *Self-help effort (ownership) and growth aspiration:* Aid is neither charity nor the moral obligation of the rich. Aid should support self-help efforts of developing countries and contribute to fostering their national pride, even if it means the recipient could overtake the donor country in the long run.
- *Real-sector concern:* In the early stages of development, government should take an active role in promoting and even creating a market economy. Greater attention should be given to the dynamic contents of the real economy such as key industries, investment and competitiveness, rather than frameworks.
- *Long-term perspective:* Development is a long-term, path-dependent undertaking. It is thus necessary to consider the history, society and culture of a country in designing its unique strategy.
- *A flexible and pragmatic approach:* While accepting general principles, each

country should interpret and adapt them to the local context. Diversity, not rigid rules and conditions, should be permitted and encouraged in both aid strategy and delivery.

By contrast, the Western countries and international organizations often prefer farsighted frameworks, convergence toward a single system, and emphasis on macroeconomic and financial issues⁶.

Japan is also unique in offering a relatively large share of loans in bilateral aid. Because loan aid can mobilize larger resources (e.g., for financing large-scale infrastructure projects or supporting reforms), it can be very effective in promoting broad-based growth if combined with a good growth strategy. At the same time, loan aid requires discipline on the recipient side including strong ownership and debt management capacity, and donor responsibility for ensuring project sustainability. The time scope of the recipient-donor relationship under loan aid is much longer than grant aid and goes far beyond project completion to the last repayment. In this sense, each party assumes shared responsibility in the long run.

Aid harmonization should be promoted whenever feasible and effective. But we must proceed with a sense of realism and careful identification of country-specific

bottlenecks of exactly where aid fails. A broad range of options for improvement should be considered, because the "transaction cost" is just one factor among many. Other factors, such as the quality and contents of development strategy, institutional capacity of recipient countries and the degree of aid dependency, may play a bigger role. Moreover, appropriate matching of aid modalities with sector conditions and intervention type is necessary. The thrust of successful aid policies should be aimed at self-sustained development and not the permanent aid dependency of recipient countries, with an eventual graduation from aid.

Suggested Actions

As a non-Western industrialized country, Japan should bring diversity and the latecomer perspective to the global development debate and aid practice. Japanese development experts and officials should:

- Take initiative in designing and implementing a good growth strategy by conducting country-specific in-depth industrial studies and engaging various development partners. The ongoing intellectual ODA to Vietnam and Laos are good examples – they provide policy advice on the overall strategy for marketization, from a long-term perspective. For latecomer

countries in Asia, it is particularly important to offer concrete industry-specific policy advice, not just general counsel, taking account of intense integration pressure. To this end, Japan should continue to offer a right mix of aid menu (loans, grants, and technical assistance) tailored to each country.

- Compile and widely disseminate the East Asian development experience, so that it can be understood by policymakers and researchers in both developing and advanced countries. To maximize policy impact, a sophisticated dissemination strategy is needed for each targeted audience.
- Bring pragmatism and flexibility into the discussion on aid harmonization. Introduce Asian experiences in order to add variety and country context to the current debate, which is too narrowly focused on African

experiences. At the same time, Japan should also reform its own aid procedures where necessary.

- In policy-making, strengthen strategic coordination in Tokyo by regular consultation among various ministries charged with ODA (especially the Ministry of Foreign Affairs, the Ministry of Economy, Trade, and Industry, and the Ministry of Finance) and the two key executing agencies (JICA and JBIC). Delegate decision-making to the country team in the field (Embassy of Japan, JICA, JBIC, and JETRO as appropriate). The country team should be made fully responsible for conducting policy dialogue and partnership activities.

These actions may require a fundamental reform in the current ODA system, which is politically sensitive and are likely to take time. But I am not too pessimistic. Under a shared strategic vision, it is pos-

sible and quite effective to build intellectual networks among Japanese policy makers, aid practitioners, academics, NGOs, and other shareholders. Websites and email propel ideas across geographical and institutional boundaries and be transformed into policy-oriented actions. Such activities have already begun by the GRIPS Development Forum and the Washington DC Development Forum, as well as by country teams in Vietnam and Bangladesh. Hopefully through these interactions, good practice from the Japanese perspective can be widely shared and disseminated, and impact global development strategy. ■

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¹This includes the World Bank and the UNDP at the international level, and at the level of individual countries, the members of the Anglo-Saxon camp with the US and the UK in the lead, and the Nordic group of donor countries.

²For example, the US has said it will add \$5 billion annually during the next three years for the benefit of poor countries with "good practices." To this end, the "Millennium Challenging Account" is to be established to provide performance-based grants to eligible countries.

³World Bank, *African Poverty at the Millennium: Causes, Complexities, and Challenges*, 2001.

⁴In the IDA 13 replenishment negotiations, the US strongly insisted on a drastic increase in grant components of IDA's concessional funding to low-income countries. After a long negotiation, it was finally agreed to raise the grant components to 18-21%, with particular emphasis on post-conflict assistance, natural disaster relief and coping with HIV/AIDS.

⁵In the mid-1990s, Tanzania had 40 donors implementing 2000 projects without coordination.

⁶For different views on poverty, market and integration, see Izumi Ohno and Kenichi Ohno (2002), "Global Development Strategy and Japan's ODA Policy," GRIPS Development Forum Discussion Paper No. 1.