PARTNERSHIP FOR QUALITY INFRASTRUCTURE: DEVELOPMENTALISM OR NEW LIBERAL ORDER?[1]

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Infrastructure export and investment has become a prominent feature of geoeconomic competition between Japan and China, particularly since 2013. This was the year when China—under the newly emerging leader Xi Jinping—announced the Belt and Road Initiative (BRI), and in response, the newly elected Japanese Prime Minister Abe Shinzo launched the Japan Revitalization Strategy, which included a rapid increase in overseas infrastructure investment. In 2015, as the Chinese-proposed Asian Infrastructure Investment Bank (AIIB) was founded with US$100B in initial capital, the Abe administration responded by unveiling the Partnership for Quality Infrastructure (PQI) initiative in collaboration with the Asian Development Bank (ADB) to expand high-quality infrastructure investment in Asia. One can also see the intense competition on the ground between these two capital-rich powers of Asia, such as in the case of the high-speed rail bidding in Indonesia and Malaysia in the last several years.[2] Due to the vast infrastructure investment needs, particularly in developing Asia, and based on the changes in the global consensus in favour of infrastructure that contributes to economic development, Japan and China proactively use their infrastructure investment in the Indo-Pacific region to enhance their respective economic leadership.[3]

Quality Infrastructure or Resurgence of the State-Led Aid Model?

Corresponding with these competitive dynamics, the Japanese government's infrastructure investment strategy has attracted policy and scholarly attention. There have been two contrasting analyses. On the one hand, the Japanese government has promoted the PQI initiative as a way to distinguish the Japanese infrastructure investment approach from the method implemented by the Chinese. The PQI aims not only to increase the amount of investment in needed physical infrastructure—from transportation to water management and energy—but it also takes into account many quality factors, such as high technical expertise, environmental and social impacts, quality of construction (including safety and reliability), life-cycle cost, and debt sustainability. Following this line of differentiation, the Japanese government has been active in promoting the high-quality standards globally through the "Principles for Promoting Quality Infrastructure Investment" at the G7 Ise-Shima Summit in 2016 and G20 Osaka Summit in 2019.

On the other hand, the Japanese government's emphasis on infrastructure exports as a way to stimulate the country's own economy and the use of public funds in collaboration with the country's private sector (in "all Japan" fashion) conjures up the resurgence of Japan's old-style foreign aid and development model, which many thought that the Japanese government had abandoned in the early 1990s.[4] Based on this perspective, the Japanese government has returned to its old developmentalist roots, hence atavism, to re-energize Japan's infrastructure exports around the developing world. This was indeed a strategy once used by the Japanese government to expand the country's access to natural resources and create the foundation for Japanese business expansion, particularly throughout East Asia.[5]

As we observe such a Janus-faced infrastructure investment strategy adopted by the Japanese government, we ask how these contrasting approaches coexist. Is Japan's foreign economic policy heading to support higher standards, rule-making, and liberal economic order, or is it retracting back to "embedded mercantilism" in favour of domestic economic growth?[6] It is essential to examine both the regional geoeconomic context and the recent domestic institutional evolution within Japan to shed light on these questions.

Regional Sources of Japan's Infrastructure Push

On the regional front, there is no doubt that the pressure from China's Going Global strategy, particularly in the form of a vast outward investment push, has put significant pressure on Japan. Having been hit quite severely by the global financial crisis (GFC) in the late 2000s, the Japanese government was already turning to an infrastructure export initiative as a source of economic stimulus. Competition with China, particularly under the Abe administration (December 2012 to present), has reinforced the government's commitment to this strategy. Since the Japanese projects tend to be of much higher costs, the Japanese government has to highlight the "quality," higher standards, and sustainability. Notwithstanding, such a strategy has created a convenient contrast of the Japanese infrastructure investment approach against the Chinese, whose recent rapid expansion has alarmed its neighbours with concerns ranging from massive inflows of Chinese workers to so-called "debt trap diplomacy."[7]

At the same time, the Japanese "high standard" and "liberal economic" strategy is to influence the regional economic order to create a level playing field, not only against China but also vis-à-vis the recipient or host governments, which have increased their demands to have more control over incoming investments. Having to follow the rules and peer pressures of the traditional Western aid donors as a member of the OECD Development Assistance Committee (DAC) since the 1960s, the Japanese government has long been constrained by global foreign aid norms. As an advanced economy and with a large, globalized business sector (as discussed below), placing these standards has become one of the government's geoeconomic instruments in the region.[8] The post-GFC shift in economic development governance in favour of infrastructure investment has also provided Japan an opportunity to combine its emphasis on infrastructure investment with the traditional Western donors' accountability norms. Furthermore, the Japanese government has had its share of bad experiences of failed projects as its foreign aid concentrated on physical infrastructure and subsidized Japanese construction firms and contractors via tied aid. As such, it is aware of the risks and danger associated with these kinds of projects. Despite the claim of a self-help philosophy of Japanese foreign aid, there are abundant episodes of borrower governments' having to reschedule their yen loan repayments.[9] Such is a possible scenario that awaits China in the near future. By influencing global and regional debate on infrastructure investment, the Japanese strategy hopes to tip China's domestic political scale in support of a more cautious and quality-pursuing approach.

Japan's high-quality infrastructure investment strategy is also consistent with the Free and Open Indo-Pacific (FOIP) framework, where liberal norms are the common feature of the alignment among countries such as the United States, India, Australia, and Japan. With the emphasis on connectivity, transparent rules, and high standards, infrastructure investment is becoming an important economic piece of the FOIP strategy.[10]

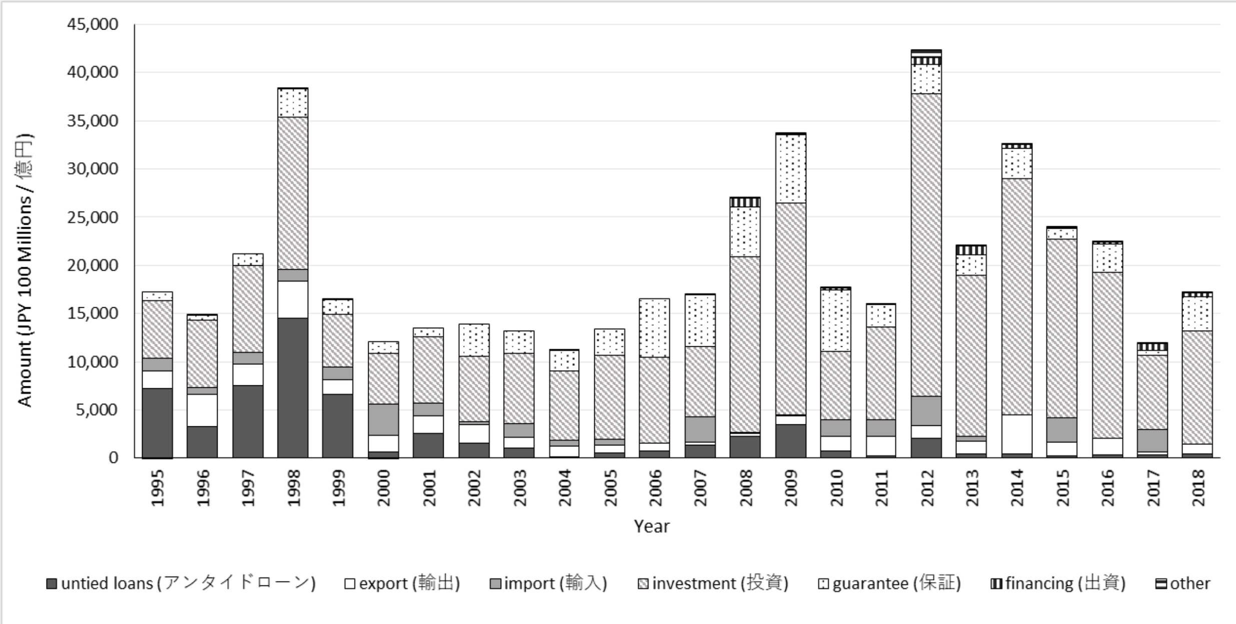
Domestic Sources of Japan's Infrastructure Investment Strategy

It is Japan's domestic political and institutional context, however, that heavily shaped the Japanese government's infrastructure investment strategy in Asia even before the onset of competition with China. After the collapse of Japan's bubble economy in the early 1990s, and facing the demographic challenge of a declining population since the early 2000s, Japanese construction companies began to increase their outward investment in the first decade of the 21st century.[11] However, the expansion has been constrained by its high cost under a strong yen, increasing competition from countries such as South Korea, Taiwan, and later China and India, and OECD/DAC norms. The Japanese government has also faced fiscal challenges.

To overcome such challenges, Japan's Ministry of Economy, Trade and Investment (METI) proactively adopted the public-private partnership (PPP) modality to Asia's infrastructure development starting in 2005. METI defines PPP as "the division of labor between the public and private in infrastructure building and administrative services, as the two entities share adequate cost and risk." Therefore, the Japanese government began to promote a "Japan package" modality where the Japanese government would engage in planning with aid recipient governments to provide a package-type aid (with increased tied aid), which included everything from identifying possible infrastructure projects and public and private financing, to construction and maintenance.[12] In 2011, the 1999 Act on Promotion of Private Finance Initiatives (PFI) was revised to increase the coverage of PFI projects and financial use of private capital to improve public infrastructure. Despite the severe fiscal condition of the Japanese government, the competition with China also drove the Japanese government to enhance funding support to Japan's infrastructure exports. In the context of the 2016 "Expanded PQI" initiative, the Abe administration promised US$200B in overseas infrastructure financing in the next five years.

The Japan Bank for International Cooperation (JBIC) has played an important role in financing trade and investment overseas at non-concessional terms. Figure 1 demonstrates the phasing out of untied loans by the JBIC since 1999. With the exception of 2009, the JBIC has hardly provided any untied loans since then. Meanwhile, there is a visible increase in the proportion of its loans in support of infrastructure investment.

Figure 1. Types and amount of JBIC loans, 1995–2018



Source: JBIC Annual Reports (https://www.jbic.go.jp/ja/information/annual-report.html)

This much swifter and more coherent infrastructure investment strategy under the Abe administration since 2013 also has its domestic political institutional roots. Since the 1994 electoral reform and the administrative reforms implemented in the early 2000s, the power of the prime minister's Cabinet Secretariat supported by the Cabinet Office has grown, allowing the prime ministers to have more control over their party as well as over the government bureaucracy.[13] Furthermore, during Prime Minister Abe's second term, the civil service reform has enhanced the prime minister's power over promotion and appointments of high-ranking government officials, allowing the prime minister's office to have greater leverage against the well-known fragmentation among ministries in foreign aid and economic policy decision-making.

With the stability that comes with the long reign of Prime Minister Abe in the face of public support to compete against China's expansion, the "all Japan" strategy reminiscent of the 1970s and 1980s emerged to re-create Japan's economic growth engine under Abenomics. Nonetheless, there are some important differences in this apparent developmentalism from the old-style Japanese aid and investment model.

The first contrast is the way in which the private sector participates in the "all Japan" ventures. In the old model, the government was the main supplier of the financial resources for Japanese companies to obtain overseas infrastructure businesses financed by public or semi-public funding.[14] Meanwhile, the current approach is intended to rely largely on private funds as government financing becomes the pump primer to tap into private financing to fill the gap of the Japanese government's fiscal shortfall.

The second contrast is the ambivalence of Japan's private sector over such incentives put forward by the government in the recent wave. Despite the lip-service support extended by Keidanren,[15] the engagement of Japan's private businesses in the PPP scheme in infrastructure investment in Asia has not been robust. Many infrastructure projects in emerging Asian economies in the 21st century come mainly in the form of "concessions," in which private firms take responsibility not only for the operation and maintenance of the invested assets but also for the financing and managing of all required investment; hence they take risks with respect to both condition of the assets and the investments themselves.[16] This scheme is quite different from earlier government-funded ventures consisting of a single project that a private company had to manage (i.e., the so-called engineering, procurement, and construction (EPC) projects) and where PPP arrangements counted on private firms to fund several phases of aid projects, with the government providing the official loans as well as trade and investment insurance.[17] Japanese businesses' high sensitivity to financial risks leads them to prefer old-style EPC schemes where they see well-identified and limited operational and financial responsibilities with limited uncertainty and risk, and Japanese businesses consider the associated risks with the current infrastructure project schemes to be too high.[18]

The Future of PQI and Japan's Regional Leadership

Through the PQI initiative and infrastructure investment push into Asia, the Japanese government has pursued the "twin goals" of creating a new growth engine for the Japanese economy and strengthening strategic links with Asian countries to counter China's regional influence.[19] In the process, the competition with China has drawn the Japanese government into revisiting its developmentalist origin. Nonetheless, the changes in conditions—both domestically and regionally—have forced the Japanese government to place much stronger emphasis on high standards, quality, and risk management in order not only to distinguish itself from China but also to allow the Japanese private sector to actively engage in the Japanese government's initiatives. High risks associated with infrastructure investment continue to demand government involvement. Nonetheless, the Japanese government's past experience as well as its receded position vis-à-vis its private sector would most likely force Japan to capitalize on high standards and liberal rules.

Notes

[1] Revised paper from the "Japan's Leadership in the Liberal International Order" conference at the University of British Columbia, School of Public Policy and Global Affairs, January 24–25, 2020. I thank Gabrielle Cheung for her excellent research assistance.

[2] Jiang Yang, "Competitive Partners in Development Financing: China and Japan Expanding Overseas Infrastructure Investment," *The Pacific Review* 32, no. 5 (2019): 778–808. doi: 10.1080/09512748.2019.1569117.

[3] In 2017, ADB estimated that there would be US$26T in infrastructure investment needs in Asia alone into 2030. For the shift to emphasize the infrastructure investment in the global development governance since the global financial crisis through the Busan consensus to the UN Sustainable Development Goals, see Emma Mawdsley, Laura Savage, and Sung-Mi Kim. "A 'Post-Aid World'? Paradigm Shift in Foreign Aid and Development Cooperation at the 2011 Busan High Level Forum," *The Geographical Journal* 180, no. 1 (2014): 27–38.

[4] Hironori Sasada, "Resurgence of the 'Japan Model'?: Japan's Aid Policy Reform and Infrastructure Development Assistance," *Asian Survey* 59, no. 6 (2019): 1044–69.

[5] Walter Hatch and Kozo Yamamura, *Asia in Japan's Embrace: Building a Regional Production Alliance* (Cambridge University Press, 1996).

[6] John T. Pempel, *Regime Shift: Comparative Dynamics of the Japanese Political Economy* (Ithaca: Cornell University Press, 1998); Kanishka Jayasuriya, "Embedded Mercantilism and Open Regionalism: The Crisis of a Regional Political Project," *Third World Quarterly* 24, no. 2 (2003): 339–55.

[7] For an interesting critique on the spread of the "debt trap diplomacy" meme, see Deborah Brautigam, "A Critical Look at Chinese 'Debt-Trap Diplomacy': The Rise of a Meme," *Area Development and Policy* 5, no. 1 (2020): 1–14.

[8] Saori N. Katada, *Japan's New Regional Reality: Geoeconomic Strategy in the Asia-Pacific* (New York: Columbia University Press, 2020).

[9] Asa Malmstrom, "Power and Development in Indonesia," in *The Business of Japanese Foreign Aid: Five Cases in Asia*, ed. Marie Söderberg (London: Routledge, 1996): 127–50.

[10] Saori N. Katada, "Indo taiheiyo koso to do chiiki no Keizai renkei [Indo-Pacific Initiative and Economic Connectivity of the Region]." Commissioned for a special issue on "The Potentials of the Indo-Pacific Concept," *Japan Institute of International Affairs* (December 2019).

[11] Tomoo Kikuchi and Sayaka Unzaki, "Japanese Infrastructure Investment in Southeast Asia," *Think Asia – RSIS*, Nanyang Technological University, Singapore (2019).

[12] Japan International Cooperation Agency (JICA) introduced the "Special Terms for Economic Partnership (STEP)" modality, where Japan's foreign aid became explicitly tied to procurement from Japan and was given to the leading partners from Japan; Ajia infra kenkyu kai, "Ajia Infura Kenkyukai no Teigen: Infura PPP Jigyo no Suishin nimukete [Proposal of Asia Infrastructure Study Group: How to Promote Infrastructure PPP Projects]," Ministry of Economy, Trade and Industry (2006).

[13] Harukata Takenaka, "Expansion of the Prime Minister's Power in the Japanese Parliamentary System: Transformation of Japanese Politics and Institutional Reforms," *Asian Survey* 59, no. 5 (2019): 844–69.

[14] In the 1970s, about 60 percent of Japanese foreign aid came in the form of yen loans whose funding was based on the Fiscal Investment Loan Program (zaisei toyushi), whose capital base was the postal savings; David Arase, *Buying Power: The Political Economy of Japan's Foreign Aid* (Boulder, CO: Lynne Rienner Publishers, 1995).

[15] Keidanren, "Towards Strategic Promotion of the Infrastructure Export: Our Interest and Challenges in Main Target Countries for 2015" (November 17, 2015), https://www.keidanren.or.jp/en/policy/2015/105.html, for example.

[16] Toshiro Nishizawa, "Infrastructure Investment and Finance in Asia," *Public Policy Review* 14, no. 5: 925–53.

[17] METI, "Keizan Sangyo Sho, PPP Tasuku Fosu Hokokusho [Ministry of Economy, Trade and Industry, PPP Task Force Report]," (2010).

[18] Yasuhiro Ezaki, "Ajia Shikou koku infura bisinesu to nihon kigyo no gurobaru risuku manajimento taisei [Infrastructure Building Business in Asia's Emerging Economies and the System of Japanese Firms' Global Risk Management]," *Higashi ajia Hyouron* 8 (2016): 19–34.

[19] Hidetaka Yoshimatsu, "Japan's Export of Infrastructure Systems: Pursuing Twin Goals Through Developmental Means," *The Pacific Review* 30, no. 4 (2017): 494–512.