

# Japanese Substitution of Multilateralism for Bilateralism: A Case of Foreign Economic Assistance in 1987

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In the period of 1985-87, Japan's response to western criticism of its contributions to the alliance had significant new elements. These were the implementation of the Maekawa Report, a steady increase in Japanese defense spending going beyond the one-percent of GNP limit, and increased aid to the developing countries. They represented watershed in postwar Japanese history because they clarified Japan's willingness as one of the secondary powers, to cooperate with and contribute to international society as tangible Japanese efforts commensurate with its economic power.<sup>(1)</sup> The purpose of this article is to show how the Japanese government took a new strategy of multilateralism in the foreign economic assistance policy as a conscious response to the U. S. criticism of Japan stemming from the huge trade imbalance in 1987. The political implication of this shift toward international cooperation is that the Japanese government and the business community in effect substituted multilateralism (cooperation

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(1) For example, the year 1987 became one of Japan's most generous years in terms of foreign aid. Japan's Official Development Assistance (ODA) reached \$7.454 billion, rising 32.3% over the previous year in dollar terms (Ministry of Foreign Affairs, 1989, p. 7). Although ODA was only one component of total financial flows to developing countries, this manifest trend explicitly illustrates the turning point of Japanese aid policy in its history.

with international development organizations) for bilateralism (Japan-U. S. relationship) in foreign aid policy.

## 1. Theoretical Purpose

Although there exists a pretty well-known and widely accepted definition,<sup>(2)</sup> the concept of international regime has attracted authors of strikingly different theoretical standpoints, and therefore has caused considerable amount of confusion about the usage and usefulness of the concept. This diversity and confusion happens because the concept was introduced by “modified structuralists (realists)” into the field of international relations as what conventional realism could not explain.

The regime literature originated from the effort to explain what conventional realists failed to explain — a relatively stable international economic order in the 1970s and 1980s in spite of America’s decline as a hegemonic power. According to the realists argument, actors’ characteristics is held constant — they are unified and egoistic self-interest maximizers, who make rational choices. That is, political idealism, altruism and irrationality as the origins of orders are irrelevant. The regime literature is basically rationalistic. Realists assume that the origins of order exist completely outside of actors. Therefore, they regarded the stable economic order after World War II to be sustained by a dominant power, a hegemon, and expected its collapse after American hegemonic decline.

International regimes have been treated as intervening variables, which intermediate basic causal variables — egoistic self-interest, political power and norms and principles — and create cooperation and order among actors. Therefore, in the modified structuralist view, the origins of order basically lie outside of actors, and in this meaning, modified structuralist stand well within the conventional

- (2) One of the most widely accepted definition is Stephan Krasner’s: “Regimes can be define as sets of implicit or explicit principles norms rules, and decision making procedures around which actors’ expectations converge in a given area of international relations” (Krasner, 1983, p. 1).

realist stance. Of course, as realists, they assume states as primary and unified actors. Robert Keohane, relying on institutional arguments in microeconomics, developed elegant functionalist expectations why the demands for regimes originate — “political market failure,” “transaction cost” etc.<sup>(3)</sup> In other words, we may explain that one widely accepted way of achieving policy adjustment among industrialized states is through the activities of a hegemonic power to build what Keohane calls “international regimes” that serve hegemon’s own interests and are also sufficiently compatible with the interests of subordinate countries.

This essay asks whether or not the modified realist explanation on the international regimes can be well applied to Japanese foreign economic policies in the mid-1980s when the international system clearly experienced structural change due to Japan’s meteoric rise as a financial superpower. If the conventional realistic view holds true of the regime, the flow of Japanese financial resources to the Latin American region must have been shrinking, especially after 1982 when debt crisis emerged as a serious problem that hampers financial flows from industrialized countries. As far as Japan pursues its narrow-minded interests based on egoistic motivations, and it takes advantage of damaging effects of the debt crisis on the U. S. economy, the capital flows to Latin American countries were supposed to be tapering off, despite the U. S. increasing pressures (*gaiatsu*) on Japan. On the other hand, if Japan’s contribution to the international regime is derived from its interest in international cooperation for the sake of sustaining current international economic order, instead of serving directly to interests of hegemon itself, the capital flows would be increasing.<sup>(4)</sup> Therefore, the theoretical implication of this paper is to evaluate the plausibility of the view of the modified realists that secondary powers in the current international regimes

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(3) Keohane, 1984, chap. 6.

(4) This puzzle is echoed in Duncan Snidal’s article. Snidal claims that there needs to be a clear distinction between two different models of regimes: benevolent model and coercive model. See Snidal, 1985.

make contribution to maintaining the international political economic order because they find it in their interests to respond to external constraints and opportunities derived from structural change in the world economy and then to reciprocate cooperation based on strategic rationality, especially under the condition of the marked interdependence in postwar years.

To answer the question, Japanese financial flow to Latin American countries is to be examined as a crucial case. This case is crucial not only because Latin America is traditionally regarded as under the U. S. sphere of influence to which Japan is imposed increasing pressures for expanding its contribution, but also there exist overt conflicts of interest between Japanese and American private sectors over appropriateness to inject further financial resources in the debt-ridden region. Thus the Japanese government was forced to face a political dilemma during the period between faithful commitment to the vital bilateral relations with the United States and strong belief in market-based, liberal resource allocation to developing countries within a framework of international regimes.

## 2. The Structural Change in the World Economy : Japan's Rise as a Financial Superpower

From the perspective of Japan's international environment, the year 1987 saw the confluence of two factors: the bilateral conflict with the United States caused by the unprecedented trade imbalance on the one hand, the worldwide struggle for dealing with the deteriorating debt crisis in Latin America on the other. The resulting policy of the Japanese government was to dedicate the nation's capital surplus through multilateral cooperation with international development organizations such as the International Monetary Fund (IMF), the World Bank (IBRD) and the Asian Development Bank (ADB).

During the 1970s-80s period, there was a series of major economic shocks in international markets for traded goods and in international capital markets. The oil-price rises of 1973-74 and 1979-80 touched off major changes in the terms of trade between manufactured goods and raw materials. These price shifts were accompanied by slow-

downs in world trade in 1974-75 and again in 1979-83, largely because of recessionary conditions in the advanced industrial countries whose markets had been the source of dynamism of world trade in the 1960s. The ensuing world recession during 1979-83 was the longest in post war history and affected both developed and developing countries.<sup>(5)</sup> The major challenge in world capital-market conditions occurred in 1974-79, in the wake of the first oil-price shock of 1973-74. As the advanced industrial countries went into a simultaneous recession, traditional corporate borrowers disappeared from the market. Consequently, the banks began to see Third World governments as attractive clients. This tendency increased as oil exporters deposited much of their increased revenues with the major international banks in 1973-74 and 1979. Previously, most of the external funding available to the developing countries had come from the savings of the industrial economies, and much of this had been distributed through official government channel or through multilateral institutions, such as the IMF or the World Bank. After 1973-74 the oil-exporting countries began to provide substantial savings to be recycled by the commercial banks. The dramatic growth in the supply of loanable funds from this savings and the resulting competition among commercial banks pushed down the real rate of interest on commercial bank loans. The low and sometimes negative real interest rates resulting from such conditions enhanced the attractiveness of external borrowing as a way to finance continued growth, despite adverse shifts in the terms of trade and temporarily reduced export prospects for many countries.<sup>(6)</sup>

In, 1979, however, world credit-market conditions began to tighten as result of the simultaneous introduction of restrictive monetary policies in several industrial economy, most significant, the United States.<sup>(7)</sup> These policies drove real interest rates sharply upward and began to attract capital flows from the developing to the developed

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(5) Kahler, 1985.

(6) Stallings, 1987.

(7) Frieden, 1987.

economies. Consequently, during the 1980s, less developing countries were suffering from a lack of funds needed to finance economic growth. Although official development assistance from industrialized countries to the third world had increased in absolute terms, it was private capital, previously the main source of financing for third world countries, that has been drying up. The cut-off of the private capital deteriorated economic conditions and caused the devastating debt crisis especially in Latin American countries. By late 1985, the debt crisis was still unresolved in the three years since Mexico's moratorium on debt service in 1982. Even those countries such as Brazil that were successful in running trade surpluses were mired in recession. Real per capita growth in Latin American countries was negative between 1981 and 1983 and stagnant in succeeding years. This stagnation was mainly the result of the policies that permitted debt service to continue. On the one hand, the principal source of the trade surplus was a lower volume of imports, which often brought a fall in production. On the other hand, the combination of high debt service payments and low capital inflow led to large net transfers from Latin American to the creditor countries, and thus a decline in both investment and consumption.<sup>(8)</sup>

Under these debilitating conditions, the widespread call for policies focusing on renewed growth brought a response from the U. S. Treasury Secretary James Baker. At the annual meeting of the World Bank and the IMF in Seoul in October 1985, he announced the so-called Baker Initiative which was to provide \$29 billion over three years to 15 heavily indebted countries, ten of which were in Latin America. However, the Baker Initiative never succeeded except in the case of Mexico, where the United States has a special relationship and particular economic interests. Under initiatives subsequent to the failure of the Baker initiative — the “Menu Approach” and the “Brady plan”<sup>(9)</sup> — new money was not provided to Latin American countries in the amounts envisioned. In May 1987, Citicorp chairman John Reed announced that the bank would add \$3 billion to its loan

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(8) The World Bank, 1988.

loss reserves, equivalent to 20 percent of its Third World loan exposure.<sup>(10)</sup> Other U. S. major banks followed Citicorp's lead.

This evolution of the debt problem suggested that private banks in the U. S. were so reluctant to provide new money that debt problems required involvement of another actor, that is, Japan, the largest creditor in the world.<sup>(11)</sup> The enormous Japanese capital surplus drew the attention of the U. S., which was interested in whether and how a portion of these funds might be channeled to deal with the debt problems and capital requirements of the developing countries. It was this time that an American business leader, James Robinson, Chairman of American Express, sounded an influential call for Japan to launch a Marshall Plan, which he termed a Global Security Initiative.<sup>(12)</sup>

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- (9) The Brady Plan in April 1989 adopted a similar idea to Miyazawa's. Following the \$30 billion recycling plan, Finance Minister, Kiich Miyazawa announced the Miyazawa Plan at the Toronto Summit in June 1988. The basic idea was to trade old loans of Latin American countries at a discount for new long-term bonds. The bonds would be guaranteed by reserves of the debtor countries deposited with the IMF. The remainder of the debt would be rescheduled, and new loans would be provided by the international institutions and Japan itself. At first, the plan was ignored at the Toronto Summit and openly attacked by American Treasury Secretary Brady.
- (10) *Financial Times*, May 22, 1987.
- (11) As with data on U. S. and Japanese Banks' medium and long-term loans outstanding to Latin America as of 1982, loans to Latin America were significantly more important for U. S. banks, when comparing Latin American loans to total banks assets (both domestic and international). See Stallings, 1987, p. 8.
- (12) His reasoning for calling for a Japanese initiative was based upon the fact that no nation was better positioned to spearhead the Global Security Initiative than Japan; with its staggered trade and capital surpluses, Japan had substantial reasons for heading the charge; with the U. S. spending about 6% of its GNP on defense, Japan's role over time would be to match in economic terms with the U. S. military contribution to security (Interview with Keidanren, June, 1989).

With the steep increase of the trade surplus against the United States after 1980, Japanese government put the highest priority in foreign policies on reducing the surplus in order to maintain a good relationship with the U. S. Nevertheless, the trade surplus kept increasing remarkably even after the appreciation of the Japanese Yen since September 1985 and the Japanese government's strenuous efforts to stimulate domestic demand. In 1987, the trade surplus with the U. S. reached the unprecedented level to \$59.8 billion.<sup>(13)</sup> In the early 1980s, Japan had been running a current account surplus with the other industrialized countries and a deficit with the developing countries. But, with the worldwide drop in oil and other commodity prices and the yen's appreciation, by 1986 Japan began to run surpluses with the developing countries as well. Japan's current account balance grew from a \$10.7 billion deficit in 1980 to a \$20.8 billion surplus in 1983. It increased steadily thereafter to \$85.8 billion in 1986. On the other hand, in the capital account, there was a net inflow of capital from the United States and Europe in 1980. But this was reversed by 1983 with the increasing current account surpluses. Japan became a net exporter of capital to the other industrialized countries. In 1986, while the total capital flow from Japan was \$130 billion,

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(13) This data draws on the International Monetary Fund, *Direction of Trade Statistics*. Although the gap between exports and imports did narrow from \$59.8 billion in 1987 to \$55.4 billion in 1988 after eight years of successive growth, improvement was unexpectedly modest given all the factors working in favor of a smaller shortfall. According to Keidanren's estimate, by itself the roughly 50 percent drop in the value of the dollar against the yen since September 1985 should have shrunk the deficit by more than \$4.4 billion. This unpredictable consequence was in clear contrast to the U. S. trade deficit with European Community, where the trade imbalance has been corrected with remarkable speed. Furthermore, in considering the robust domestic demand in Jaan, the cumulative effects of seven Japanese market access packages dating back to December 1981 and the enhanced competitiveness of American manufactures, the stage seemingly was set for a major correction in the bilateral trade account.



three quarters of it went to the United States and the EC countries and only \$7.6 billion, or 6% of the \$130 billion went to the developing countries.<sup>(14)</sup> To make matters worse for the developing countries, in 1986, global financial flow reversed and capital went from developing countries to developed countries as a result of capital flight and retrenchment in commercial lending. The net inflow to developing countries amounted to \$30 billion in 1980-81. However, the tide shifted completely by 1985-86 with \$30 billion in net outflows from the developing countries. This figure was then projected to rise to \$40 billion a year by 1991.<sup>(15)</sup>

However, the problem in recycling Japanese capital surpluses was the fact that most of this capital surplus was held by the private sector. Net external assets held by the private sector accounted for \$105 billion of the \$130 billion surplus as of 1986.<sup>(16)</sup> The fact that these funds were privately held and were responsive to but not controlled by government policies and actions made it more difficult for the Japanese government to harness the financial resources for serving to U. S. economic interests. While the United States had limited success in persuading commercial banks to lend additional amounts to developing countries, Japanese banks were no more eager than their American counterparts. In response to this policy dilemma facing the Japanese government, Japanese private sector interests formulated one position paper saying that unless the Japanese Government provided the necessary environment that would encourage Japanese capital movements into developing countries, it would be very difficult to increase the flow of Japanese capital into these countries at a time of the international debt problem.<sup>(17)</sup>

The Japanese government and the business community had realized the limitation of policies for reducing the trade surplus by the adjustment of the exchange rate and the expansion of domestic

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(14) The Export-Import Bank of Japan, 1989a.

(15) Interview with Keidanren, June 1989.

(16) Keidanren, October 1988.

(17) Keidanren, 1987.

demand.<sup>(18)</sup> Nonetheless, despite these misgivings, U. S. pressure forced the Japanese government to continue to follow stimulative economic policies. Specifically, the government outlined two measures related to the expansion of domestic demand on two occasions. First, during three years from 1986 through 1988, the official discount rate was lowered five times; four times in 1986, once in 1987. Second, the Japanese government adopted "Emergency Economic Measures" in May 1987 with the intention of implementing immediate measures to stimulate domestic demand, accompanied by fiscal measures amounting to more than Y6 trillion (about \$46 billion at then exchange rate). While those two policies were considered to have been successful in reducing political tension between Japan and the United States, we can discern a new strategy in the Emergency Economic Measures in 1987, that is Japanese multilateralism.

As the limited effects of the emergency measures on rectifying the imbalance, and as pressures from both the domestic and international business community mounted, the Japanese government was determined to establish some mechanism to mobilize the funds held by the private sector. Japan responded by announcing and implementing a "\$30 billion recycling program," a three year program to recycle capital to developing countries. Also, Saburo Okita, former Minister of Foreign Affairs, proposed "Okita Plan," a \$125 billion recycling scheme over five years to channel the Japanese capital surplus to developing countries. The details of these plans and their assumptions will be discussed below.

### 3. Emergent Multilateralism: Cooperation with International Financial Organizations

#### A. \$30 billion Recycling Plan to Developing Countries<sup>(19)</sup>

Former Prime Minister Nakasone announced the plan during his May 1987 visit to Washington to recycle \$30 billion (combined with the \$10 billion plan announced in 1986) over three years to developing countries, with the details of this plan presented on June 9 at the

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(18) Interview with Keidanren, June 1989.

Venice Summit. It should be noticed that, although the purpose of the recycling program, as it was explained by the Japanese government, was to encourage Japanese capital movements to developing countries, the plan was positioned as a part of a Y6 trillion package of the above-mentioned emergency measures adopted by the Cabinet on May 29, 1987. This stimulus package was prepared for the summit meeting as a key element in the Japanese Government's plan to demonstrate that the Japanese were determined to boost domestic demand and to reduce the trade deficit, in spite of the fact that the Japanese government had realized the limitations of the effectiveness of such measures. In this context, the ultimate purpose of the recycling plan was not to direct the capital surplus towards debt-ridden counties but to ease the bilateral tension with the United States through a multilateralist gesture. There are two parts to the Japanese recycling program :

(i) \$10 billion, announced in 1986, consisting of contributions and subscriptions to the multilateral development agencies, such as the World Bank, the Asian Development Bank (ADB), and the IMF. Out of the \$10 billion, \$2 billion was allocated for the Japan Special Funds within the World Bank. This was additional borrowing authority up to Y300 billion over three years in Japanese financial markets. Agreement was signed in June, 1987 ; \$0.2 billion was for grant funds to the World Bank for co-financing of the World Bank's projects. International Development Association (IDA) countries were not eligible for this funding. These funds were for technical assistance, feasibility studies, sectoral and structural adjustment and disaster assistance. The funding came from the Japanese government's budget ; \$3.6 billion was for IMF special lending. Total of SDR 3

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(19) Following data draws on a memo prepared by the Economic Cooperation Department, Keidanren, "Shikin Kanryu Keikaku no Gaiyo [Outline of the Capita Surplus Recycling Plan]" and interviews with staffs of the department, June 1989. The total amount dose not add up to exact \$30 billion, because the amount was set first as a goal before designing details.

billion for the IMF special facility for critical situations that required financial support beyond the usual recourse. Funds came from the Foreign Exchange Special Account (*gaikoku kawase tokubetsu kaikei*); \$2.6 billion was for Japan's contribution to the eighth replenishment of IDA (21% of the total); \$1.3 billion Japan's contribution to the Asian Development Fund.<sup>(20)</sup>

(ii) \$20 billion, announced in 1987. Like the \$10 billion recycling, this was provided through the multilateral development banks. \$8 billion of the total was allocated for creating funds similar to the Japan Special Funds at the World Bank also in the Asian Development Bank and the Inter-American Development Bank. Roughly \$7 billion of this total was supposed to be private funds raised on the Tokyo market, while the remainder consisted of government contributions to the capital subscriptions of the multilateral development banks; \$9 billion was funds for co-financing from the Overseas Economic Cooperation Fund (OECF), the Export-Import bank of Japan (Exim Bank), and private banks with multilateral development banks' lending. Roughly two-thirds of these funds could be expected from Exim Bank, and one-third from OECF;<sup>(21)</sup> \$3 billion was for direct untied loans by the Exim Bank. Large portion of the funds, at least 40 percent of the loan extended by the Exim Bank, were expected to go to Latin American countries, that is, the 'back yard' of the United States.<sup>(22)</sup>

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(20) The Asian Development Fund is a special fund established within the ADB that specializes in provision of concessive loans for member countries in the Asian Development Bank.

(21) OECF funds are counted as official development assistance (ODA), while Exim funds are not.

(22) To avoid the impression of an undue emphasis on Latin American countries, the Japanese government announced with the above plan its intention to increase its grants to Sub-Saharan Africa and the least developed countries by \$500 million. These were designed to be on-project grants for a three year period from 1987 to help in structural adjustment. These funds were not channeled through the World Bank, but were being provided through the Ministry of Foreign Affairs.

In short, the entire amount of the \$30 billion recycling plan was channeled through or in close consultation with the multilateral development banks. This concentration on the multilateral development banks was noteworthy in shifting ways of resource allocation by the Japanese government.<sup>(23)</sup>

#### B. The Okita Plan

Saburo Okita, the former Japanese Foreign Minister, proposed in September 1987 that Japan launch a \$125 billion five year plan to transfer resources to developing countries, at annual rate of \$25 billion. Okita's proposal came from a study group he had chaired under the auspices of the World Institute for Development Economic Research (WIDER), an arm of the United Nations University in Tokyo. The WIDER report, "Mobilizing International Surplus for World Development: a WIDEP Plan for a Japanese Initiative," was issued on May 7, 1987, a few days after Prime Minister Nakasone had presented his \$30 billion plan in Washington. The upstaging was of course no coincidence. Okita was called a "boss" in the realm of bureaucracy, because he had held various important positions in the field of Japanese foreign aid; among others President of OECF and the Chairman for Council for Overseas Economic Cooperation (*taigai keizai kyoryoku shingikai*). Policy recommendations under his name had been highly respected among the bureaucrats concerned. Among the many policy proposals dealing with Japanese aid in 1987, Okita's suggestion was one of the most influential, and proposal was carefully discussed not only by government officials but by the business

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(23) Although the outstanding feature of this plan was the close collaboration with multilateral development banks, it did not tilt the balance towards the multilateral channels at all. The Japanese allocation ratio between multilateral and bilateral aid of 3:7 was maintained even after the implementation of the plan. The share of multilateral assistance in Japan's total ODA in 1985-87 was: 32.7% in 1985, 31.7% in 1986, and 29.6% in 1987. Therefore, bureaucratic conflict between bureaus in charge of regions and those that contact with multilateral organizations could be avoided.

community, because it dealt explicitly with key questions such as undesirability of a sharp fall in the current account surplus.<sup>(24)</sup> Although there were a number of innovative financing elements to the Okita Plan, the methods and principle of recycling the capital surplus followed closely the mechanisms instituted by the Japanese government's \$30 billion recycling plan, that is, close cooperation with multilateral financial institutions. The plan called for a three part program :

(i) The Japanese Trust Fund would raise funds on the Tokyo market using guarantees from Japanese government agencies. Developing countries might borrow from the Japanese commercial banking system against the collateral of zero coupon bonds issued by the fund.<sup>(25)</sup> WIDER estimated that this mechanism could raise \$10 billion annually, or \$50 billion over five years.

(ii) The Export Import Bank of Japan would increase its co-financing arrangements beyond its 1987 levels of \$2 billion per year. WIDER calculated that a co-financing program of \$10 billion per year was quite realistic, given the \$150 billion annual flow of funds into the government's Fiscal Investment and Loan Program (*Zaisei Toyushi*), which includes postal savings, government pension funds, and other collections. The Exim Bank had unutilized guarantee power of about \$40 billion. The report pointed out that a major advantage of co-financing was that it was not limited by the capital adequacy of the multilateral development banks. This was an important element of the scheme since the World Bank was lending close to its capital ceiling at the present 1:1 gearing ratio. On the other

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(24) The report articulates that "[Japan's] surplus is now viewed in a negative light—because it is associated with Japan's export drive and the problems caused in other industrial countries by Japan's super-competitiveness. Instead, the potential of the surplus for world economy should be emphasized" (WIDER 1987, p. 5).

(25) The amounts borrowed would be a substantial multiple of the investment needed to buy these bonds, whose face value on maturity will be equivalent to the principal borrowed, thereby fully securing repayment of the principal.

hand, decisions on co-financing were within the discretion of the Exim Bank and the Japanese government.

(iii) The IMF should be permitted to borrow in Japan's capital market at a rate of \$5 billion annually to provide the program lending to low income developing countries, using the IMF's Extended Financing Facility.<sup>(26)</sup>

The plan emphasized the need to find an outlet for Japan's current account surplus, and concluded that as domestic demand in Japan could not be sufficient to absorb the Japanese surplus, it was necessary to boost demand in developing countries through a major recycling plan that asked intermediate roles played by multilateral financial institutions.

Both the \$30 billion recycling plan and the Okita plan represented Japan's interests in extending international cooperation that brings little relative gains to the Japanese government in international relations, let alone to the Japanese economy. Politically, since Japan's participation at senior levels in the World Bank and the IMF has been quite limited, the multilateral development banks could use the recycling money, to some extent, at their discretion. In other words, Japanese government interests lay not in how the money was to be used, but in how much money was to be recycled. The recycling money was merely bestowed upon the multilateral organizations by the Japanese government. For example, as far as the Ministry of Finance is concerned, it is generally believed that the posts in the international organization do not lead to the "fast track" in bureaucrats' future careers. As few people became Director-general of a bureau in the ministry after the service in multilateral organizations, the position in such organizations have been regarded as a dead end

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(26) The Study Group also called for a Debt Reconstruction Facility, which would retire LDC debt through the issuance of long-term bonds. This proposal called for participation by the U. S., Japan and other countries, and would aim to provide relief from current debt

of career path.<sup>(27)</sup> The underrepresentation of Japanese nationality in international organizations leads to difficulty in affecting decision-making process within them and thus in strengthening voting power of Japan. For example, in 1986, Japan raised its contributions to the World Bank's International Development Association (IDA) by \$350 million, becoming IDA's largest supporter with a total subscription of \$2.6 billion. In response the United States agreed to decrease its share of voting rights in the World Bank so that Japan's share could be raised — but only after the veto threshold to ensure continued American control was also agreed.<sup>(28)</sup> In June of 1987 Japan took another initiative at the World Bank, when it became the first industrialized country to ratify the convention establishing the Multilateral Investment Guarantee Agency (MIGA). However, it did neither change Japan's voting power nor increase its voice in the World Bank.

Also Japan's financial cooperation with multilateral organizations realized little economic gains, at least in a short term. The expectation that a large percentage, at least a quarter of the \$20 billion announced in 1987, was supposed to come from the Japanese private sector suggests that this policy was formulated by the Japanese government-business complex with close consultation.<sup>(29)</sup> However, this time the close relations between the government and business failed to realize domestic interests but aimed to contribute to sustaining international economic order. On the one hand, increased borrowing by the multilateral development banks from the Tokyo market or

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(27) When the World Bank offered the post of the Executive Vice President to Toyoo Gyoten, the Deputy Vice-Minister for financial Affairs at the Ministry at that time, just after the announcement of the recycling plan, the Ministry refused the request and proposed instead a lower-level official in his place. Gyoten was simply too high in rank to accept the proposal. Interview with Keidanren, June 1989.

(28) Japan Economic Institute, *JEI Report*, No. 20F, 20 May 1988; the World Bank, 1988.

(29) Interview with Keidanren, June 1989.



co-financing with the Exim Bank allowed the Japanese government to tap private market without requiring new budget authority or Japanese government guarantees. The government's role in mapping out this scheme was only to decide plausible total amounts of the recycling money using normal consultative channels between the Ministry of Finance and the private banks. On the other hand, the Japanese government insisted repeatedly that these funds were to be in the form of untied aid so that the recycling plans would be understood by U. S. Congress not as an export promoting policy but as a new approach based on multilateralism.<sup>(30)</sup> It was agreed between the Japanese government and the World Bank that procurement under this new program would be supervised by the World Bank.

#### 4. Decreasing Bilateralism : Financial flows to Latin America

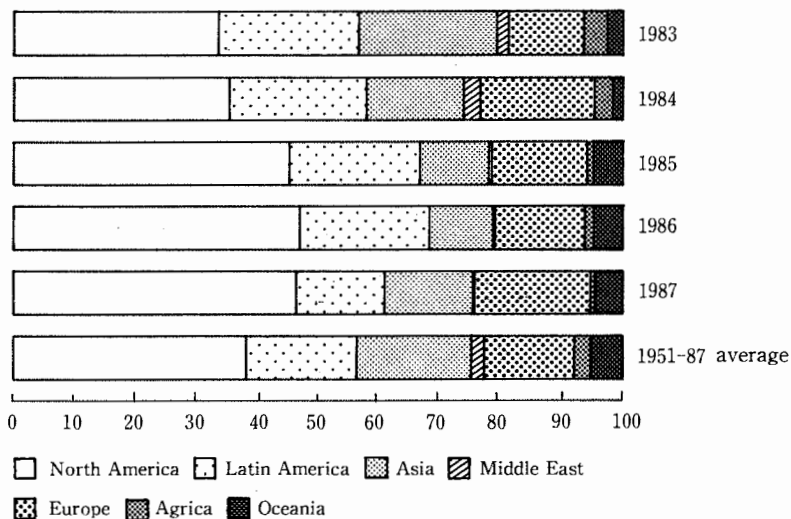
In contrast to the enhanced multilateralism, decreasing bilateralism has been the other side of the same coin of Japanese foreign economic assistance policy since the late 1980s. While a huge amount of Japan's surplus capital was recycled through multilateral financial institutions, little political attention was paid on a bilateral basis to improve deteriorating economic conditions in Latin American countries. During a period in which it has generated huge current account surpluses and long-term capital outflows, Japan invested primarily in industrialized countries, particularly in the United States and Europe rather than increased capital flows to developing countries. In 1987, 45 percent of long-term capital outflows went to the United States and 25 percent to EC countries. In comparison to 1983 levels, this represented an increase in percentage of capital flows to the United States from 31 percent and to the EC countries from 16 percent. The percentage toward the developing countries decreased from 57 per-

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(30) Japan had been severely criticized by OECD countries for directly or indirectly tying its aid, especially for permitting feasibility studies by Japanese consultants to tailor projects to Japanese specifications.

cent in 1983 to 17 percent in 1987.<sup>(31)</sup>

Japanese reluctance toward developing countries in the 1980s was particularly true to decreased foreign direct investment in Latin America. In the 1980s, generally, while Japanese investment in North America continued to be almost half of the total for the period, and investment to Asia and Europe almost doubled their shares over the period, investment in Latin America, apart from that seeking tax havens, remained low. Especially, in 1987, with volume remaining at the same level as the previous year, Latin America's share of total investment fell drastically from 21.2% in 1986 to 14.4%. Thus, it fell in the ranking by region from second place, maintaining up to 1986, down to fourth place below Europe and Asia<sup>(32)</sup> (See Figure 1).



Source : Ministry of Finance, Japan, Zajsed-Kinyu-Tokey-Geppo

Figure 1 Overseas Direct Investment by Region (1983-87) (%)

(31) The Export-Import Bank of Japan, 1989a.

(32) As to absolute amount, investment in Latin America in fiscal 1987 came to a new record high for the sixth year in succession, with a total of \$4,816 million, though this was only \$79 million greater than the previous year's total.

The main reasons for the overall drop in investment 1987 were decrease in investment in manufacturing decreased from \$273 million to \$161 million, and in resource development from \$114 to \$33 million.<sup>(33)</sup> Large-scale Japanese “national projects” in the region in the late 70s and early 80s, such as the Peruvian oil pipeline, the Mexican port and pipeline facilities, the Sicartsa steel complex in western Mexico, the Cerrado agricultural complex in central Brazil and the Carajas multi-resource project in the Amazon basin, could not be initiated without corresponding bank lending.<sup>(34)</sup>

Therefore, Barbara Stalling’s statement that “<b>oth the pre-1982 and post-1982 periods clearly reveal the influence of the United States. Japanese banks got into Latin America lending by following the lead of their U. S. counterparts”<sup>(35)</sup> might be persuasive no later than 1987 when the Japanese private flows began to shrink.

## 5. Conclusion

The American view of Japan as a nation where the market mechanism does not work and which poses a threat to American interests has been growing just as the perception of the Soviet military threat has ebbed. Japan’s reactions to the U. S. criticism has been based upon multilateralism since the late 1980s, claiming that rectifying bilateral conflicts with the United States must be compatible with sustaining existing international economic order. For instance, in a field of international trade, the United States targeted supercomputers, communication satellites and forest products for bilateral negotiations under the terms of Super 301 provision of the Omnibus Trade and Competitiveness Act of 1988, even if it was readily acknowledged that the trade barriers explain only a small part of the persistent U. S. trade deficit with Japan. In addition, negotiations were being held on alleged “structural impediments” in Japan’s distribution system, keiretsu issue, etc. In the U. S. view, the

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(33) The Export-Import Bank of Japan, 1989b.

(34) Wellons, 1988 ; Hollerman, 1988.

(35) Stallings, 1987, p. 35.

only way to overcome such trade-distorting practices might be to set numerical import goals for Japan, that is, "managed trade."<sup>(36)</sup>

In contrast to the above U. S. views that have inclined to bilateral solutions, Japanese views and reservations on this situation could be summarized as multilateral. The multilateralism has been pervasive even among Japanese business sector which used to rely on bilateral means to reduce economic conflicts with the United States, such as voluntary exports restrains on various manufactured goods on which Japan has high pride and competitiveness. For example, Keidanren's policy paper on international trade in the late 1980s clearly articulated that demanding bilateral negotiations with threat of sanctions runs against the basic spirit of GATT, which provides for negotiations on an equal footing among the contracting parties ; in imposing sanctions on a trade partner, the U. S. is disregarding accepted GATT procedures for resolving disputes which require explicit endorsement of other contracting parties before the sanction is effected ; should the United States choose to impose sanctions, the depth of the two countries' economic interdependence today is such that the U. S. economy will be affected as well as Japan, and the economy of Asia and many other countries will also be dealt a severe blow ; therefore, talks should, to the fullest extent possible, be carried out under the supervision of GATT or other third parties and should be conducted within a multilateral framework, and this would be in accordance with the international law.<sup>(37)</sup>

This policy stance makes it clear that Japan, as one of major beneficiaries of a liberal, multilateralist trading order, would "sustain the openness of the trading system and strengthen those regime mechanisms which will protect them from the arbitrary actions of its trading partners."<sup>(38)</sup> The contrast of the Japanese desire to seek a multilateral settlement with the U. S. persistence in seeking a bilateral represents an example of the profound structural alteration in

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(36) *The Economist*, November 18, 1989.

(37) Keidanren, 1989.

(38) Haggard and Moon, 1983, p. 135.

the international political economy. In this sense, the Japanese multilateralism of the foreign economic assistance policy of 1987 that I have described above may actually portend the spread of universal multilateralism into other issue areas such as trade, environment, etc. In contrast, the United States found itself in a much less commanding position relative to its major economic partners than was the case during the creation and formative years of post-war international regimes.

The findings of this paper supports modified realistic (neoliberal-institutionalists) view that secondary powers in the current international regimes are motivated to make contributions to maintaining the international political economic order only because they find it in their interests to respond to external pressures imposed by structural change in the international system and to reciprocate cooperation based on strategic rationality. In other words, the international regime can be stable when policy adjustments among industrialized states serves the declining hegemon's own interests and are also sufficiently compatible with the interests of subordinate countries. In this sense, in the field of the economic cooperation toward the Third World, the functional view of the international regimes developed by the liberal institutionalists explains the Japanese foreign economic policies in the late 1980s well.

Realist concern that growing Japanese participation in multilateral institutions must at some point collides with declining American participation has not been materialized. Japan's real intention in using the multilateral organizations was to disburse the surplus money as quick as possible, not to expand its monetary authority to the multilateral organizations. It has been reported that Japan is now clearly in a position that deserves a permanent status on the Security Council of the United Nations and/or president of the IMF or the World Bank. However, Japan will achieve such status without transcending American hegemonic power, but with invoking the substitution of multilateralism for bilateralism.

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