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Asia's Infrastructure Investment Battle

With all the talk about China's investment clout in Southeast Asia, another player is being overlooked.

By Nicholas Borroz and Hunter Marston

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China's expanding influence in Southeast Asia has been the subject of much fear mongering in U.S. media and policymaking circles. Of particular concern is China's activity in the South China Sea, where it is building up naval bases and airstrips atop reefs and atolls. Some worry that China will displace the United States as Asia's principal maritime power in the not too distant future.

American critics are not just fretting over China's sea projects; they worry about those on land as well. One can only guess how many alarmist articles have been written about China's New Silk Road policy, Beijing's grand plan to connect itself to other economies via transport corridors and pipelines.

Railroads are one type of infrastructure project that has gained attention. In Southeast Asia, China plans to build a railroad connecting southern China to Laos, Thailand, Malaysia, and Singapore. For those who fear China's expansionism, the possibility of this railroad indicates a future where Southeast Asia will fall under Chinese dominance.

Japan, one of the United States' closest Asian allies, is also building a railroad in Southeast Asia. This project is part of Japan's larger plans to create an East-West Economic Corridor that cuts through Myanmar, Thailand, Laos, and Vietnam.

It might be argued that China's railroad plans are advancing, whereas those of Japan are stalling. Laos and Thailand are currently considering using Chinese funds to give Beijing access to the Gulf of Thailand. Japan, in turn, is in talks with Thailand regarding a railroad, but it has no plans to build connecting lines in Myanmar, Laos, or Vietnam. China will gain access to the sea, but Japan's railroad will be landlocked. By looking at these two projects alone, you could be forgiven for thinking that China has become a serious competitor for Japan in the infrastructure battle in Southeast Asia. But you would be wrong.

First of all, even in terms of railroad plans, it is debatable to say which country is advancing more quickly. In fact, no serious construction has begun on either railroad, and the projects so far remain only notional. If the railroads do some day come to fruition, the Japanese railroad would be more effective in achieving geopolitical goals. It would run along an economic corridor that bypasses the Malacca Strait, the narrow channel through which both China and Japan import most of their hydrocarbons.

The Chinese railroad, however, would not bypass the Malacca Strait. This is because Beijing has been forced to settle for its second choice of Southeast Asian railroad route. Its first choice was to pass through Myanmar, which would have allowed China to avoid its Malacca Dilemma. But China's heavy-handed investment and diplomatic approach in Myanmar alienated Naypyitaw, so Beijing had to turn to Thailand.

In terms of infrastructure development generally, Japan certainly has the edge on China. Japan has been actively integrating itself into Southeast Asian economies for decades, starting shortly after World War II. Southeast Asian manufacturing centers are critical to Japanese companies, which are some of the region's largest investors. For instance, nearly every Japanese car manufacturer has a presence in Thailand, which is the seventh largest exporter of automobiles worldwide.

Japan has built numerous transportation infrastructure projects in Cambodia, Laos, Thailand, and Vietnam. In January 2014, Japan granted more than \$320 million in official development assistance to build expressways in Vietnam. In March 2015, Japan pledged \$150 million to Cambodia to expand a major highway.

In contrast with Japan, China is a relative newcomer to building regional infrastructure projects. Only in the last decade or so has China finally begun to emerge from its temporary decline – it was, of course, previously a superpower for centuries. Beijing has marked its economic reemergence by beginning to build large international infrastructure projects in its backyard. Chinese projects are managed by state-owned enterprises (SOEs), are funded with government-provided loans, and are big, flashy, headline-catching ventures.

Nuanced Approach

Japan follows a much more nuanced approach. There are many implementers from various sectors that advance Japanese interests. These actors include private Japanese companies, such as Mitsubishi, Toyota, Nintendo, and Sumitomo Mitsui Financial Group. They also include government entities and multilaterals like the Japan International Cooperation Agency, the Japan Bank for International Cooperation, and the Asian Development Bank (ADB). The railroad is just one component of a much larger Japanese plan that has been in place for many years.

As far as fostering a conducive environment in which to build infrastructure projects, at first glance it seems that China has the upper hand. In Washington, critics fear that the impending establishment of the Asian Infrastructure Investment Bank (AIIB) will facilitate Beijing's infrastructure projects in the region, leading to the geopolitical subordination of Southeast Asian countries.

In fact, the AIIB is still in its nascent stages and it is not yet ready to compete with the ADB, of which Japan is the largest shareholder. It's not even clear that the AIIB will someday overtake the ADB. For nearly 50 years, the ADB has proven its ability to develop large-scale infrastructure projects that are positively received in the countries where they are built.

At a recent gathering in Singapore, AIIB organizers announced that the bank will offer \$100 billion in loans for infrastructure investment in Asia. Shortly thereafter, Japanese Prime Minister Shinzo Abe responded: over the next five years, Japan will funnel \$110 billion into Asian infrastructure development projects, via the ADB and Japanese state agencies. The ADB is not simply sitting back and watching the AIIB grow. Rather, the ADB aims to expand its already well-established capacity and influence.

All this is to say that China does not yet pose a threat to Japan's preeminence as a developer of regional infrastructure. A more accurate description of what is happening is that China is just now entering the competition.

Compared to Japan's development model, China's state-backed projects are more politically driven, which presents a problem for their financial sustainability. Many Japanese projects have private backing by companies expecting to make a profit back in Tokyo. These companies are advancing economic integration in Southeast Asia because it helps their bottom line. China's political calculus is different, and it sometimes blinds it to economic realities. The pipelines that China recently built in Myanmar, for instance, have already encountered significant criticism and do not seem financially viable.

Moreover, Japanese projects are more resilient because they have a large number of financial backers. Although China's state-controlled approach has its benefits, it is very reliant on the political atmosphere in Beijing. The Japanese strategy, on the other hand, can withstand the shifting political winds and obstacles that face any particular implementer.

Perhaps Japan can take one lesson from Washington's fear of China's infrastructure projects: It is difficult for bystanders to understand the achievements of Japan's infrastructure development

in Southeast Asia. Japan is simply not very good at advertising what it has done there, at least to audiences in the United States. Maybe Tokyo does not want to broadcast its activity in the same flashy way that Beijing does. If, however, Japan wants to raise awareness about its successes, perhaps it should take a leaf out of Beijing's book and consider pursuing headliner infrastructure projects. These easier-to sell projects would also help Japan to justify its expenditures abroad at a time when it is grappling with serious fiscal problems.

Then again, Japan might want stick to its current model. It has worked well so far. China may one day pose a threat to Japan's dominance of infrastructure development in Southeast Asia. For the moment, though, Japan should not be overly concerned.