



# THE REVIEW OF INTERNATIONAL AFFAIRS

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BELGRADE, VOL. LXX, No. 1173, JANUARY–MARCH 2019

*Vladimir Grečić*

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FOR THE ECONOMY AND SOCIETY  
OF A LESS DEVELOPED COUNTRY

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ON DEVELOPMENT OF HOST ECONOMIES



THE INSTITUTE OF INTERNATIONAL POLITICS AND ECONOMICS

# The Review of International Affairs

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ISSN 0486-6096

UDK 327

VOL. LXX, No. 1173, JANUARY–MARCH 2019

## **Publisher**

Institute of International Politics and Economics,  
Belgrade, Makedonska 25

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BiFS doo, Books and Periodicals, Supilova 10  
11000 Belgrade, Serbia,  
Tel/fax: +381 11 20 84 229  
E-mail: [bfsbooks@sezampro.rs](mailto:bfsbooks@sezampro.rs)

**Printed by:** Donat graf doo, Mike Alasa 52, Beograd

The Review of International Affairs is included in ERIH PLUS (European Reference Index for the Humanities and Social Sciences) <http://erihplus.nsd.no/>



The Review of International Affairs is the leading journal of national importance, classified M51, according to the classification by the Ministry of Education, Science and Technological Development, the Republic of Serbia.

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Publishing of *The Review of International Affairs* is funded by  
the Ministry of Education, Science and Technological Development of the Republic of Serbia

# The Review of International Affairs

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Vol. LXX, No. 1173, January–March 2019

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UDK 327 ISSN 0486-6096

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## **THE IMPORTANCE OF SOCIAL REMITTANCES FOR THE ECONOMY AND SOCIETY OF A LESS DEVELOPED COUNTRY**

Vladimir GREČIĆ<sup>1</sup>

*Abstract:* It is known that foreign remittances are current private transfers from migrant workers residing in the host country for more than a year to recipients in their country of origin regardless of their immigration status. Transfers of migrants are defined as their net income of which a portion is transferred from the host country to the country of origin at the time of migration. Compensation of employees is the income of migrants who have lived in the host country for less than a year. Remittances play an important role in the economic development of the countries of emigration, individual households and businesses. However, it is relatively unknown that non-monetary remittances are also of great importance for the migrant countries of origin. The author of this article is focused on the importance of non-monetary transfers, which are known in the literature as well as socioeconomic and cultural contribution. This article is based on the concept of Peggy Levitt (1998) non-monetary remittances as well as the expansion of social norms, practices and social capital to and from the countries of origin of migrants; which means that migration involves the flow of ideas, knowledge, identity, and cultural values.

The article claims that the attitudes of migrants in their relationship with other social institutions such as the family and the state, help to understand better the specific contexts within the country of origin that may perpetuate or interfere with the networks of migrants, including the rapid emergence and consolidation of new networks. The author claims that the diaspora and migrants can play a key role in the development of the home country by the presentation of its rich and diverse experiences. Engaging the Diaspora in the development of the home country largely depends on it. Talented people remain an important component of the country and the enterprise's long-term competitiveness. Therefore, special attention is paid to the role of highly skilled and highly educated migrants.

*Key words:* migration, monetary remittances, non-monetary remittances, knowledge diffusion, development, Serbia.

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## INTRODUCTION

In the process of increasing economic interdependence and globalization across the world, the diasporas become a significant factor in the development. It is now widely acknowledged that as trans-nationalized individuals, groups and communities, the diasporas – with their accumulated financial resources, as well as acquired human and social capital – are capable of making significant contributions to the political and socioeconomic development of their home countries (African Diaspora Policy Centre, 2011). The diasporas can be an important source of trade, capital, technology and knowledge for the countries of origin and destination. International migration may be a powerful factor in the development process for both recipient and destination countries and opens up significant opportunities for the emigrants. In fact, the emigrants are the ones who benefit most from the process. When people are able to choose their place of residence with fewer restrictions, their human freedoms are increased, and they are allowed access, albeit selectively, to better living conditions (Alonso, 2011).

Recent research has shown that remittances play a huge role in developing countries' economy, individual households and businesses (Table 1). As for the remittances received, in addition to income from production, the households seek to spread these remittances across consumption and leisure. Otherwise, the reduction of steady labor supply in a country of origin leads to a decrease in income, but it is not enough to offset the additional resources from remittances. Therefore, the total household income increases in the presence of remittances which leads to an increase in the household in consumption, confirming the widespread belief that remittances help in poverty reduction and improves the living standard. According to the World Bank data, remittances are a more stable and reliable form of foreign exchange earnings in developing countries as compared to foreign direct investments (FDIs) or aid flows. They also serve to alleviate balance of payments and debt crisis that beset the economy of developing countries. In addition, remittances represent a potential stabilizing factor for the economy and financial development of the less developed countries. They also play a substantial part in the social aspect of the economic system, including education at all levels; they can allow for the payment of school and college fees and enable children to study at home and abroad.

Remittances are an important component of the local economy. They help individuals to invest in real estate sector, to invest in different kinds of equipment, to provide capital for starting new companies and embarking on entrepreneurial activities that could be seen as an improvement in the earning capacity of a migrant home country.

Therefore, remittances are very important and they involve large sums. According to the data of the World Bank (2018) “after two consecutive years of

decline, remittance flows to low and middle-income countries (LMICs) increased in 2017 by 8.5 percent, rising to \$466 billion<sup>4</sup>. Globally, remittances reached \$613 billion. Remittance flows rebounded in all regions in 2017: in Europe and Central Asia by 20.9 percent, in Sub-Saharan Africa by 11.4 percent, in the Middle East and North Africa by 9.3 percent, in Latin America and the Caribbean by 8.7 percent, in East Asia and the Pacific by 5.8 percent, and in South Asia by 5.8 percent.

Remittance flows to LMICs are projected to accelerate by 10.8 percent in 2018, to reach \$528 billion - a new record (World Bank, 2018a). Remittances are a major source of foreign exchange earnings in many LMICs and continue to be more than three times the size of official development assistance. According to the World Bank data, migrant remittances to Serbia increased in 2017 and 2018 by 12 and 26 percent, respectively, and reached \$4.5 billion in 2018 (Table 2).

According to a definition of Marko Pavlović (2017), migrant remittances are the monetary transfers made by migrants to their country of origin. Most remittances are personal cash transfers from a migrant worker or immigrant to a relative in the country of origin, but they can also be funds invested, deposited or donated by a migrant in the country of origin, or in-kind personal transfers and donations – transfers of skills and technology, as well as “social remittances”.

However, if we only focus on money at the expense of the people, objects, skills, and ideas that circulate within transnational social fields, our analysis of the migration – development nexus remains incomplete. Recognizing this, many scholars have taken up these facts and extended research on the importance of social remittances. The term “social remittances” was coined over fifteen years ago to capture the notion that, in addition to money, migration also entails the circulation of ideas, know-how, practices, skills, identities, and social capital also circulating between sending and receiving communities (Lacroix et al., 2016).

## **METHODOLOGICAL DIFFICULTIES AND LIMITATIONS**

There are three main methods of data collection on social remittances (Helgesson Sekei et al., 2014): (a) a literature review; (b) an online survey; and (c) in-depth individual interviews.

For this article, the relevant data are collected from both national and international publications and statistical sources. It should be noted that social remittances are even less understood and studied, and even harder measurable.

In Serbia, the researchers faced enormous lack of data on its emigrants and the diaspora, relevant to quantitatively analyze the diaspora business and investment impact. “There is no system and database that is specific, simple and used by all the institutions tracking investments, employment based on investments, diaspora

investments and the developmental impact of investments (FDI and DDI) on the local and national level“ (Pavlovic, 2017).

As regards the number of migrants and members of the Serbian diaspora, researchers usually use statistics of the major immigration countries such as the USA, Canada and Australia, as well as the EU. Unfortunately, the statistics of these countries are not always clear or accurate when it comes to immigration from Serbia. The main reason for this is the disintegration of the country, an ongoing process that had several cycles. Until 1992, the Republic of Serbia was one of the six republics of the Socialist Federal Republic of Yugoslavia (SFRY). During the period 1992–2006 Serbia went through several changes in its statehood status. After the disintegration of the SFRY in 1992, two former republics, Serbia and Montenegro formed the Federal Republic of Yugoslavia (FRY). In 2003, its statehood status changed once more with the formation of the State Union of Serbia and Montenegro. In June 2006, Montenegro became an independent state after a referendum, and Serbia likewise declared its independence on the 5 June 2006. In February 2008, Serbia's Autonomous Province Kosovo and Metohija declared its independence. These changes in the statehood status of Serbia have resulted in some confusion in the immigration statistics of many countries.

Studies on the relationships between diasporas and development in Serbia tend to quantify this relation by focusing on the economic aspects of remittances and their effects on the macro and microeconomic levels. A few studies investigated the socio-cultural effects of migration and their societal impact. Mirjana Bobic (2009), among other things, wrote that it was the examination of new and more complex possibilities towards performing the closer ties of the homeland with key persons and groups that live abroad and possess significant assets (economic, cultural, social), who are also willing to contribute to country's socioeconomic recovery, very important for Serbian society. The case of Serbia indicates that while the impact of financial remittances is positive, the impact of socio-cultural remittances is generally neglected.

Therefore, researchers should devote more effort to study the impact of socio-cultural remittances on Serbia. It is not enough to study only the flow of monetary remittances, but they should also pay more attention to the study of the impact of socio-cultural remittances which may play an important role, negative or positive, in reshaping societies (Zohry, 2017). Many migrants and returning migrants have gained knowledge and changed their attitudes and practices as a result of their exposure to other countries, and they are talking about their experiences to people in their community. These people are also human resources that can be used to spread information and make progress in terms of human development on issues such as education, health, livelihood, the environment or governance. They can be considered agents of change in society (Helgesson Sekey, 2014).

## **SOCIAL REMITTANCES AND SOCIAL CAPITAL – THEORETICAL CONCEPT**

Changes in political, social and economic contexts have drawn the attention of various non-state and state actors to the utility of remittances (Goldring, 2003). Governments even designed programs and policies to manage and attract remittances from successful migrants to enhance the entrepreneurial spirit and the welfare of communities of origin (Markley, 2011).

Peggy Levitt (1998) uses the term social remittances to describe the diffusion and circulation of different social practices and ideas into the migrants sending and migrants-receiving areas, which accompany the migration process. Noteworthy, while monetary remittances are usually conceived as unidirectional flows from host countries to the homelands of migrants, social and political remittances may be multi-directional (Goldring, 2003; Levitt and Lamba, 2011).

According to Mohamoud and Fréchaut (2006), social remittances represent ideas, practices, minds set, world views, values and attitudes, norms of behavior and social capital (knowledge, experience and expertise) that the diaspora mediates and transfers from host to home countries. There are at least four types of social remittances – normative structures, systems of practice, identities, and social capital (Levitt and Lamba, 2011). Peggy Levitt (2005) defined normative structures as “ideas, values and beliefs that include norms of behavior, notions about family responsibility, principles of neighborliness and community participation, and aspiration for social mobility“. They are related to ideas about gender, race, and class identity, principles and values of organizations, government and churches. Systems of practice are the actions shaped by normative structures. They encompass organizational practices, such as recruiting and socializing new members, goal setting and strategizing, establishing leadership roles, and forming interagency ties (Levitt, 2005). They also include how individuals delegate household tasks and how much they participate in political, religious and civic groups (Mohamoud and Fréchaut, 2006).

Eliza Markley (2011) is on the right track when she says “both values and norms on which social capital is based, and social capital itself were socially remitted“. Likewise, Bourdieu (1986), Putnam (1993, 2000) and Coleman (1988) understand social capital as a resource for collective action, consisting of social networks of civic engagement and associated norms that have an effect on the productivity of the community. A broader view of social capital includes the social and political environment that enables institutional norms to develop and shape the social structure (North, 1990). Social capital’s characteristics and its role in facilitating the circulation of values and norms between new lands and homelands have been described by Eliza Markley (2011). Features of social organisation are networks, norms, and social trust that facilitate coordination and cooperation for mutual benefit. Putnam (1995: 67) compares social capital to physical and human capital: “Whereas

physical capital refers to physical objects and human capital refers to the properties of individuals, social capital refers to connections among individuals – social networks and the norms of reciprocity and trustworthiness that arise from them“.

Levitt and Lamba (2011) argue that migrants' experiences from their home countries have a strong influence on how they settle into the new culture which, in turn, affects what they subsequently remit back home. For this reason, social remittances have to be understood through a transnational perspective. They argue that only by looking at changes and effects of other remittances in the home and host countries will not reveal how or why values, norms and practices travel within the transnational social space created by migrants.

According to Eliza Markley (2011) findings, recent studies suggested that contemporary immigrants did not sever their relationships with the home country. On the contrary, they forge and sustain multiple linkages with it. However, Peggy Levitt (2005) argues that immigrants are better understood as transmigrants, persons who live their lives in a transnational social space, and according to Glick-Schiller et al. (1995) develop identities configured in relations to both home and host countries. That means twenty-first-century immigrants belong to two societies simultaneously (Levitt, 2005). They become incorporated into the institutions and patterns of the daily life of the country in which they reside. At the same time, yet, they maintain connections, build institutions, conduct transactions, and influence local and national events in the countries from which they migrated (Glick-Schiller et al., 1995).

It should be noted that because of the phenomenon's vast expansion and tremendous complexity of modern diasporism, theories, analyses, and debates occur across various disciplines: law, political science, history, sociology, economics, philosophy, and anthropology. These debates concern almost every aspect of modern diasporism. The nature of diasporans' identity is important.

Basically, now there are two theoretical approaches to current diasporism. One approach – which is called “Transnational Communities” - views diasporas as imagined transnational communities, espousing deterritorialized identities and robustly influenced by post-modern, globalized, hybridizing processes, and economic developments. The main argument of this school is that diaspora entities lose their ties to their homelands and exist as independent communities in the new global environment. The second approach argues that because of their inherent ethno-national identities and deeply rooted connections to a real or imagined homeland reflected in the profile presented above, most diasporas cannot be viewed as pure transnational entities (Sheffer, 2003).

According to the explanation of professor Gabriel Sheffer (2003), currently, there is a growing awareness and understanding that diasporas are neither purely “imagined” nor utterly “constructed” communities. This is due to the fact that

diasporas' identities are intricate combinations of non-essentialist primordial, psychological/mythical, and instrumental elements. Over time the cultural and social identities of these entities may undergo certain adaptations to changing circumstances in both their hostlands and homelands, but the basic elements in their ethno-national identity remain intact. The most important facts are that ethno-national trans-state diasporas are not going to disappear in the foreseeable future, that their impact on almost all homeland and hostland societies and states is increasing, and that these developments occur despite hostility toward them and despite the fact that they are not dangerous entities. On the contrary, diasporas positively contribute to their hostlands and homelands (Sheffer, 2003).

Not all of the ideas and practices migrants send back to their homelands are well received. Much work suggests that social remittances shake up gender and generational dynamics in ways that benefit women (Levitt, P. and D. Lamba-Nieves, 2010). Social remittances can also challenge people's ideas about democracy and the rule of law. Finally, hi-tech professionals and entrepreneurs from developing countries not only send back new technology and skills but ideas about conducting business.

According to Orozco-Rouse (2007) findings, for many migrants, their first priority is staying connected to families and friends left behind. They do so by calling relatives, visiting home, and sending remittances. Emotional connections with the homeland are not limited to family ties, and migrants may also maintain their cultural identities by patronizing migrant businesses or purchasing nostalgic products from their countries of origin, such as tortillas, rum or spices. Social remittances are also harnessed collectively. Hometown associations (HTAs) allow immigrants from the same city or region to maintain ties with and materially support their places of origin. Therefore, a special type of diaspora engagement –hometown associations, also known as HTAs — are organizations that allow immigrants from the same city or region to maintain ties with and materially support their places of origin. At the same time, HTAs create a new sense of community among recent immigrants with similar backgrounds. They also represent a transnational identity rooted as much in the migrants' country of origin as in the migrants' adopted home (Orozco-Rouse, 2007). Members of the Serbian diaspora have not organized their HTAs so far.

Peggy Levitt and D. Lamba-Nieves (2011) suggest directions for future research. They propose that in order to help policymakers concerned about development, researchers need to uncover what determines how ideas and values travel and under what circumstances idea change contributes to behavioral and institutional change. Another question to resolve: when does local-level change in something like gender relations, for example, scale up to produce broader shifts in reproductive behavior and labor market participation? Scholars and practitioners either focus on what happens to immigrants once they arrive in a new place or what happens in the places where they come from. This artificial separation does not reflect migrants'

lives, nor does it allow policymakers to respond creatively to the challenges migrants face. Migration research needs to span migrants' origin and destination countries and go beyond economic considerations to include the social and cultural migration (Levitt, P. and D. Lamba-Nieves, 2011). The “migration-development nexus” perspective (de Haas, 2010; Kapur, 2010) or “migration-development inter-linkages” (Katseli, Lucas, & Xenogiani, 2006) are hardly appropriate for studying the social and cultural effects of migration within the enlarged EU.

### **SOME RESEARCH FINDINGS IMPORTANT FOR A LESS DEVELOPED COUNTRY**

The literature elucidates the complex relationship between the social infrastructure of transnational connections, remittances and their political implications. Scholars debates were in several ways: (1) by piloting innovative, interdisciplinary methods that reveal the role of networks in cultural circulation; (2) by bringing to light the legal and socioeconomic factors affecting *who* transfers what; (3) by beginning to untangle the complicated relationship between social remittance transfers and broader inequalities; (4) by explanation what contributes to social remittances' scaling up and out; and (5) by calling into question some of the epistemological assumptions underlying migration studies and the social sciences in general (Lacroix et al., 2016).

So far, transfers of norms have been found in various fields (Gubert, 2018): (a) health (with impact found on fertility); (b) family and gender issues (on the position and role of women); (c) political sphere (with changes in political attitudes between migrants and their left-behinds, higher demand for political accountability, etc.).

How to actively engage the diaspora in supporting the institutional and policy changes in Serbia remains a key question. The diaspora needs to be engaged to move its activities to Serbia, that is, its production and operations. When “landing” in Serbia, its interest will be to show all the potential and capacities the Serbian market and the economy have and need. This process is currently underway in Serbia, but not enough to bring about a substantial “developmental push”. The country needs a developmental push forward from the private sector, from the innovative, technology-driven, business-driven diaspora enthusiasts coming home (Pavlović, 2017). One of the key issues in engaging the Serbian diaspora is the lack of understanding of the diaspora as an individual and collective actor, and differentiating the diaspora from the regular foreign investors, business and education actors. By assessing the empirical evidence, Pavlović (2017) has identified the diaspora's developmental role. The returning diaspora and transnational companies (home and away) are pushing for a strong change in the domestic economy. Overachieving returnees have a clear goal in developing their companies based on the pillars of knowledge learned abroad. Usually, they build companies

step by step, from a group of returnees or a group of pioneers. The thing that is specific to these companies is the pattern of fast expansion. In a couple of years, a very large percentage of these companies expands drastically and becomes successful (Pavlović, 2017).

The strategy of preserving and strengthening the ties of the home country and the diaspora, as well as the home country and Serbs in the region from 2011 has opened the possibility of engaging the diaspora in the transfer of knowledge, with the aim of learning from scientists from abroad and transforming the home country. However, action plans for each of these areas have not yet been developed. What we are missing in this is a creative strategic approach. Still no answer to the question of how the diaspora could be connected and coordinated with institutions (government support), business (capital) and universities (knowledge) that allow the creation of a competitive economy and the modern state. This certainly affects the process of connecting and cooperation between the home country and its diaspora.

Considering the possibilities of hiring talents from abroad for the overall development of Serbia, there were several conclusions. First, the time in which we live implies the necessity of engaging career accomplished and talented people from abroad (overachievers) to accelerate economic, social and cultural or any other development in Serbia. In order to realize this need, it is necessary to create a favorable environment for such developments - as voluntary “migrations are the cause and consequence of globalization, and its effects on the country of origin depend on internal factors in the home country” - by building relevant capacity to attract talents. Second, without the proper functioning of the competent state institutions, it is hardly possible to ensure the success of any joint project of the diaspora and the mother country. On the other hand, the civil sector and the media should have a significantly greater role in attracting talents from abroad to the home country. Third, the competent national authorities should initiate the creation of cooperation projects of the home country and the diaspora, since they have the best insight into the needs and scarce capacity for the development of Serbia. Fourth, the science and technology parks (STPS) of Serbia have a reasonable chance of a significant shift in the initiation and implementation of joint projects, STPS workers and their counterparts from the creative diaspora. After a long waiting, Science and Technology Park in Belgrade published a call for members of the Serbian scientific and technological Diaspora, inviting experts, primarily from the IT sector, but also from other areas for cooperation (details, <https://ntpark.rs/>).

Executive power in Serbia should reconsider its policy of institutional capacity building related to the promotion of cooperation with the Diaspora, to evaluate their effectiveness and to create new forms of engagement and methods suitable for building closer ties with the Diaspora in today's global society. The competent authorities should pay greater attention to the academic, professional and

entrepreneurial networks and associations in the Serbian diaspora to encourage their self-organization and cooperation with the mother country. Strategy for Cooperation with Diaspora should be adequately implemented and where needed upgraded to increase the contribution of the Diaspora intellectual development of their home country.

In Serbia, there is no sufficiently developed awareness of the importance and potential of the Serbian Diaspora, not only among ordinary citizens but also with the authorities. The policy towards the diaspora includes the harmonization of the various aspects of development and conflicting motives contained in the programs of relevant ministries. Expedient resolution of such conflicts requires a political will and commitment. Key assumptions necessary for the acceptance and implementation of the concept of a new policy towards the Diaspora, as well as for the successful achievement of the concept is a broad political and social consensus. In addition, strong political will and public support are the most immediate success factors.

Therefore, special attention and adequate activities of public authorities, businesses - especially chambers of commerce, as well as the media, is needed to raise awareness among the people but also in the executive and legislative authorities that without investment in research and development and in innovation in all fields and even in politics, there is neither progress nor increase of the competitiveness of the Serbian economy.

Therefore, international migration can improve institutions through several direct and indirect channels: (i) the transfer of political norms; (ii) voting from abroad; (iii) financial remittances; (iv) return migration; and (v) lobbying activities from abroad (Lodigiani, 2016). At the macro level, recent key studies consider the overall impact of emigration on institutional quality and discuss the possible effects through which emigration may affect institutions in the home country, but without disentangling those effects. In contrast, the micro literature focuses on one specific country and investigates more thoroughly the channels through which emigration may affect institutions (Lodigiani, 2016).

## **CONCLUDING REMARKS AND LESSONS LEARNED**

Remittances are not the only channel through which migration affects development. Less obvious are the social remittances that migration brings by increasing trade flows and facilitating the transfer of skills, knowledge, values and innovation (United Nations, 2012). Diaspora groups, often consisting of several generations of migrants, can be particularly effective due to their connections to and knowledge of both sending and receiving countries. Furthermore, migrants play a key role in promoting economic dynamism in the countries in which they

work, often filling labour and skill gaps. In the light of demographic changes in much of the industrialized world, the role of migrants will become increasingly important to fill specialized high-skill positions, as well as meet additional labour needs, for instance in the health and human care sectors. Furthermore, some research suggests migrants may have more “entrepreneurial spirit” than native-born. While the emigration of highly skilled workers (often referred to as “brain drain”) can have negative implications for the development efforts of small developing economies, particularly in crucial sectors such as health and education, recent research has shown that the migration of highly skilled workers can have benefits for both sending and receiving countries, even more so with effective policy measures and enabling environments (United Nations, 2012).

There is evidence that emigrants from the developing world do affect the economic, political, and social institutions in their home countries. Emigrants can directly affect the political institutions in their home country without returning home (Landgrave and Nowrasteh, 2016). Improved institutions can help jump-start economic growth in poor countries. Emigration can improve the quality of political institutions in origin countries through several channels. The first is by encouraging domestic elites to liberalize institutions to retain skilled workers. The second is by easing the international flow of ideas through social remittances and direct engagement by return migrants (Landgrave and Nowrasteh, 2016). In other words, the existing literature shows the importance of international migration acting as a political agent working to shape institutions in the country of origin. Whereas macro studies show the positive global effect of emigration, micro studies try to disentangle the channels through which migrants can become important in shaping political outcomes in the place of origin. Even if more research is needed to clarify the mechanisms and effects of international migrants on political outcomes at home, it is recognized that they could be important agents of democratization (Lodigiani, 2016).

Thus, policymakers should take into account that migration policies, both at the origin and the destination, may promote the role of migrants as transnational political agents. Home countries can favor migrants’ political participation by allowing external voting. At the same time, host countries can help to support the organization of external voting. International organizations could also play an important role in implementing voting programs from abroad, especially following post-conflict elections (Lodigiani, 2016).

The Serbian practice of engaging the diaspora needs to move beyond the weak institutional context (a chronic lack of finances, specialized employees focused especially on engaging the diaspora, supporting events and institutional cooperation). An integral framework allowing for the cumulative action, efficiency and success of all the institutional actors from embassies to local municipalities would be an important step forward (Pavlović, 2017).

The main pillars of the long-term development of Serbia should be: (a) *better use of talents*: retention of professionals in the country and attracting talents from abroad who are carriers of innovation and contribute to increasing competitiveness; (b) *adequate institutions*: completion of building institutions that will ensure the realization of the objectives of the Europe 2020; (c) *adequate human capital management*: extension and implementation of the strategy of cooperation with the Diaspora and development of concrete cooperation projects “at a distance”. From the profiled and competent experts in the Diaspora is expected that, in addition to knowledge, they bring to the home country “entrepreneurial spirit, contacts and initiative.” Creation of a powerful diaspora “searching network” requires time, patience and institutional capacity.

Generally speaking, each member of the Serbian diaspora is undoubtedly important for their home country. However, when it comes to development, especially economic, and in the area of cooperation with the Diaspora, innovators who are holders of technology development which increases the productivity and competitiveness of any economy, are a special target group for decision-makers in Serbia who should be more serious regarding overachievers from the diaspora. The success of the cooperation between the intellectual diaspora and the home country largely depends on the home country, its will, commitment and adequate measures to promote such cooperation.

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## Annex

Table 1: Possible effects of brain drain on (developing) home countries

Effect types/ Processes	Adverse	Beneficial
Knowledge and human capital	Shrinking human capital base	Brain gain
	Less innovation	Transfer/sharing of skills/technology
	Negative impacts on various, especially health and education	Diaspora knowledge networks
	Brain waste	Accumulation of broader/deeper knowledge/skills/experience
Macroeconomic Processes	Slower economic growth	Returnee entrepreneurship
	Declining high-skill labour Externalities	
	Lower productivity growth	
	Less entrepreneurship	
	(Fiscal) cost of educating highly skilled persons	
	Foregone taxes paid by highly skilled persons	
Flows Trade/ capital	Changing relative resource endowments away from skills	Remittances
		Diaspora savings: bonds, deposits, loans, funds, etc.
		Diaspora effects and business networks
		Creation/strengthening of business flow: merchandise and services (e.g. tourism)
		Creation/strengthening of businesses funded through foreign direct investment
Institutional Processes	Lower supply of/ demand for institutions	Diaspora assistance in/pressure for institution-building
		Returnee supply of/demand for Institutions

Source: Helgesson Sekei, et al., 2014: 21; UNCTAD, 2012.

*Table 2. Migrant Remittance Flows to and from Serbia, 2007-2017 (US \$ million)*

	Migrant remittance inflows	Migrant remittance outflows
2007	3,765	129
2008	3,544	180
2009	4,648	153
2010	4,118	155
2011	3,960	204
2012	3,549	218
2013	4,025	255
2014	3,696	267
2015	3,371	245
2016	3,205	239
2017	3,587	273
2018(a)	4,552	...
Total 2007-2018	46,020	2,318

(a) Estimate

*Source:* World Bank, Annual remittance data (updated as of December 2018).- estimate online.

## **ZNAČAJ NE-MONETARNIH MIGRANTSKIH DOZNAKA ZA PRIVREDU I DRUŠTVO JEDNE MANJE RAZVIJENE ZEMLJE**

*Apstrakt:* Poznato je da devizne doznake predstavljaju tekuće privatne transfere od radnika migranata koji žive u zemlji domaćinu više od godinu dana, bez obzira na njihov imigracioni status, primaocima u svojoj zemlji porekla. Transferi migranata se definišu kao neto zarade migranata čiji se deo prenosi iz zemlje prijema u zemlju porekla u vreme migracija. Nadoknada zaposlenima je prihod od migranata koji su živeli u zemlji domaćinu manje od godinu dana. Doznake igraju važnu ulogu u privrednom razvoju emigracionih zemalja, kod individualna domaćinstva i preduzeća. Međutim, manje je poznato da su ne-monetarne doznake od velike važnosti za zemlje porekla migranata. Središte pažnje autora ovog članka je usmereno na važnost ne-novčanih transfera, koji su poznati u literaturi kao socio-ekonomski i kulturni doprinos. Ovaj članak se oslanja na koncept Peggy Levitt (1998) ne-monetarnih doznaka kao širenje društvenih normi, prakse i društvenog kapitala prema i iz zemalja porekla migranata; što znači da migracija podrazumeva i protok ideja, znanja, identiteta, i kulturnih vrednosti.

U članku se tvrdi da će stavovi migranata u njihovom odnosu sa drugim društvenim institucijama, kao što su porodica i država, pomoći da se bolje razumeju specifični konteksti u okviru zemlje porekla koji mogu ovekovečiti ili ometati mreže migranata, uključujući i brzu pojavu i konsolidaciju novih mreža. Autor tvrdi da bi dijaspora i migranti mogli da igraju ključnu ulogu u razvoju zemlje, stavljanjem u službu matičnoj državi svoja bogata i različita iskustva. Angažovanje dijaspore u razvoju matične države u velikoj meri zavisi od nje same. Talenti ostaju kao važna komponenta za zemlju i preduzeća u pogledu dugoročne konkurentnosti. Stoga, posebna pažnja je posvećena ulozi visoko-obučanih i visokoobrazovanih migranata.

*Ključne reči:* migracije, novčane doznake, ne-monetarne doznake, difuzija znanja, razvoj, Srbija.

*Received: 12 March 2019*

*Accepted: 4 April 2019*

UDC 341.71(497.15)

327(497.15)

Biblid 0543-3657, 70 (2019)

Vol. LXX, No. 1173, pp. 24–44

Original paper

## **(UN)SUCCESSFUL ENFORCEMENT OF DEMOCRACY: THE CASE STUDY OF THE HIGH REPRESENTATIVE IN BOSNIA AND HERZEGOVINA**

Natalija SAVIĆ<sup>1</sup>

**Abstract:** The peculiar case of a strong and powerful international presence in Bosnia and Herzegovina embodied through the institution of the High Representative, as well as its impact on democracy has already been approached from various perspectives. However, some questions still remain, most notably those concerning one of the fundamental and necessary elements of democracy – the effective power to govern in the hands of the elected representatives. Focusing on this issue, the article attempts to provide an answer to two questions: firstly, what were the implications of arbitrary imposition of decisions by the High Representative for the effective power to govern of the elected representatives and secondly, why is the effective power to govern in the hands of the elected representatives a crucial component for successful functioning of democracy in Bosnia and Herzegovina? By relying on the theory of Embedded democracy by Wolfgang Merkel and methodology based on the understanding and measurement of power by Max Weber and Robert Dahl, the author seeks to contribute to current debates about democracy and democratic consolidation in post-conflict societies. However, he also tries to assess the implications of the use of the Bonn powers and the arbitrary imposition of decisions by the High Representative on the effective power to govern by the elected representatives and explain the reasoning behind the very idea of governance by the elected officials for the successful functioning of democracy.

**Key words:** Bosnia and Herzegovina, international community, High Representative, state-building, democracy, the effective power to govern, elected representatives.

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## INTRODUCTION

The four-year war on the territory of Bosnia and Herzegovina was officially brought to an end in the Wright-Patterson air force base near Dayton, Ohio, the United States on 21<sup>st</sup> November 1995 with the reaching of *the General Framework Agreement for Peace in Bosnia and Herzegovina (GFAP)*. It is known as the Dayton Agreement, officially signed in Paris on 14<sup>th</sup> December, which provided the framework for the future state structure of Bosnia and Herzegovina. This Agreement strongly advocated and supported by the international community, mainly the USA and the EU member states, proposed the model of ethnically based power-sharing between three major ethnic groups - Serbs, Croats and Muslims. At this point, this was considered the only possible institutional arrangement which could ensure their democratic legitimacy as well as peaceful coexistence and preserving the fragile peace (Josef 2013, p. 218). The agreement created two entities with essentially different internal setup – the Republic of Srpska, with a strong central authority, and the Federation of Bosnia and Herzegovina, with a federal government and internal division into 10 cantons. Interestingly enough, internal institutional systems of the Entities allowed them to act as practically sovereign states, but their wartime constitutions, in the end, became incorporated into the Dayton Agreement and together with the Constitution of the state of Bosnia and Herzegovina currently represent an essential part of the complex constitutional framework (Ibid, p.288).

The agreement itself is a rather complex document, consisting of two parts (military and civilian) and 10 Annexes, each of them dealing with a particular issue relevant for the new state and its post-war context. This is all the more important bearing in mind that this agreement was ‘unlike any other peace treaty of modern times, not merely because it was imposed by powers external to the conflict, but because of the far-reaching powers given to the international community’ (Chandler 2000, p. 43). Related to the issue of democracy, Annex 4 foresaw that Bosnia and Herzegovina is to be “a democratic state, which shall operate under the rule of law and with free and democratic elections”<sup>2</sup>. In order to achieve this, the international community in Annex 10 devised an institution which would supervise and monitor the process of implementation of the civilian part of the Agreement - the Office of the High Representative (OHR). This institution should fulfil the objectives of international involvement, one of them being ‘to establish and guarantee the irreversibility of democracy and to thus prepare the country for self-government’ (Dimitrova 2005, p. 44). Although its authority was more or less symbolical in the political sphere in the first two years, this severely changed in December 1997 during the meeting of the Peace Implementation Council (PIC) in Bonn, Germany. At the

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<sup>2</sup> *Annex 4* Article I (2) to the GFA, 35 I.L.M., p. 118.

meeting, the so-called ‘Bonn powers’ were promulgated and the PIC welcomed the OHR’s ‘intention to use its final authority in theatre regarding interpretation of the Agreement on the Civilian Implementation of the Peace Settlement to facilitate the resolution of difficulties by making binding decisions, as he judges necessary’ (PIC 1997). This uncontrolled freedom of interpretation of the situation has created unprecedented consequences for political development in Bosnia and Herzegovina. Moreover, each OHR has been more ruthless in the exercise of the Bonn powers than its predecessors. It is considered that the number of legally binding decisions imposed by the OHR has practically doubled in just a couple of years, from 242 during the mandate of Wolfgang Petrich to 430 under the rule of Lord Paddy Ashdown (Franić 2013, p. 50), strongly affecting undergoing democracy-building.

During its first years, the international actors led by the OHR have ‘loudly professed to work for the installment of peace and democracy’ (Dimitrova 2005, p. 57) in Bosnia and Herzegovina. However, the results have been rather ambiguous, which is why it is of utmost importance to explore whether the internationally advocated Bonn powers and their exercise by the OHR have managed to fulfil this goal. From today’s perspective, this will provide an insight into the period of a quite intense international presence and exercise of powers by the representatives of the international community compared to the current relatively silent one, but with growing domestic voices for its final termination which might leave democracy in Bosnia and Herzegovina for the first time fully in the hands of its main actors.

### **THEORETICAL CONCEPTS: STATE-BUILDING AND DEMOCRACY**

Approaching democracy in Bosnia and Herzegovina is a rather challenging attempt due to its complexity and ambiguity. Indeed, Bosnia and Herzegovina as a state presents a unique case in the international community. Therefore, to understand why one has to rely on the theory of state-building first which can provide some answers.

Theory of state-building presents a sort of a roof theoretical basis for understanding the phenomenon of international intervention in the first place. According to this theory, state-building is an externally driven process which deals with three main aspects: security and peace, economy and political sphere in order to create a viable state with sustainable and self-governing institutions. After the end of the Cold War and during the unstable 1990s in almost every corner of the world, this essentially political paradigm was particularly significant for the war-torn territories as well as weak and failed states where the international administration was set up in order to foresee the process from scratch (Caplan 2004, pp. 53–54). However, what distinguished it from the original form of internal state-building was the fact that it was almost completely driven by a neutral third-party. It was

considered that ‘one possible answer to the problems of building good governance/democracy, states and markets is a disinterested party to take charge simultaneously. The disinterested party should be able to see where the common good of a society lies and have no interest other than construction of an effective state’ (Robinson 2007, p. 14). In other words, it should be totally free from any kind of ideological bias or affiliation. Notwithstanding the very high number of employed international agencies, organizations and institutions which were dealing with various issues and aspects of state-building in Bosnia and Herzegovina, it could be said that the international presence was headed by the High Representative, legally incorporated into the Dayton Agreement, who transformed from the role of its guardian to one of its most vigorous enforcers.

State-building agenda in Bosnia and Herzegovina has attracted both support and praises as well as criticisms.<sup>3</sup> What, however, provides the basis for a mutual agreement between the two sides is the undisputed necessity for some kind of international presence and the fact that there are visible discrepancies between the theory and its implementation in practice. Issues which remain in the ‘gray zone’ are questions of legitimacy, accountability and (evaluation of) the effect of the international intervention in Bosnia and Herzegovina. According to Oliver Richmond, state-building has to be ‘more accountable, democratic and law-governed...than at present’ (Richmond 2013, p. 387), but that does not mean it should be completely revoked. It does, however, point to the intrinsic vagueness of the concept and its main components, one of them being democracy building and strengthening.\_

Understanding democracy presents a challenge of its own, due to the concept’s inherent intricacy and vagueness, but also because of various different definitions and theoretical perspectives approaching it. However, for the purpose of this research, the theory of *Embedded and Defective Democracy* by Wolfgang Merkel has been perceived as the most comprehensive one in terms of its explanatory power and postulates it provides for the extensive understanding of the issue in question. According to this theory, both internal and external embeddedness of a democratic regime should be achieved to provide for a stable consolidated democracy. However, only the factors of the internal embeddedness are considered to present the necessary preconditions inherent to the very concept of democracy. There are five of them: (1) electoral regime (2) political rights (3) civil rights (4) division of powers and horizontal accountability and finally (5) the effective power to govern (Merkel 2004). What is of particular concern for this research is the last one, namely *the effective power to govern*, which according to the author means ‘the necessity that the elected representatives are the ones that actually govern’ (Ibid, p. 41).

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<sup>3</sup> See e.g. David Chandler (2000), *Faking Democracy After Dayton*, London, UK: Pluto Press, pp. 154–181.

If this is not the case, then it presents a serious impediment to democracy. As Philippe Schmitter and Terry Lynn Karl argue, democracy is in danger if ‘state managers retain the capacity to act independently of elected civilians or even veto decisions made by the people’s representatives’ (Schmitter and Karl 1991, p. 9). Furthermore, they stress the necessity of self-governance by questioning the democratic character of the state system ‘if its elected officials are unable to make binding decisions without the approval of actors outside their territorial domain’ (Ibid). A similar conclusion has been reached by Juan Linz and Alfred Stepan who emphasize that a system cannot be considered democratic if ‘democratic institutions coexist with nondemocratic institutions outside the control of the democratic state’ (Linz and Stepan 1996, p. 15). These conclusions are connected to the understanding of the very nature of democracy which essentially means government for and by the people or, in line with modern developments, the governance of the elected representatives that derive their legitimacy from the people and are thus accountable to the people. Notwithstanding the significance of four other necessary elements and their interconnectivity for the development and consolidation of democracy, the Bonn powers have had the strongest effect on the right of the government officials to exercise their authority as legitimate representatives of the electorate.

Further on, the accountability of the elected representatives is an issue that requires to be at least a little more elaborated for the purpose of better understanding of the examples that will be explored. This aspect of democratic behavior is very significant for both its theoretical and practical implications. Theoretically speaking, I fully agree with the fact that ‘“people power” is the root meaning that provides the inspirational source of most understandings of democracy’ (Alexander and Welzel 2011, p. 271). In its essence, but also literally, democracy is a system of governance in which people should decide and, through the representatives they have elected, freely govern their lives. For the elected representatives, on the other hand, this means pursuing objectives which are in the best interest of those that elected them and responsibility for both success and failure in pursuing these goals. Some authors argue that the rules and conditions for the election of the representatives as well as their accountability to the people are precisely two features that distinguish democratic from non-democratic ones (Schmitter and Karl 1991, p. 5). However, the other side of the coin points to the fact that the same democratic norms and rules should also exist for the removal of the elected leaders from office. If they are elected by and accountable to the people, democratic mechanisms should also be followed in the opposite case - the dismissals from office. This is of particular significance for Bosnia and Herzegovina, which will be further elaborated in the empirical part of this research.

In order to conclude the theoretical approach of this research, it is important to address briefly two more issues. Firstly, it is crucial to take into consideration the

specific post-war context of Bosnia and Herzegovina. It is not a nation-state in the modern sense of the word, but rather a loose federation comprised of three ethnic groups with still disputed sovereignty due to the presence and exercise of the authority of the international community on its territory. From this perspective, it might not seem possible to apply the theory of embedded democracy in this particular case. However, the existence of the OHR has been agreed and accepted by the representatives of the internationally recognized Entities and incorporated into the framework of the Dayton Agreement (Banning 2014, pp. 262–263), just like their constitutions. The issue of legitimacy, nevertheless, remains acute since no referendum so far has been conducted in order to obtain the consent of the people (Karan 2012, p. 301). Anyhow, these arguments point to the fact that the OHR is a part of the system of Bosnia and Herzegovina based on the Dayton framework and therefore can be perceived as an undemocratic institution outside of the control of the elected representatives, but still coexisting with them in the same political system.

Secondly, I argue the very aim of the international presence has been precisely to assist in the creation of favorable conditions for the eventual consolidation of democracy. This can be understood from the wording of Annex 10 of the agreement<sup>4</sup> and was multiple times addressed even by the OHR itself. High representative Wolfgang Petrich has on one occasion stressed to the leaders and the citizens of Bosnia and Herzegovina that ‘this is their country, these are their problems, and they bear the primary responsibility for sorting those problems out’ (Knaus and Martin, 2003, p. 68). This implies the role of the OHR in the process of democratization and democracy promotion in Bosnia and Herzegovina. Its engagement, however, was not intended to be understood as an impediment to democracy, but quite the contrary, as assistance on the way of achieving it, leaving the decision-making process in the hands of the elected representatives. Still, without going deeper into the reasoning behind this decision, its influence has increased significantly since 1997 and its power of interpretation and implementation of the Agreement was confirmed by the Peace Implementation Council. The implications of these powers for the effective power to govern of the elected representatives will thus be examined and elaborated in the subsequent chapters.

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<sup>4</sup> *Annex 10* Article I (1) to the GFA, 35 I.L.M. p. 147 states that ‘the Parties agree that the implementation of the civilian aspects of the peace settlement will entail a wide range of activities including...*the establishment of political and constitutional institutions* in Bosnia and Herzegovina’, further declaring in the second paragraph that “the Parties request the designation of a High Representative...*to facilitate Parties’ own efforts*...’.

## THE EFFECTIVE POWER TO GOVERN: TRACING A METHODOLOGICAL ASSESMENT

If the main aim of this research is to explore the impact of the Bonn powers to the effective power to govern by the elected representatives, then the main question is how to approach this notion of the effective power to govern? How to understand it? What does it entail? Starting from the very beginning, it is possible to dissect this concept in two parts: *the effective power* and *to govern*. A causal linkage between them is quite clear - to have the effective power is a necessary precondition in order to be in the position to actually govern the state. This is of particular importance precisely because of the existing discrepancies between this theoretical aspect and reality. Questioning the effective power to govern of the domestic leaders in Bosnia and Herzegovina is hence also possible with all of its specificities, which was elaborated in more detail in the previous chapter. Here, however, I would like to approach this notion from a methodological perspective which will allow for the main questions of this research to be answered in a comprehensive and concise manner.

Therefore, it is important to define these two elements of the concept in order to leave out any possibility of future doubts about their meaning. Starting from the second element, *to govern* can be understood as governing the state, having legitimate authority over state issues or more concretely - being in control of the process of policy-making and administration. If perceived as the main objective and goal of various actors in the political sphere, what should be determined is who actually has the power to do so. Power, however, presents a rather obscure concept with a potential risk of various possible meanings attached to it and not even one that can be detected as the most correct one. This also presents a burden for the researcher, due to a large number of available theories for exploration. Under the necessity to make a clear and unambiguous decision for the purpose of the scientific utility of this research, my choices are Weberian understanding of the concept of power and Dahl's understanding of the means to measure and compare power.

Although considered to be primarily a sociological theory, Weber's theory of power is very much political in nature. Moreover, it is considered that "the very phenomenon of power is intrinsically linked to the definition of a modern polity" but also 'to our very understanding of many things political: the human as a political being, the origins of political action, the political aim of order and security from fear, and the sphere of government' (Guzzini 2017, p. 97). Power seems to be inherent to the very essence of the political system, being the final goal of permanent competition between various actors in society. However, the sociological side of this theory can be best observed from his definition of power. According to Weber, power means 'within a social relationship, every chance (no matter whereon this chance is based) to carry through the own will (also against resistance)' (Walliman 1977, pp. 232-233). And although his original apprehension rests

primarily on the relationship between individuals, I argue that this understanding can be wider considering other actors in the society. This is the point in which Dahl's conceptualization and operationalization of power steps in.

For Robert Dahl, power is more a practical tool than a theoretical concept with a 'higher' meaning. Albeit sometimes disputed, the usefulness of his theory precisely relies on its practical use and the possibility of empirical verification. Dahl understands power as a device in the process of decision-making, which can be in the hands of various actors depending on their prevalence in different policy areas (Guzzini 2017, p. 98). In his *Concept of Power*, Dahl (1957) argues several things: firstly, that actors in a relationship of power do not have to be only individuals but can also include groups, offices and governments, even nation-states; secondly, he provides for a clear methodology of assessing power, namely (a) the *base* of power, understood as the source or domain of power, such as opportunities, acts and objects which are passive and thus have to be exploited (b) the *means* of power, perceived as the instruments of exploitation (c) the *amount* of power, grasped as its extent, and (d) the *scope* of power, considering the responses of those influenced by it; thirdly, he states two necessary preconditions for a power relation to exist in the first place (1) a time lag between the actor who exercises power and the respondent and (2) a connection between the actor and the respondent; and finally, the means of assessing power can also be used for power comparison between different actors in society (pp. 203–206). However, Dahl also argues, albeit with much less certainty, that there should be 'a successful attempt by A to get *a* to do something he would not otherwise do' (Ibid, p. 204). I argue that this does not necessarily have to be the case in every situation, precisely because if *a* (respondent) does not act due to fear, for example (a decision not to act is also an act of some sort) or rebels against the decision of A (actor), but A still continues with its own decision, then it is quite obvious that A has power, albeit more in a Weberian sense. In spite of the above-mentioned obscurity of the concept which can present a potential risk, the liberty of interpretation of concepts or at least some of their elements should exist in order to provide for the possibility of their empirical usage. Even Dahl points to this when he states that 'the particular definition one chooses will evidently have to merge from considerations of the substance and objectives of a specific piece of research, and not from general theoretical considerations' (Ibid, p. 207). Accordingly, the purpose of this research points to a necessity of a 'methodological mix' in order to achieve the results which will be of high scientific value and significance.

The work of the OHR, especially during the 'Bonn period', has been quite extensive which is why it seems to be more practical to focus on some key aspects and decisions that had a lasting impact on state structure and democracy in Bosnia and Herzegovina. Therefore, empirical research will consider three aspects: (1) the emergence of the Bonn powers, their legal basis and background, and their

subsequent development depicted in (2) the discretionary removal from office of the elected representatives, probably the most notable expression of the denial of their power to govern democratically, and (3) policy shaping, such as the case of police reform, which was practically dictated by the OHR. These cases are chosen as the representative examples of the two powers that marked the Bonn period: the power to impose laws and the power to dismiss any public official from office (ESI 2000, p. 26). They will not only demonstrate the effect of the decisions of the OHR but also how its powers changed during time. The elaborated methodology will be applied to these concrete examples and the power of the OHR over and vis à vis the elected representatives and their power to effectively govern the state will thus be empirically examined.

## **EMPIRICAL RESEARCH: THE BONN POWERS AND THEIR PRACTICAL IMPACT**

### **The Bonn powers: their emergence and the ‘Transmitter war’**

The period of the Bonn powers has certainly been the period during which the international community headed by the OHR has left the lasting traces on political system and democracy of Bosnia and Herzegovina. During this period, the OHR has deeply penetrated in all pores of the political system of Bosnia and Herzegovina shaping it not only from the outside but also from the inside, leaving visible marks on its functioning as we know it today. However, to fully understand the implications of the Bonn powers as well as their significance, it is important to trace back the roots for their adoption in the first place.

A crucial moment came in December 1997 during the meeting of the Peace Implementation Council in Bonn, Germany, where the annual strategic review had taken place. This, however, was not the only meeting of such character. Formally speaking, the powers of the international community have been amended in several meetings of the PIC, most notably at conferences in Florence in 1996, Paris in 1996, Sintra in 1997, Bonn in 1997 and finally Luxembourg in 1998 (Chandler 2000, p. 53). Still, the Bonn meeting in 1997 is remembered precisely because of the fact that this was the conference in which the PIC issued the famous and frequently cited statement in the ‘Bonn conclusions’. The officials adopted the document, whose wording was used by the OHR as a legitimate but also as a legal basis for the use of its powers. In the Bonn conclusions, the PIC (1997) stated that:

‘The council welcomes the High Representatives intention to use his final authority in theatre regarding interpretation of the Agreement on the Civil Implementation of the Peace Settlement in order to facilitate the resolution of difficulties by making binding decisions, as he judges necessary, on the following issues: (a) timing, location and chairmanship of meetings of the common

institutions; (b) interim measures to take effect when parties are unable to reach an agreement, which will remain in force until the Presidency of the Council of Ministers has adopted a decision consistent with the Peace Agreement on the issue concerned; (c) other measures to ensure implementation of the Peace Agreement throughout Bosnia and Herzegovina and its Entities, as well as the smooth running of the common institutions. Such measure may include actions against persons holding public office or officials who are absent from meetings without good cause or who are found by the High Representative to be in violation of legal commitments made under the Peace Agreement or the terms for its implementation.’

One thing seems to be quite obvious from this text, and that is the very wide discretionary power of the OHR. What is even more astonishing is the fact that the OHR itself was not only the interpreter of the Agreement but consequently of its own authority and powers. This is important to emphasize for the purpose of tracing the legal background of these powers, which indeed do present a controversial case in international law due to the fact that there is no solid legal basis for their adoption. Although the OHR has frequently stated that these powers were delegated to it by the PIC, there are strong arguments suggesting this was not even possible due to the fact that there is no principal-subordinate relationship between them. And even if it were, the sessions of the PIC which is not even mentioned in any regard in the Agreement, are chaired by the OHR which points to an opposite direction of influence from the one necessary to exist in order for these powers to be delegated in the first place, making this relation far more complex from a legal basis for such a simplified statement (Banning 2014, pp. 293–296). Tim Banning even goes further arguing that this ‘must be seen as a tragic form of wishful thinking of the OHR’ (Ibid, p. 296). Additionally, the position of the institution of the OHR in the political system of Bosnia and Herzegovina has been accepted by the Constitutional Court, which has argued that the OHR by intervening in the political system in a particular case represents a substitute for domestic authority, therefore, acting as the authority of Bosnia and Herzegovina (Franić 2013, p. 48). Whatever be the case, there is no doubt that this resulted in ‘the ceding of...policy-making powers to Bosnian institutions...now to be dependent on a broad range of “benchmarks” to be determined by the international institutions themselves’ (Chandler 2000, p. 55).

Even the situation behind the decision of the PIC to promulgate the Bonn powers serves as an interesting case for analysis from the standpoint of power. The crisis, which became known as the ‘Transmitter war’, culminated in May 1997 when the international community was advocating for the independence of the media in the Republic of Srpska. At that time, the media was in the hands of the Pale fraction, close associates of Radovan Karadžić, the war leader of the Bosnian Serbs. This period has been openly described by the spokesman of the OHR as the time of

‘deliberate misinformation, inflammatory commentary, insulting language and highly based reportage’ (ESI 2000, p.24), all the result of the high level of political control over the media. Consequently, this crisis was one of the main topics of discussion of the Steering Board of the PIC in Sintra, when the OHR was encouraged to take all the necessary measures to ensure the enforcement of the Agreement. The letter of the OHR sent to Momčilo Krajišnik, the chairman of the board of Serbian Radio and Television (SRT) and member of the Presidency of Bosnia and Herzegovina, represents a good depiction of the rising power in the hands of this institution – he stated that ‘all this must stop – permanently... You should be quite clear that I will have the resources I need’ (Ibid, p. 25). Eventually, the transmitters were forcibly taken by the military forces, while the OHR put significant pressure on the members of the board of SRT, requesting their resignation as a condition for the return of the transmitters and in the end, ensuring the compliance of the Entities with the reform program of the media which would guarantee their neutrality and protection from political control.

Now, by applying suggested Dahl’s concept on power, we shall be able to draw the conclusion about the power of the OHR vis à vis the elected representatives in this particular case. First of all, the *base* of the power of the OHR can be clearly traced in the wording of the Steering Board of the PIC from Sintra, which declared ‘the High Representative has the right to curtail or suspend any media network program whose output is in persistent and blatant contravention of either the spirit or the letter of the Peace Agreement’ (Ibid). Moreover, the possibility to rely on military force presents a significant opportunity for the OHR to fully exercise its authority. This is precisely this passive source of power, as understood by Dahl, which has to be exploited to affect the behavior of others. Secondly, the *means* of power, in other words, the potential or actual use of the base, can be traced firstly in the open threat of the OHR to Momčilo Krajišnik, and secondly in the actual employment of the base, which is the holding down of the transmitters by the military forces under the request of the OHR. Thirdly, the *scope* of the power of the OHR is clearly seen in the compliance of the respondents, the resignation of the members of the board of SRT and acceptance of the suggested reform model by both Entities. Finally, the *amount* of power or its extent, which in this particular case is obviously very high if considered the probability that the respondents would not comply was far less possible than otherwise. All of this leads to a conclusion that the OHR has had power over the members of the board of SRT but also the elected representatives which, under pressure, had to accept something they otherwise would not, stripping them of their right to govern and decide by themselves. Finally, this case opened the door to the active use of the Bonn powers by the OHR in the political sphere for the next decade.

### **Appointments and dismissals of public officials**

From 1997 and the Bonn conference of the PIC, the so-called Bonn powers have become the instrument used almost daily by the OHR for the purposes of implementation of the Agreement and ensuring peace in Bosnia and Herzegovina. The argumentation behind this practice emphasized the need ‘to speed the process of democratization and enable a measure of international disengagement’ (Chandler 2000, p. 37). The irony lies precisely in the fact that the rather aggressive top-down approach of the OHR was deemed as necessary in order to achieve self-government and democracy in Bosnia and Herzegovina. However, with time this became a highly controversial matter due to the rather low effects of the mostly short-term solutions with questionable legitimacy and accountability issues.

The number of decisions by the OHR has significantly increased through the years following their endorsement - according to some accounts, their number rose from 29 decisions in 1998 to 158 decisions in 2004, the year which also represents the peak of its powers (Franić 2013, p. 48). The subsequent period was marked by the slow but gradual withdrawal of the High Representative from the political system, although this did not mean the complete abandonment of its proactive approach. Decisions were made about various issues, some of them regarding citizenship, foreign investment, import duties, flag, coat of arms and the national anthem of Bosnia and Herzegovina, vehicle license plates, common currency, privatization, witness protection and property legislation (ESI 2000, p. 27), all of which left a profound impact on the functioning of the Bosnian state. From a standpoint of democracy, the problem lies in the fact that these decisions should essentially be adopted by the elected representatives themselves through and as a result of negotiations on all levels, which would provide stable consensus for their implementation in the future and respect in practice. However, this was at times regarded as impossible by the OHR, which is why it has relied on its power to discretionally decide to remove the elected representatives if they were, according to his own subjective interpretation, violating or obstructing the implementation of the Agreement.

It has to be noted that the power of the OHR to appoint the representatives cannot and should not be regarded as necessarily bad at all times, considering the specific context of the post-war situation in Bosnia and Herzegovina which was still burdened with nationalist rhetoric and nationalist leaders who were holding key power positions even several years after the war. According to some accounts, it is considered that the institutions in which the international community has had influence over the appointment of the staff, have performed much better than those in which the staff has been appointed by the nationalist parties.<sup>5</sup> The same can be

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<sup>5</sup> An example of such an institution is the Federal Ombudsman, whose candidates have been selected by the Organization for Security and Cooperation in Europe (OSCE) (ESI 2000, p. 32).

said for the discretionary removals from office of the elected representatives, albeit this presents a more dangerous practice for the overall democratic climate and development of political culture in a highly dysfunctional society burdened by war memories. And although a certain number of those dismissed were indeed relying on nationalist and war rhetoric causing a potential threat for the stability of the post-war Bosnia and Herzegovina, many officials and elected representatives were still removed for rather vague reasons, such as the frequently used notion of representing ‘the obstruction to the implementation of the Dayton Agreement’. The number of dismissals has steadily increased since 1997, amounting to a total of 187 dismissals in more than a decade (Franić 2013, p. 49). This has affected officials on all levels, both local and cantonal as well as on the level of Entities and state. An illustrative example is the removal of Nikola Poplasen, the President of the Republic of Srpska in March 1999 for not accepting the majority government of Milorad Dodik after the parliamentary elections the year before. The OHR stated that President Poplasen has ‘abused its power, blocked the will of the people and...obstructed the implementation of the General Framework Agreement for Peace’ (OHR 1999). This decision consequently created more damage than benefit for the political situation in the Republic of Srpska, since the new president was not elected for more than a year, resulting in a new legislative decision of the OHR which stated that ‘when there is a vacuum in the RS Presidency...the signature of the RS President on the adopted laws is not required’ (OHR 1999a). This case serves as a useful example of both powers frequently used by the OHR – the power to dismiss public officials and the power to legislate. Moreover, it represents a blatant overriding of all rules and procedures of both appointments as well as accountability of the elected representatives to the electorate. It indeed is the manifestation of the power of the High Representative over the elected public officials, which undoubtedly shows that their mandates were, despite the common democratic practice, in his own hands and dependent on his own discretionary interpretation of their actions without any chance of legal appeal against it.

Applying Dahl’s model of power, a similar conclusion can be reached as in the first suggested example. The *base* of power of the OHR can be traced in the wording of the Bonn conclusions, more concretely part XI, point 2, article (c) which states that in order to secure the implementation of the Agreement, the High Representative may take ‘actions against persons holding public office or officials... who are found by the High Representative to be in violation of legal commitments made under the Peace Agreement or the terms for its implementation’ (PIC 1997). Consequently, the *means* of power is the potential or actual use of the base, which is the right to unilaterally decide to remove public officials from office or impose significant pressure on them by adopting sanctions or penalties, mostly of a financial character. The *scope* and the *amount* of power have been quite exceptional in these cases – there has been silent or almost no objection by the removed public officials.

The inability but also lack of legal or any other kind of possibility to react against the decisions of the High Representative points to the unquestionable and unchallenging power of this institution over the elected representatives in the political system of Bosnia and Herzegovina, stripping them once again of their legitimate and necessary effective power to govern.

### **Police reform and the dawn of the Bonn powers**

The reform of the police and the forces of public order represents probably one of the most important reform processes in Bosnia and Herzegovina. It is suggested that ‘the OHR has been more engaged on police reform than other issues’, which does seem to be understandable because the police have during the war served as ‘a key ethnic cleansing instrument’, and despite some improvements, continued to be ‘highly politicized’ in the years after the war (ICG 2007, p. 14). On the other hand, this case, compared to the ‘Transmitter war’, shows the slow but ongoing process of weakening of the Bonn powers of the OHR and growing resistance against its top-down approach regarding the imposition of laws and their enforcement.

The request for the police reform came from the European Union (EU) in 2004 for the purpose of bringing Bosnia and Herzegovina closer to European standards in this field. According to the European Stability Initiative (ESI), the EU left quite enough space for negotiations between the parties about the model to be adopted. There were three possibilities, ‘all in line with the best European practice’ and to be achieved through ‘the domestic ownership of the process’ (ESI 2007, p. 4), but this did not prevent the High Representative to once more interpret the situation unilaterally and take matters in his own hands. Only three days after the EU report, the OHR has made use of its Bonn powers and imposed a Police Restructuring Commission with a clear mandate – to achieve a centralized model of structure and control over police forces – and without a possibility for any further discussion (Ibid, p. 5). The OHR has once again taken the power to effectively govern the state from the elected representatives, i.e. the power to have full ownership of the process of decision-making, which is even more important in such a sensitive case.

However, there is a notable difference compared to the other two mentioned cases that passed rather smoothly and without voices raised against it. This process almost immediately came to a stalemate due to the open opposition coming from the government of the Republic of Srpska, which was against any kind of centralization or cross-entity police forces (Belloni 2009, p. 364-365). The situation continued for the next three years during which an important change occurred – the mandate of the international community and actions undertaken by Lord Paddy Ashdown, former OHR (2002-2006), were questioned by his successor Christian

Schwarz-Shilling (2006-2007) who openly called the actions taken by his predecessor a form of ‘colonization’ and argued that the authority of the High Representative should be exercised with a clear mandate and in clearly defined boundaries and situations (Franić 2013, p. 50). This paved the way for the gradual weakening of the powers of the OHR and finally opened space for stronger voices opposing its rather aggressive top-down approach.

Although the analysis of the international context in the second part of the first decade of the 2000s requires a separate detailed and exhaustive research, it has to be at least briefly noted that these years brought significant changes, with the focus shifting from Bosnia and Herzegovina to other important hotspots. Indeed, after more than 10 years from the Dayton Agreement, Bosnia and Herzegovina was considered a rather resolved question which on the other hand explains the loose interest of the international community in its internal affairs controlled and handled in large part by the High Representative. On a regional level, the diplomatic attention of the EU and other major players was turned to the issue of settling the final status of Kosovo to preserve the fragile stability of the region (Belloni 2009, p. 365). Globally speaking, however, the differences were much more profound – the continuous strengthening of NATO on one side and Russia and China on the other, together with rising tensions between them, best depicted in the antagonisms and eventual open armed conflict in Georgia (Bowker 2011, pp. 199-203), signified a major shift in the strategic priorities of these powers, thus leaving Bosnia and Herzegovina in the shadow.

Consequently, the process of reshaping the mandate of the international community and the High Representative simultaneously affected the blocked process of police reform. After Schwarz-Shilling, his successor Miroslav Lajcak proposed another deal to the parties. However, this was equally rejected by the government of the Republic of Srpska, headed by Milorad Dodik, who threatened that the representatives of RS would resign from their positions in state institutions if the High Representative was to use its powers to dismiss the elected representatives (ESI 2007, p. 7). And even though the OHR had to eventually rely on his powers to legislate due to resistance of representatives of the Republic of Srpska to comply amending Law on the Council of Ministers, which would allow for the decision to be adopted with a vote of only one member of the constituent peoples, the strong objection, in this case, brought concrete results – the High Representative had to accept a mild compromise which meant no cross-entity police regions and essentially a failure of the whole process (Belloni 2009, p. 365).

This example, however, from the perspective of power deviates from the previously suggested cases. Examined through Dahl’s concept of power we can see that the base and means of power have remained rather stable and in the same form as in the previous cases. The *base* of power is rather clear, established in the Bonn conclusions, part XI, article 2, point (b) which gives the right to the High

Representative to adopt interim measures effective immediately in the cases when there is no agreement between the parties. At the same time, the *means* of power is, as in the two previous cases, the potential or actual employment of the base, which in this case is the endorsement of a particular model of police reform by the OHR and creation of the Commission for its achievement. What is, however, different is the *scope* and *amount* of power – the decision of the OHR has produced open resistance rather than silent compliance and thus did not achieve the set goal, despite further unilateral decisions, which clearly shows how the responses of the respondents changed, consequently lowering the amount of power of the OHR or the probability of compliance of the respondents with his decisions. From Weberian perspective as well, it can be argued that the High Representative has lost its power over the elected representatives by not being able to exercise its own will against resistance and having to take it into account. Still, the fact that only the OHR itself was able to challenge its own powers shows their uncontested character which has had a huge impact on the power of the elected public officials to freely govern the state.

## CONCLUSION

The main focus of this case study has been on the implications of the Bonn powers of the High Representative on the effective power to govern by the elected representatives as one of the five major elements for stable and embedded democracy in one society, or more concretely Bosnia and Herzegovina. This has been elaborated on three presented examples: (1) the ‘Transmitter war’ (2) the dismissals from the office of the public officials and (3) police reform, as an example of one of the major reform processes started during the peak of the so-called ‘Bonn period’. However, these examples were chosen not only as representative cases of the two powers frequently used by the OHR – the power to legislate and the power to dismiss public officials – but also as cases which demonstrate the power of the High Representative in a particular period. The ‘Transmitter war’ was the very case which provided for the base for the promulgation of the Bonn powers in the first place and it can be seen as the first unequivocal expression of the OHR’s powers over the public officials; the dismissals from office of the elected representatives represent a practice that has been present from the beginning to the end of the ‘Bonn period’, albeit with different intensity, but can still be seen as a constant expression of the OHR’s powers; and finally, police reform, which is an example of a major reform project which coincided with the changed perception about the very mandate of the High Representative and open objection with its top-down approach and imposed solutions, presenting the beginning of the end, the slow but gradual weakening of its powers.

The presented methodology of Robert Dahl and his concept of power and its empirical assessment on these three examples have indeed shown that the High Representative has, with its exercised authority taken away the effective power to govern from the elected representatives and thus has impeded the development of democracy and self-governance in Bosnia and Herzegovina. As demonstrated, the High Representative did not hesitate to intervene when it deemed necessary, arbitrarily deciding when a breach of the Agreement has occurred and imposing solutions with immediate effect without leaving enough time for any kind of negotiations, let alone consensus among the interested parties. Additionally, it did not leave time or possibility for appeal or any kind of legal remedy against its decisions. This was the most salient in the first years of the Bonn powers but has changed during the time when it became visible that the effects produced were not always stable and persistent. It, however, left an indelible track on the self-governance in Bosnia and Herzegovina which was postponed and neglected for mostly short-term political objectives.

For the purpose of clarifying the argument, it might be useful to consider a rather comprehensive and coherent analysis of this very issue addressed by the Venice Commission of the Council of Europe already in 2005, which examined in detail both powers of the High Representative and their practical impact. And despite their recognized benefit and necessity at times, the Venice Commission concluded that ‘the democratic principle of sovereignty of the people requires that legislation is adopted by a body elected by the people’ which is automatically revoked ‘if legislation is adopted by another body’ (Venice Commission 2005, p. 22), more so if that body is highly undemocratic in character. Furthermore, the Venice Commission inferred that ‘the termination of the employment of a public official is a serious interference with the rights of the person concerned’, the same being in cases of the dismissals of elected representatives when ‘the rights of their voters are also concerned’, suggesting that it should be based on ‘serious grounds with sufficient proof and the possibility of a legal appeal’ (Ibid, p. 23). If an institution of such significance and prestige in the international sphere, especially in terms of setting the standards for democracy and the rule of law, comes to this kind of a conclusion, it certainly does point to the gravity of the involvement of the international community, embodied in the powers of the OHR in the political system of Bosnia and Herzegovina.

All in all, the aforementioned suggests that the arbitrarily imposed decisions of the High Representative were continuously taking away the power of the elected representatives to effectively govern the state. However, it is even more important to address now the question why this is seen as something necessarily detrimental to the stability of one political system and how does it affect the overall conditions for further democratic development in Bosnia and Herzegovina. Above all, this relates to the issue of the majorly distorted behavior of the elected representatives.

Removing the process of decision-making from the elected bodies and placing it in the hands of another non-elective body has resulted in high dependency of the elected representatives on some other source of power in society, in this case the OHR, which is making decisions on their account. It is true when stated that ‘the incentive of Bosnian politicians is to acquiesce quietly in international demands, rather than to develop an independent policy agenda’ (ESI 2003, p. 3) precisely because they are aware of the fact that their jobs and positions depend on their compliance with the suggested policy solutions coming from the High Representative. On the other hand, by favoring the so-called ‘moderate’ political actors while trying to discredit the nationalist ones, the OHR has either intentionally or unintentionally made them dependent on its own powers and less aware of their own responsibility. Furthermore, ‘if they are encouraged to believe that they enjoy unconditional support in their fight against nationalist parties, they have no need to engage in compromise and consensus-building with their political opponents’ (ESI 2001, p. 8) creating a vicious circle of dependency and ultimately no benefit for others than themselves. Therefore, only if the political candidates are left to freely compete with their opponents without some of them being favored by another outside body will they have the incentives to actually fight for the votes of the people and consequently, if they win, justify their political support with decisions made for the benefit of the electorate. Moreover, only then will they be able to have stable negotiating positions, allowing them to reach compromises and consensuses on issues of high importance for society. The decisions emerging from discussions involving political actors representing the majority of social strata will thus be stable, persistent and will ensure long-term solutions to the best interest of the voters. Finally, only if the composition of the post-conflict state is decided by the inhabitants of that state, thus ensuring the ownership of the peace process, only then its implementation will be successful (Von Hippel 1999, p. 204).

To conclude, this research has surely raised some new-old questions that ought to be explored in the future. One of them is the *legitimacy* of the powers of the High Representative, an issue that has been brought up several times but continues to present a pertinent matter for many scholars and academics. However, what might be interesting to see is the new aspect of research of the old problem. One possible way to approach it could be through Max Weber’s theory of legitimacy and authority, which may provide new insights into this subject. The same goes for the question of *accountability* of the international power structures in Bosnia and Herzegovina and its fundamental contradiction – while seeking to enhance accountability of domestic structures, they remain unaccountable themselves in many ways (Caplan 2005, p. 464). These two problems represent yet just another part of a much more complex puzzle. Nevertheless, their unquestionable importance points to the need to approach them in a comprehensive and coherent

way to achieve, together with this research, a complete and clear picture of the international presence and its powers in Bosnia and Herzegovina.

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### **(NE)USPEŠNO SPROVOĐENJE DEMOKRATIJE: ISTRAŽIVANJE SLUČAJA VISOKOG PREDSTAVNIKA U BOSNI I HERCEGOVINI**

*Apstrakt:* Jedinstvenom slučaju snažnog i moćnog međunarodnog prisustva u Bosni i Hercegovini, otelotvorenog kroz instituciju Visokog predstavnika, kao i njegovom uticaju na demokratiju je već uveliko pristupano iz različitih perspektiva. Ipak, neka pitanja još uvek ostaju, a pre svega ona koja se tiču jednog od fundamentalnih i neophodnih elemenata demokratije – efektivne moći upravljanja u rukama izabраних predstavnika. Fokusirajući se na ovaj slučaj, članak pokušava da pruži odgovore na dva pitanja: prvo, kakve su implikacije proizvoljnog nametanja odluka od strane Visokog predstavnika za efektivnu moć upravljanja izabраних predstavnika i drugo, zašto je efektivna moć upravljanja u rukama izabраних predstavnika ključna komponenta za uspešno funkcionisanje demokratije u Bosni i Hercegovini. Oslanjajući se na teoriju Ugrađene demokratije Volfganga Merkela i metodologiju baziranu na razumevanju i merenju moći Maksa Vebera i Roberta Dala, autor teži da doprinese aktuelnim debatama o demokratiji i konsolidaciji demokratije u post-konfliktnim društvima, ali takođe da proceni implikacije upotrebe Bonskih moći i proizvoljnog nametanja odluka od strane Visokog predstavnika na efektivnu moć upravljanja izabраних predstavnika, kao i da objasni razloge koji stoje iza same ideje o upravljanju od strane izabраних zvaničnika za uspešno funkcionisanje demokratije.

*Ključne reči:* Bosna i Hercegovina, međunarodna zajednica, Visoki predstavnik, izgradnja države, demokratija, efektivna moć upravljanja, izabrani predstavnici.

*Received:* 6 March 2019

*Accepted:* 2 April 2019

UDC 327(520:510)  
Biblid 0543-3657, 70 (2019)  
Vol. LXX, No. 1173, pp. 45–60  
Review paper

## HOW COULD JAPAN-CHINA RELATIONS BE STABILIZED?

Yoshikazu KATO<sup>1</sup>

*Abstract:* Japan-China relations enter a new “Two Giants” era, unprecedented in the history of East Asia. Multi-dimensional interdependence between Japan and China has been proceeding rapidly as one of the most positive factors in terms of pushing forward the bilateral relationship for the long run. However, emotions among the public from the two sides are problematic and uncertain, and it is crucial to investigate how to “normalize” people-to-people emotions. Contingency events, which tend to lead to inward-looking, and to narrow nationalism, always undermine Japan-China relations. The “Nationalization” crisis in 2012 is one of the typical cases from which the two nations should absorb the lessons deliberately. A lack of facts and truthful information, failure of diplomatic communication, simultaneously rising nationalism and declining governance capability and transforming power balance in the Asia-Pacific region created the crisis over the uninhabited islands. How Japan and China can overcome these dilemmas and manage the complicated bilateral relationship more effectively? Beyond continuously promoting multi-dimensional interdependence, the two sides have to establish channels and mechanisms of crisis management in order to avoid the bilateral relationship being constantly threatened by the occurrence of contingency events and rampant, irresponsible nationalism.

*Key words:* Japan-China relations, Diplomacy, Interdependence, Emotions, Contingency Events, Nationalization, New era.

## JAPAN-CHINA RELATIONS ENTER A NEW ERA

In the course of human history, East Asia has never faced a situation in which two strong, economically powerful nations have coexisted simultaneously. In the

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ancient era, China was one of the strongest powers in the world; during that extended time, Japan as the weaker side implemented tributary diplomacy toward China. China was strong, Japan was weak.

After the end of the Sino-Japanese War in 1895, Japan began to exceed China in the balance of power. The Meiji Restoration had prompted Japan to push forward with modernization, and eventually, China was defeated by Japan and subsequently failed in its Hundred Days Reform of 1898.

With Japan's rise and fall before and after World War II, both domestically and internationally, and especially after the collapse of the Cold War and the bubble economy in Japan, and China's acceleration of its Reform and Opening policy instituted by Deng Xiaoping in 1978, East Asia seems to have gradually but explicitly entered what might be called a "Two Giants Era." The dynamic, uncertain rise of China and the relative, actual decline of Japan at the early stage of the 21st century have reshaped the general power structure of East Asia.

At the same time, this new structure has undermined the Japan-China bilateral relationship and also destabilized the entire East Asia region in recent years. Narrow, emotional and inward-looking nationalism on the part of both China and Japan is rising. Particularly when contingency events happen in some sensitive areas between Japan and China, politicians and even conservative intellectuals in the two nations have dangerously tended to "compromise" with hyper-populist opinion among the public, especially on the Internet.

Now Japan-China relations have entered a new stage. How the governments and citizens of each nation communicate and perceive each other in the Two Giants Era, maximize their own national interests, and contribute to regional peace and prosperity is an essential issue. This is the challenge of the 21st century for Japan and China.

2018 marked the 40th anniversary of the signing of the Treaty of peace and friendship between Japan and China. The governments of both sides would have been wise to try as much as possible to make a point of the mutual importance of this year. For Japan, 2019 is an imperial transition year. With the ending of the Heisei era, Japan is entering a new era in terms of its domestic politics.<sup>2</sup> For China, this is the 70<sup>th</sup> anniversary of the founding of the People's Republic of China. Under these circumstances, the two sides must inevitably concentrate on coping with

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<sup>2</sup> On April 1, the Japanese government announced the name of the new imperial era - "Reiwa" which represents a break with centuries of tradition as the first era name to have been inspired by a Japanese, rather than a Chinese work of classical literature. The characters are taken from *Man'yōshū*, the oldest existing collection of Japanese poetry, compiled sometime after 759. It also means the Abe administration tends to make a point of Japan's own tradition, culture and history which might be somehow controversial in the international community.

domestic affairs. It would thus be beneficial for the countries to try to have deliberate stances on management of the bilateral relationship, to avoid any confrontations in sensitive areas such as the territorial problem over the Senkaku Islands, the historical problem, as well as a couple of geopolitical issues concerning the South China Sea, the Taiwan Strait and the Korean peninsula.

Given the ups and downs of the bilateral relationship in the past, strategic stability can be realized on the basis of political stability and positive interactions among the high-ranking leaders. In 2018, Li Keqiang conducted the first state visit to Japan by a Chinese premier in seven years; in return, Shinzo Abe reciprocated with the first state visit to China by a Japanese prime minister in seven years as well. The reciprocal state visits could be described as a milestone in such a historically important year for the bilateral relationship. And in 2019, a highly anticipated political event will see Chinese President Xi Jinping conducting a state visit to Japan – the first such visit by a Chinese president in eleven years. These interactions between top leaders will absolutely influence the overall relationship between China and Japan, enabling them to play constructive roles in terms of maintaining regional stability and prosperity.

### **THREE PILLARS OF FUTURE JAPAN-CHINA RELATIONS**

What are the driving forces which could promote Japan-China relations in the long run even though the bilateral relationship would still inevitably encounter a series of critical problems or even crises, in terms of territory, history, as well as the competition as rivals under the “Two Giants” era? Three pillars could be pointed out and discussed to interpret the future discourse of Japan-China relations.

First, China and Japan have basically pushed forward their mutual relationship in a positive direction since normalizing their diplomatic relationship in 1972. Multi-dimensional interdependence could be shaped as a symbolic context for bilateral relations. According to the working report launched by the Ministry of Foreign Affairs of Japan (Ministry of Foreign Affairs of Japan, 2018), in 2017, the total amount of trade between Japan and China amounted to 297 billion U.S. dollars (+9.8%)<sup>3</sup>; Japan’s foreign direct investment (FDI) toward China amounted to 3.3 billion U.S. dollars (+5.1%)<sup>4</sup>; in total, 32,349 Japanese companies have registered and launched business initiatives in mainland China<sup>5</sup>; in addition, 7,360,000 tourists

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<sup>3</sup> For Japan, China has been the largest trade partner and for China, Japan has been the second largest trade partner since the largest one has been the United States.

<sup>4</sup> For China, Japan has been the third largest source of foreign direct investment (FDI), No.1, No.2 and No.4 have been Singapore, South Korea and the United States respectively.

<sup>5</sup> The number of Japanese companies registered in China mainland has been the largest over the years, No. 2 and No. 3 have been the United States and India according to the statistical data in October 2017.

from mainland China visited Japan.<sup>6</sup> Obviously, China and Japan have been deepening economic interdependence over the last two decades, while, as this article discusses and argues, China has recently shown territorial ambitions and initiated disputes with Japan. This runs contrary to the commercial liberal literature that argues that trade promotes peace. On the other hand, the realist theory also does not fully explain Sino-Japanese relations because Sino-Japanese relations are not always in conflict. (Takeuchi, 2013)

In spite of this complexity, ‘Mutually Beneficial Relationship Based on Common Strategic Interests’, the initiative launched by the two governments in 2006, should become a principle for the two countries. The initiative was elevated to a Joint Statement, which was defined as ‘the 4<sup>th</sup> political document’<sup>7</sup> between Japan and China during former Chinese President Hu Jintao’s state visit to Japan in May 2008 (Ministry of Foreign Affairs of Japan, 2008). In this historic document, the two sides recognized that the Japan-China relationship was one of the most important bilateral relationships for both countries and that Japan and China now have great influence on and bear a solemn responsibility for peace, stability and development of the Asia-Pacific region and the world. More importantly, the two sides recognized that they are partners who cooperate together and are not a threat to each other. It also stated that they would support each other’s peaceful development, and they shared the conviction that Japan and China that uphold the course of peaceful development, would bring great opportunities and benefits to Asia and the world (Ministry of Foreign Affairs of Japan, 2008).

It has been undoubtedly difficult for Japan and China not to recognize each other as a threat. On the one hand, the Chinese government and citizens always see Japan, which invaded China during World War II, as a sort of threat as well as being cautious on any potential resurgence of Japanese “militarism”. On the other

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<sup>6</sup> The number of Chinese tourists to Japan rose up to 8 million and thirty-five thousand in 2018. Regarding the number of tourists between Japan and mainland China, the number of the Chinese who visits Japan exceeded the number of the Japanese who visits China for the first time in 2014. For examples, in 2012, more than three million Japanese visited China while about one million Chinese visited China. Arguably, the reasons why the number of Chinese tourists who visit Japan has rapidly increased are related to (1) the Japanese government has loosened the VISA policy toward Chinese tourists under the Abe Administration which was established in December 2012; (2) the Abe administration has made a point of tourism in order to boost its economy; (3) the Chinese citizens have strengthened purchasing powers over the years.

<sup>7</sup> The other three political documents between Japan and China are: (1) the Joint Communiqué of the Government of Japan and the Government of China issued on September 29, 1972, (2) the Treaty of Peace and Friendship between Japan and China signed on August 12, 1978, and (3) the Japan-China Joint Declaration issued on November 26, 1998. These documents have been the political foundation for advancing the Japan-China relationship in a stable fashion and forging the future of the relationship.

hand, the Japanese government and citizens have been continuously cautious on whether China under the one-party politics of the Communist Party of China would rise up and manage relations with neighbours peacefully. The joint statement in this sense represents a milestone in the history of Japan-China relations, and the bilateral relationship has reached a relatively mature level.

Second, emotions between the people in both China and Japan have been one of the biggest uncertainties in the bilateral relationship, due to their complex, tenacious and fragile nature. Emotions running high among the citizens of the two countries are the most serious problem requiring our attention and concern. As argued above, mutual distrust and skepticism between the people from both sides have never been resolved. Although it has been almost fifty years since Japan and China normalized diplomatic relations, people-to-people emotions have never been normalized. A long time and process would be required for the two societies to establish mutually trustful foundations on the perceptions of each other.

According to *the Japan-China Joint Opinion Survey 2018* launched by the Genron NPO, an independent, neutral, non-profit network-based Japanese think tank founded in 2001, and China International Publishing Group, 66.8% of Chinese respondents have bad or relatively bad impressions of Japan, while 42.2% have good or relatively good impressions of Japan; 86.3% of Japanese respondents have bad or relatively bad impressions of China, while only 13.1% have good or relatively good impressions of China. On the question of “whether Japan-China relations are good (or relatively good) or bad (or relatively bad)”, 30.3% of Chinese respondents answered good or relatively good while 45.1% answered bad or relatively bad; 39.0% of Japanese respondents answered bad or relatively bad while only 7.2% answered good or relatively good (Genron, 2018a).

The Genron NPO, in an analysis based on the result of the joint survey, pointed out several findings; (1) the most significant finding of this year’s survey is that sentiment among the Chinese citizens toward Japan is improving dramatically, but in sharp contrast, the impression the Japanese people have of China shows no such improvement; (2) the number of Chinese respondents who feel Japan-China relations are “bad” dropped substantially to 45.1 percent, almost 20 points down from 64.2 percent in the previous year’s survey. The corresponding figure by Japanese respondents is 39 percent, an improvement from the previous year’s 44.9 percent. However, these findings do not mean the Japanese and Chinese people consider the current state of Japan-China relations to be “good.”; (3) although the Chinese people’s impressions of Japan are visibly improving, the number of Chinese respondents who feel Japan is a military threat increased from 67.6 percent in the previous year’s survey to 79.4 percent. This means that according to the perception of the Chinese people, Japan poses the world’s greatest military threat to their country. The same holds true for the Japanese people’s perception of China’s military threat with 57.5 percent of the respondents feeling that way, up from 45.3

percent in the previous year's survey. Indeed, tensions continue between the Japanese and Chinese people in the area of security (Genron, 2018b).

These data and analysis are relevant in order to understand there is still a long way to go for Japan and China to improve mutual perceptions and establish positive feelings among the people in the two countries. Given the recent survey, it would be more critical to understand whether and how the Japanese people could improve their emotions and perceptions toward “the peaceful rise of China”.

Thirdly, relating to the second pillar, contingency events could stir up nationalism and bring about crises of trust between the two nations. For example, the poisoned dumplings crisis at the end of 2007 and the beginning of 2008 became a serious emergency that worsened Japanese feelings toward China and destabilized bilateral relations. About ten Japanese consumers ate frozen dumplings which were produced and exported by Tianyang food company located in Hebei province, China, and then they collectively claimed to have food poisoning. As the incident was directly related to the lives of ordinary citizens in Japan, it was widely and continuously reported in mass media. As a result, emotions among the public in Japan toward China sharply worsened, leading to the undermining of diplomatic relations between Japan and China.

Referring to the above survey on Japan-China relations, from 2007 to 2008, the number of Japanese respondents who had bad or relatively bad impressions toward China increased from 66.3% to 75.6%, while the respondents who had good or relatively good impressions toward China dropped from 33.1% to 24.1% (Genron, 2018b). In order to understand why and how contingency events always lead to a rise in unhealthy nationalism, inevitably undermining diplomatic relations or even political stability between Japan and China, the so-called “territorial dispute” over the Senkaku Islands (“Diaoyu Islands” in Chinese) around the East China Sea, one of the most politically sensitive and structurally complicated areas in Japan-China relations, must be examined. Harvard academic and expert on Japan and China, Ezra Vogel argues that the difficulties between China and Japan also focus on the conflicting territorial claims over the Senkaku/Diaoyu Islands. The dangers of accident and conflict are real and have the potential to set back reconciliation for decades. (Vogel, 2014)

### **CASE STUDY: “NATIONALIZATION” OF THE UNINHABITED ISLANDS**

When the Japanese central government “nationalized” the Senkaku Islands on 11 September 2012, Chinese officials immediately and fiercely criticized the decision. “This move taken by the Japanese government constitutes a serious violation of Chinese territorial sovereignty. The Chinese government and people firmly oppose

it and have strongly protested against the move,' the Ministry of Foreign Affairs of China said in its statement (Ministry of Foreign Affairs of China, 2012). The statement also condemned the Japanese government with relatively strong rhetoric such as 'Diaoyu Islands have been China's inherent territory since ancient times', 'Japan's occupation of Diaoyu Islands is illegal and invalid', 'China has taken a strong stance to safeguard its sovereignty over Diaoyu Islands' and 'any Japanese attempt to covet Diaoyu Islands is doomed to failure' (Ministry of Foreign Affairs of China, 2012). What was seen in the Chinese media was much more aggressive: 'Japan stole Chinese territory' (People's Daily, 2012); 'the action of nationalization means risk on a revival of Japanese militarism'. (Xinkuaibao, 2012)

*Sanctions* were imposed against Japan economically, culturally, diplomatically and even politically. After the nationalization, for example, the Chinese government tightened up customs inspections for Japanese products at its ports (*Japanese firms complain*, 2012). A number of meetings, forums, cultural and commercial events between Japan and China were postponed or cancelled by the Chinese side unilaterally. Books and articles related to Japan or written by Japanese authors were prohibited from publishing under the 'serious circumstances'.<sup>8</sup>

Perhaps contrary to those criticisms and sanctions, the Chinese government actually seemed to see the crisis as a sort of 'strategic opportunity' to turn around the existing situation over the islands. In the past, the islands were administered by the Japanese government which was working closely with the United States as part of their security alliance, whereby the United States returned the rights of administration of Okinawa to Japan according to the Agreement between Japan and the United States of America. And China is currently making efforts to challenge directly Japan's longstanding administrative authority over the islands through a fairly regular pattern of incursions into nearby spaces by a variety of mainly civilian government aircraft and ships. (Swaine, 2013)<sup>9</sup>

'We got a historical benefit from the nationalization policy toward Diaoyu Islands by the Japanese government. We have to thank the Japanese prime minister,

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<sup>8</sup> The author has personally experienced these situations. It got much harder to meet with Chinese officials, intellectuals, publish articles and books in mainland China since the nationalization incident took place.

<sup>9</sup> This is one of the elements of which Michael Swaine, China security expert, argues this dispute is particularly significant among Beijing's altercations with its maritime neighbors because of the uniquely volatile combination of elements involved. Other elements include a) the relatively high numbers and in some cases, level of capability of the government vessels participating on both sides; and b) the intensity of elite and public emotions involved, especially in China. Swaine also argues these and other factors significantly increase the likelihood of a serious crisis occurring, and perhaps escalating out of control as a result of either a miscalculation and subsequent escalatory reaction by either side or a deliberate attempt by one or both sides to gain a lasting advantage during the ongoing crisis.

Mr. Noda,' a senior official who was in charge of foreign relations in the Communist Party of China insisted.<sup>10</sup> This viewpoint or stance at that time seemed to be a sort of 'strategic consensus' beyond sectors within the Communist Party of China, including among scholars who are close to policymakers. 'We now could have a reasonable excuse to send more vessels, even aircraft, to the disputed area so as to oppose the Japanese step-forward policy over the islands. Through this dispute, they will no longer be administered by Japan', added the official.<sup>11</sup>

In fact, Chinese officials accelerated to send a number of public vessels, even aircraft, to the Senkaku area in order to pressure the Japanese government (Asahi Shimbun, 2017).<sup>12</sup> They repeatedly made propaganda both domestically and internationally that 'Diaoyu Island and its affiliated islands have been an integral part of Chinese territory since ancient times' (Ministry of Foreign Affairs of China, 2012; *Japanese firms complain*, 2012).

The Japanese government, which tried to 'stabilize' the Senkaku area through nationalization, has never acknowledged the existence of "territorial disputes" with China. Instead, it criticized Chinese aggressive actions toward Japan's sovereignty. Anti-Japanese protests that exploded in more than one hundred Chinese cities in September 2012 stirred anger among Japanese citizens. Emotions among Japanese citizens toward China worsened dramatically. At the same time, the interests of Japanese companies in China were affected. Confidence in the Chinese market among Japanese investors and entrepreneurs was shaken.

The perception gaps between the two governments and societies of Japan and China were obvious, which made the circumstances over the uninhabited islands more uncertain. Chinese officials opposed the "nationalization" and forced the Japanese government to recognize 'the continual existence of the territorial disputes'. On the other hand, Japanese officials continuously opposed the Chinese intrusion into the territory and asked the Chinese government to stop the provocations. Both sides sought to portray themselves as victims while describing

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<sup>10</sup> Interview with a high official in the Central Foreign Affairs Commission under the Communist Party of China. The interview was conducted in August 2012, Beijing. The official asked for anonymity because he was not authorized to discuss the situation.

<sup>11</sup> Interview with a high official in the Central Foreign Affairs Commission under the Communist Party of China, op. cit.

<sup>12</sup> On reasons of the assertive actions taken by the Chinese government, an expert on China and Japan-China relations, Professor at the University of Tokyo, Akio Takahara raised up six reasons: (1) in order to crack down criticisms toward China in Japan (2) The Chinese government expects assertive actions toward Japan could make the third countries being scared to China and co-opt for them (3) in order to unite the domestic opinions (the Communist Party of China is most afraid of being criticized by the public in domestic) (4) the rise of nationalism (5) organizational interests of the Navy and maritime police (6) characteristics of Xi Jinping (Takahara, 2016)

the other as the *invader*. Interestingly, in terms of perception gaps at that time, the Japanese government believed that it was China whose national image was injured internationally thanks to such provocative and assertive actions toward the islands, while the Chinese government, as argued above, tended to estimate that it was China whose national interests had been maximized. On the contrary, the Japanese government did not perceive nationalizing the islands positively, rather, it seriously worried about deteriorating Japan-China relations in the areas of economic ties, business interests and emotion among the public.

Looking back on the crisis that the world's second and third largest economies encountered, the causes of the occurrence were structural. Why did the emergency event happen and undermine the diplomatic relationship between Japan and China? In terms of lessons learned from history, four implications should be examined.

First, an information asymmetry with a lack of mutually-agreed facts and truths should not be ignored. Chinese citizens were not aware of the fact that 'Diaoyu Islands have been administered by Japan since 1972'. Meanwhile, Japanese citizens have never tried to acknowledge the truth that "China has claimed sovereignty over the Senkaku Islands". Both parties have been too stubborn, seriously lack flexibility and a manner of mutual understanding and respect which diplomacy always requires.

Second, both Japan and China have to recognize that some miscommunications and misperceptions in diplomacy were taking place. The Japanese government "nationalized" the islands on September 11 just after Japanese Prime Minister Yoshihiko Noda met with Chinese President Hu Jintao in Vladivostok. Was this decision rationally made? Chinese citizens were sensitive to or even felt humiliated by the word "nationalization"<sup>13</sup>, and President Hu seemed to lose face because of the sensitive timing and wording. According to a couple of officials both from Japan and China, the Chinese government once accepted the idea that the "nationalization" approach would be more appropriate, rather than the islands being purchased by nationalistic Tokyo Governor Shintaro Ishihara, in terms of maintaining stability around the islands. However, it eventually and suddenly turned to oppose the decision and implementation of nationalization at the beginning of September. Why and how did this policy shift happen? It casts doubt on whether

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<sup>13</sup> It is not difficult to understand deep dissatisfactions of the Chinese government from the below official statement made by the Ministry of Foreign Affairs of China on 14 September 2012: "Since the beginning of this year, the Japanese government has taken actions one after another over the issue of Diaoyu Islands. Even this year, it staged a farce of naming Diaoyu Island and its affiliated islands. Then it encouraged the right-wingers to instigate a political storm around the issue of "purchasing" the islands. Finally, the Japanese government pulled off its mask and revealed its own intention to "purchase" and "nationalize" Diaoyu Island, Nanxiao Island and Beixiao Island. By "nationalizing" the islands, the Japanese government aims to reinforce its "actual control" over the Diaoyu Islands and eventually occupy the islands."

the leadership of the Communist Party of China possessed coherent and integrated policies toward working with Japan as well as its external strategy in the Asia Pacific region (Kato, 2013).

Third, the rise of nationalism and the decline of governance capability in both countries undermined the rational policy implementation on diplomacy. The economic downturn, social disparity, complicated international relations made the power foundation of the two administrations vulnerable. Simultaneously declining governance capabilities in the two nations also arouse rampant populism. This is a vicious cycle and a significant lesson for the two governments and societies in terms of assuring the long-term development of Japan-China relations.

Fourth, as an important background, which would have affected the discourse of Japan-China relations, the balance of power in East Asia has shifted dramatically. Nowadays, East Asia is entering *the Two Giants era*. China overtook Japan as the world's second-largest economy in 2010 and was eager to surpass the United States economically even diplomatically under the Xi Jinping administration in these years. In the 21<sup>st</sup> century, “the strong Japan” and “the strong China” have to find some ways to coexist, which have never happened in the history in East Asia. This has also led to the U.S. rebalancing policy in the Asia-Pacific region, which inevitably makes Japan-China relations more complicated.

In short, a lack of facts and truthful information, failure of diplomatic communication, simultaneously rising nationalism and declining governance capability and the transforming power balance in the Asia-Pacific region created the crisis over the uninhabited islands between Japan and China. The question is how the two nations can overcome these dilemmas and manage the complicated bilateral relationship more effectively. Again, there are four things Japan and China should tackle respectively as well as work together on.

First, Japan and China have to prevent any accidental military clashes through a strong political commitment by top leaders from the two sides. In order to do that, as an effective measure of crisis management, a “military hotline” should be established. A consistent and stable communication mechanism would be inevitable to constrain an escalation of confrontations. In this sense, it is remarkable progress for the two sides to successfully launch the implementation of “Maritime and Aerial Communication Mechanism” between the Japanese and Chinese defence authorities.<sup>14</sup>

Second, Japan and China need to strengthen communication channels, not only at governmental levels but also along all social sectors, including scholars, journalists, entrepreneurs, youths, etc. At the same time, in order to prevent further diplomatic and intelligence failure, the ministries dealing with diplomacy should institutionalize

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<sup>14</sup> These issues were discussed in the 10<sup>th</sup> Japan-China high-level initiative on maritime policy in Jiaxing city, Zhejiang province, China on 17-18 December 2018.

communication channels between the two governments and improve verdict coordination within the administrations. The two governments had a discussion toward improving Japan-China relations before the meeting between President Xi and Prime Minister Shinzo Abe in November 2014 in Beijing. The two sides agreed to share the view that, by utilizing various multilateral and bilateral channels, they would gradually resume dialogue in political, diplomatic and security fields and make an effort to build a political relationship of mutual trust (Ministry of Foreign Affairs of Japan, 2014).

Third, what Japanese and Chinese officials have to promote is to tell the “facts” to their own public. For China’s part, Mr. Xi Jinping has to tell his own people that ‘Diaoyu Islands, in fact, has been administered by the Japanese government since 1972’ even though China has claimed its own sovereignty over the islands. For Japan’s part, Mr Shinzo Abe has to tell his own people that ‘Japan acknowledges that the Chinese side has, in fact, claimed sovereignty of the Senkaku Islands over the years, so the territorial disputes are existing’ even though the islands remain administered by Japan as well as under the effective and actual control by the U.S.-Japan security treaty and alliance.<sup>15</sup> The issue on how should Japan position diplomatically in front of the territorial dispute with China has been controversial in Japan, given this circumstance, different institutions beyond sectors such as the Diet should deepen the constructive discussion. (Nakauchi, 2012)

Fourth, top priorities for the two nations in terms of preventing any escalations over the islands would solve innumerable domestic problems. As argued above, the simultaneous decline of domestic governance capabilities in both countries is a crucial reason why national interests are often threatened by nationalism and why rational policy implementations are always undermined by populism. Inward-looking, narrow nationalism and populism should be “common enemies” for Japan and China. Stable and healthy interaction among top leadership should be a key foundation to building a good relationship between Japan and China. Given the fundamental differences on political and value systems between Japan and China, there is a long way to go in order to realize a real mutual understanding and trust as well as building a truly stable bilateral relationship.

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<sup>15</sup> In November 2014, both sides agreed to recognize that they had different views as to the emergence of tense situations in recent years in the waters of the East China Sea, including those around the Senkaku Islands. They shared the view that, through dialogue and consultation, they would prevent the deterioration of the situation, establish a crisis management mechanism and avert the rise of unforeseen circumstances. (Ministry of Foreign Affairs of Japan, 2014)

### **INSTEAD OF CONCLUSION: CAN THE JAPANESE ACCEPT THE RISE OF CHINA?**

Whether one likes it or not, the rise of China is a reality in contemporary international relations. One question is fundamentally important in thinking about the future development of Japan-China relations: can the Japanese “accept” the rise of China?

In 2010, China exceeded Japan in the total amount of GDP, becoming the second-largest economic power in the world. In other words, Japan lost its 42-year hold on the position of the world’s second-largest economy.<sup>16</sup> It looked like it would have been shocking for Japan. However, most Japanese seemed to have awaited this historical event rationally, even believing that an open prosperous and dynamic Chinese economy could provide Japan with enormous benefits. Japan did not have to take countermeasures against the rise of China but instead needed to take advantage of it.

Many believed that restoring the Japanese economy without a free and open Chinese market would be impossible. This kind of perception, which is both reasonable and pragmatic, seemed to be universal, especially among policymakers and businessmen considering the huge and lucrative Chinese market. In the area of economics and finance, very few people seemed to believe that the rise of China was unacceptable. They not only accepted it but they enthusiastically expected the rapid and long-term growth of the Chinese economy.

The problem then is how Japan can take advantage of the rise of China based on its own grand strategy, and stimulate the “re-reform and re-opening-up” of the Japanese economy. That should be a core question for Japan’s government and citizens in the days to come. As discussed above, at the governmental level, Japan and China have already normalized mutual perceptions. Former Japanese Ambassador to China Yuji Miyamoto emphasizes the importance of the “4<sup>th</sup> political document” signed by China and Japan’s top leaders in May 2008, particularly in the fact that both China and Japan define the rise or development of each other as peaceful. ‘It was the first time that China had described Japanese development after World War II with the words “peaceful nation”,’ Ambassador Miyamoto argued (Miyamoto, 2011).

The biggest uncertainty is at the level of people-to-people relations. Misunderstandings or misperceptions will inevitably increase in accordance with rapidly developing, multi-dimensional communications. People in China and Japan need to communicate consistently with each other with tolerance. Mutual

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<sup>16</sup> Japan overtook Germany and became the second-largest economic power in 1968.

understanding and trust will take a long time, so strategic patience would be required for both Japanese and Chinese.

As discussed above, emotions among the Chinese and Japanese against each other's countries suffer a lack of balance. While Chinese emotions toward Japan are obviously influenced by political circumstances, Japanese emotions toward China have been much more changeable and unstable over the past couple of years. In fact, Chinese emotions toward Japan were greatly improved when President Hu Jintao visited Japan in May 2008. The Great Sichuan earthquake struck on 12 May that year and, desiring to help manage the crisis, the Japanese government dispatched professional rescue teams to the disaster area before any other country did. Unfortunately, however, the mutual emotions between the Chinese and Japanese during that term were not interactive. Because of the negative impact of the poisoned dumpling incident that occurred at the beginning of 2008, ordinary Japanese completely lost trust and confidence in China.

What we should learn from the incident is that the Japanese tend to recognize livelihood issues such as food, health, the environment, public order and so on as the most important criteria to judge the meaning of the rise of China. Comparatively, the Chinese people place more emphasis on political circumstances such as how often top leaders visit or whether the Japanese prime minister has a “sincere” attitude on historical matters, especially on how to deal with the Yasukuni Shrine issue.

Although the Japanese seem basically to accept the rise of China, emotions among ordinary people toward the rise of China are still very complicated. According to research on public opinion regarding diplomacy annually conducted by the Japanese Cabinet Office, those who feel an affinity for China were 18.7% (2017) and 20.8% (2018), while those who do not feel an affinity for China were 78.5% (2017) and 76.4% (2018). In contrast, these numbers were pretty optimistic in 1980 – at that time, they were 78.6% (affinity) and 14.7% (no affinity) (The Japanese Cabinet Office, 2018).

For most of the Japanese public, their perception of the rapid rise of China surely reflects how they perceive the relative decline of Japan. In this sense, the rise of China has been like a “mirror” for a re-identification process for the Japanese. They are not only very cautious toward China, but they are also losing confidence in themselves. That is why, no matter how China and Japan promote or stabilize their bilateral relations at least in the short term, Japanese emotions toward China and the Chinese would not be pushed forward dramatically.

In order to keep these emotions from plunging to the bottom, three conditions must be ensured. First, the top leaders should visit each other often, to maintain a friendly atmosphere between China and Japan. Secondly, under consistent political stability, “multi-dimensional interdependences” should proceed sequentially. Thirdly,

the two governments have to establish and regularize a mechanism on crisis management against emergency events as soon as possible so as to tackle any uncertainties that occur in different areas – livelihood, business, territory, history, cultural exchange and so on – between Japan and China. A strategic mechanism that facilitates mutual and frank communication in different areas between the two nations would play a crucial role in a time of misperceptions and distrust.

It is a positive situation for Japan-China relations that a certain number of efforts to meet these three conditions have been made, as discussed in this article. During Japanese Prime Minister Shinzo Abe's latest visit to Beijing in November 2018, he emphasized that Japan-China relations are entering a new phase, and the two governments agreed to strengthen cooperation in third countries while Japanese official development assistance (ODA) toward China, which has lasted 40 years, "completed its historic mission". As the second and third-largest economy, China and Japan are playing vital roles not only in Asia but in the entire world's economic development. Interdependence has proceeded, problems that cannot be resolved unilaterally have increased. Under these circumstances, now is the time for Japan and China to contribute to world peace and prosperity together (Abe, 2018).

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### **KAKO SE ODNOSI JAPANA I KINE MOGU STABILIZOVATI?**

*Apstrakt:* Japansko-kineski odnosi ulaze u eru „Dva Džina”, koji su bez presedana u istoriji Istočne Azije. Višedimenzionalna međuzavisnost Japana i Kine se razvija ubrzano, kao jedan od pozitivnih faktora u smislu ubrzanja njihovih bilateralnih odnosa u dugom periodu. Sa druge strane, emocije u javnostima obeju strana su problematične i neizvesne, i od krucijalne je važnosti da se istraži kako da se one „normalizuju”. Autor tvrdi da nepredviđeni događaji, koji utiču na to da ljudi budu više okrenuti sebi, i okrenuti nacionalizmu, dovode do podrivanja japansko-kineskih odnosa. Kriza „nacionalizma” iz 2012. godine je tipičan slučaj u kome su dva naroda morala da promišljeno savladaju lekcije. Nedostatak podataka i istinitih informacija, neuspeh diplomatskih komunikacija, simultani rast nacionalizma i opadanje sposobnosti države i transformacija balansa snaga u Azijsko-pacifičkom regionu proizvela je krizu oko nenasiljenih ostrva. Kako Japan i Kina mogu da prevaziđu ove dileme i upravljaju efikasnije komplikovanim bilateralnim odnosima? Potrebno je da dve strane uspostave kanale i mehanizme upravljanja krizom. Pored kontinuirane promocije višedimenzionalne međuzavisnosti, nove metode omogućiće da se izbegnu stalne pretnje od povremenih kriza do nadirućeg i neodgovornog nacionalizma za bilateralne odnose Japana i Kine.

*Ključne reči:* Japansko-kineski odnosi, diplomatija, međuzavisnost, emocije, nepredviđeni događaji, nacionalizam, nova era.

*Received:* 26 March 2019

*Accepted:* 8 April 2019

UDC 330.322(510:549)  
Biblid 0543-3657, 70 (2019)  
Vol. LXX, No. 1173, pp. 61–76  
Original paper

## **THE IMPACT OF CHINESE INFRASTRUCTURE PROJECTS ON DEVELOPMENT OF HOST ECONOMIES**

### **Empirical evidence from Pakistan economy**

Nataša STANOJEVIĆ<sup>1</sup>

*Abstract:* This paper examines the impact of Chinese investments in infrastructure facilities within the Belt and Road Initiative (BRI) on the economies of host countries. Pakistan was selected for the case study as one of the first destinations of Chinese FDI within the BRI, which allows necessary time distance for the research. Its important geographical position at the new Silk Road traces, a significant amount of Chinese investment, and evidence of both positive and negative effects of Chinese penetration, are the additional reasons for choosing Pakistan for a case study. Using Multivariate Analysis methods, the impact of Chinese FDI and total FDI on several key economic indicators of Pakistan are measured and compared separately. The results show a much stronger and more positive impact of Chinese investment than total FDI but also point to the direction of a change, such as increasing of import, and potential challenges, such as external debt to China.

*Key words:* China, Pakistan, FDI, Infrastructure, Belt and Road Initiative.

*JEL codes:* F21, F43.

### **1. INTRODUCTION**

Infrastructure is one of the key conditions for the economic and overall development of a country. Infrastructural shortcomings are almost a general problem of developing countries, and even in the medium-developed countries, it is a common occurrence. Thus, at the same time, weak infrastructure can be observed both as the cause and effect of a weak economy.

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The Asian Development Bank study (ADB, 2017) asserts that in Asia, \$26 trillion in infrastructure investments is needed over the 2016-2030 period to eliminate poverty and maintain 3-7% economic growth. The condition of the infrastructure in developing countries usually cannot be sufficiently improved by internal resources. These are countries with a general lack of capital, slow growth, numerous structural weaknesses and budget deficits, which indicates that foreign investment in infrastructure is required.

At the same time, the impressive economic rise of China, mainly based on exports and investments, has created a need for new and more efficient transport routes to the West. The concept of the traditional Silk Road as a network of infrastructure connections has been renewed through a new project called the Belt and Road Initiative (BRI).

In a short time, the project outperformed the initial intention for China's transportation link with the countries of Western Europe. The National Development and Reform Commission of China (2015) presented the detailed strategy of the BRI as a gigantic supra-national infrastructure project. It included railway (standard and fast), land and maritime roads, ports and airports, infrastructure facilities related to energy - hydroelectric power plants, dams, oil pipelines, gas pipelines and electric lines, but in the latest phase, the BRI included the development of economic corridors, industrial parks, duty-free zones, and the like. The Belt and Road Initiative also goes beyond the geographical framework of the traditional Silk Road and increasingly acquires a global dimension.

The BRI could be an efficient means of keeping a relatively high growth of the Chinese economy. It could provide a new dimension to the same mechanism which has already raised it – investments and exports (Stanojevic, 2016, p. 144). International infrastructure projects are becoming a new driver of Chinese economic growth and expansion, as the exports were in the previous phase. Some of the benefits that China gains within the BRI are the engagement of its over-sized construction industry, increased exports of construction materials and machines, employment of skilled labor in this sector (engineers, architectures), interest revenue (investments have a form of loans), security of energy supply and internationalization of the yuan (RMB). New land routes and new arrangements with the countries to which routes lead will enable China to conquer new export markets and maintain or expand the existing ones (Stanojevic, 2016, p. 146).

This Chinese strategy has been successfully implemented since 2013, and the placement of Chinese FDI annually increases by more than 10% (UNCTAD Stat, 2018).

Interests of China and countries with poor infrastructure performance are obviously complementary. China offers investment in infrastructure objects which is necessary for further growth and development and cannot be realized from

internal financial and other resources. Given the fact these investments are usually placed in the form of loans, negative effects, such as high foreign debt to China, are also possible and expected in smaller countries. Examples include Pakistan, Laos and Montenegro, etc., whose debt to China has become an unbearable burden for the domestic economy.

A general hypothesis is that Chinese FDI has different, and, in many aspects, more favorable effects than foreign direct investment in general. The specific features and the current state of the Chinese economy determine the sectors, amounts and conditions of investing, making Chinese FDI very different from those of the Western countries.

The aim of this research is to assess the effects of Chinese investments on the key development indicators of the economy of Pakistan. This country is chosen for analysis because it is one of the first countries to be involved in the Belt and Road Initiative project, which provides the necessary time distance for measuring the effects. A large external debt to China is another reason for analyzing the economy of this country. The aim is to evaluate whether other effects of Chinese FDI are positive and strong enough to be worth the risk of excessive debt. The third criterion is the relatively large volume of investments. Namely, China today has investments probably in all the countries of the world, but the impact cannot be analyzed when they are negligible within the overall FDI in this country. With \$52 billion FDI stock, Pakistan is the destination of China's largest investment in all of Asia, despite the competition of oil economies for which China is also very interested.

The quantitative analysis in the case study of Pakistan includes the comparative application of Multivariate Analysis method on both Chinese investment and total foreign investment impact.

## **2. THEORETICAL BACKGROUND**

### **2.1. The impact of infrastructure investment on economic development**

Infrastructure is widely recognized as a key precondition for the economic success of countries. The volume, state and efficiency of an infrastructure strongly influence the production and distribution of goods and services, as well as the living conditions of the population, i.e., the labor force. The need for a developed and efficient structure is indisputable. The main problem in this area is the optimal amount of investment in infrastructure, which depends on the country's ability to provide necessary resources from its own or external sources.

An important mechanism of the influence of infrastructure on development is generating a production increase through market expansion. Transport

infrastructure has affected the increase in the commodity market by lowering transport costs and accelerating the delivery of perishable products. The market's increase leads to the strengthening of competition, specialization, productivity growth and increase in the volume of production. The modern advancement of telecommunication infrastructure has caused the expansion of the concept of infrastructure and intensified the process of market expansion. Besides, infrastructure and its services are used not only by enterprises but also by households. Even the benefits that households gain from improved infrastructure have a positive impact on development, through lowering costs, increasing the quality of workforce and productivity (Prud'homme, 2004, pp. 15-16).

The World Economic Forum in its report for 2018 points out that investing in infrastructure is “the key and the most efficient policy, which can respond to the tremendous challenge of growing unemployment in the world” (WEF, 2018, p. 20). Infrastructure investments have been shown to sustain real income growth among the lower-skilled and foster employment and re-qualification in deindustrialized areas.

The assessment of the competitiveness of the economy shows that the countries with the most developed infrastructure have a far greater Global Competitiveness Index (GCI) than those with poorly developed infrastructure (WEF, 2018, p. 28).

Romer (1993) considers infrastructure as a basic assumption of business. If countries do not have enough financial resources for building or necessary modernization of infrastructure which usually involves very high investments, it is necessary to provide foreign direct investment (Romer, 1993, p. 547).

## **2.2. FDI impact on economic development**

The attractiveness of the idea of the exceptional impact of FDI on the development of the host countries comes from several theoretical assumptions. Some of them are: new enterprises increase the total volume of production, and new businesses or the expansion of existing activities generate jobs, thus reducing unemployment. The effects can also be manifested by increasing quality, not just quantity production: multinational companies (MNCs) transfer new technologies and knowledge into their branches in a host country (Romer, 1990, Grossman and Helpman, 1991), MNCs apply better organizational or management practices, improve the ability of companies to absorb more technology (Grossman and Helpman, 1991), they use better quality inputs, the branches gain access to foreign export markets by providing them access to the entire business group (Stanojević, Kotlica, 2015, pp. 544-545). These mechanisms should contribute to raising production to a higher level in qualitative and/or quantitative terms, stimulate economic growth and trade and reduce unemployment. Indirectly, this would

further lead to the improvement of the macroeconomic environment, labor efficiency and increasing competitiveness in the global market.

This theoretical assumption gave rise to hundreds of papers analyzing the impact of FDI on economic growth. However, despite theoretically positive assumptions, most studies in quantitative terms do not result in a significant positive correlation between FDI and economic growth, although statistical methods are different (simple correlation or multiple regression in combination with time series or panel data, and others).

Most empirical studies show a minimal positive or negative impact (absence of effects) of FDI inflows on economic growth - Kentor and Boswell (2003) on a sample of 39 less developed countries, Firebaugh (1992) 65 less developed countries, Naveed and Shabbir (2006) on the sample of 23 countries, Estrin and Uvalic (2013) on the sample of all transition countries, Dar, Muhammad and Mehmood (2016) on the sample of Pakistan, Tahiri (2017) on the sample of Afghanistan, etc.

Significant positive effects of FDI on economic growth are recorded by Hofmann (2013), Hlavacek and Bal-Domanska (2016) in the analysis of the effects of FDI in the Central European countries, Rahman A. (2015) on the case of Bangladesh, although in the last-mentioned study the statistical significance of the results is relatively small.

Some studies have suggested negative effects of FDI on economic growth: Rahman Z. U. (2014) on the sample of Pakistan, several empirical studies of post-socialist states - Bandelj and Mahutga (2010), Curwin and Mahutga (2013), Stanojević and Kotlica (2015). In addition to the FDI flow analysis, the mentioned authors Kentor and Boswell (2003) and Firebaugh (1992) have analyzed the impact of FDI stock. In this case, the effects are not insignificant but rather markedly negative, such as the effects of long-term FDI concentration.

Some possible reasons for the negative effects of FDI are the outflow of the entire profit from the host country, leaving the local economy with no funds for reinvestment. Transition economies experience negative impacts of FDI usually due to conducting privatization rather than greenfield investments (Estrin and Uvalic, Hofmann 2013, Stanojević, Kotlica, 2015). Privatization in these countries has led to a reduction in the number of jobs (mass dismissal) and a reduction in salaries to increase efficiency. Some analyses (Curwin and Mahutga, 2013, Stanojević, Kotlica, 2015) point out the problem of predominant placement of FDI in non-productive, thus non-export sectors, such as banks, insurance, auditing and other financial agencies, as well as trade and telecommunications.

We may note that studies encompassing a large number of countries have resulted in a very low coefficient of correlation between FDI and economic growth. So, the analysis of a large number of different experiences does not show the *general* but the *average* impact of FDI, which is not useful to the researchers or the

governments. The significance of the sample size is rendered invalid due to the data at a high level of aggregation. In these cases, a dependent variable is a widest-range parameter – GDP, and an independent one is total FDI which is also analyzed in the broadest sense, regardless of the sector in which they are placed, the origin country of investors, forms (greenfield or merger), etc. Researches limited to one country get better results but also have a problem of the generality of these basic input data, which is why statistical significance is usually low.

Bearing in mind the weakness and the opposite results of the former studies, we conclude that FDI is neither an incentive factor nor a negative phenomenon a priori, but should be explored in a specific context by applying the case study method. The specific characteristics of a host country, its size, natural, economic and human resources, the state and the structure of the economy, the geographical position, its population, and many other features, are the key factors which have affected the origin and volume of investments, the target sector and the conditions of investing.

The analysis of FDI effects on economies should be limited and narrowed down, not only to a particular country or a group of countries but generally the data must have a lower aggregate level: special economic sectors or individual economic activities instead of the whole economy, individual macroeconomic parameters instead of GDP, FDI origin instead of total FDI, etc.

### **3. THE ECONOMIC PENETRATION OF CHINA INTO PAKISTAN**

Regardless of whether they are in an alliance or conflict, Pakistan had been an interest zone of America for decades. China did not show its willingness to compromise this special relationship. After one decade of the Pakistan-US alliance, based on the joint activity in the so-called *War on Terror* 2001 during 2011, the mutual animosity was renewed and the United States took an armed intervention in Pakistan. During and after this conflict, Pakistan tried to strengthen its ties with China in order to find a strong ally. At that time, China resisted any arrangement that could jeopardize its relations with the US and India, which has a border conflict with Pakistan on the territory of Kashmir.

However, this tough position of China appears to have weakened over time due to great geo-strategic interests in Pakistan. The specific circumstances and changes in the Chinese development strategy have brought this South Asian country into the focus of Chinese investment.

The geographical position of Pakistan gives the country the role of a “gateway” to the Middle East. Thousands of kilometres of pipelines will run gas and oil from the Middle East, across the territory of Pakistan to China. China is trying to establish

control over this country with unstable security to safeguard energy supplies. In 2015, China and Pakistan started the 46 billion-dollar project entitled the China-Pakistan economic corridor — the CPEC. This project is a series of sub-projects aimed at expanding and improving Pakistani infrastructure. This corridor connecting the Sinkiang (Xinjiang) region and the Gwadar Harbor shortens the road from China to the Middle East for 12,000 km and opens the way to the Indian Ocean.

Chinese investments in Pakistan are multiplying on an annual basis. With \$320 million in 2009, China's FDI increased to \$12-19 billion a year (China Global Investment Tracker) after launching the CPEC. This is the most spectacular growth of Chinese investments in one country. Almost all investments are placed in transport infrastructure (passenger cars, ports, railways, and airport), hydropower plants, and telecommunication infrastructure.

Such a large amount during a long period would have to leave a deep mark in this relatively poor economy.

## **4. RESEARCH METHODOLOGY**

### **4.1. Methodological framework**

As one of the research objectives is the comparison of the effects of total FDI and Chinese FDI within the BRI project, it requires a quantitative analysis to be done for both of them. The effects of investments (total and Chinese) are split into several variables. The impact on total GDP, i.e., economic growth as a common analytical setting is considered, but also the impact of FDI on a series of separate indicators of growth and development is explored. The goal is to monitor in which manners the investments affect the economy.

The dependent variables on which FDI has a hypothetical impact are GDP, GDP per capita, unemployment rate, external debt, imports of goods and services and exports of goods and services, as well as two indexes of wider social development — the Human Development Index (HDI) and the Global Competitiveness Index (GCI). Given the theoretical assumptions about investment in infrastructure as a factor of attracting foreign direct investment (Romer, 1993), the overall FDI will also appear as a dependent variable in relation to Chinese FDI, seen as an indicator of investment in infrastructure.

Data for general indicators for all the countries: GDP, GDP per capita, unemployment rate and external debt are taken from the World Bank database. Total imports of goods and services, as well as exports of goods and services of the analyzed economies, were taken from the UN COMTRADE database.

The Human Development Index was created by the UNDP (United Nations Development Program) to emphasize that people and their abilities should be the

ultimate criterion for assessing the development of the country instead of economic growth. The HDI is a composite index that focuses on three basic dimensions of human development: the ability to lead a long and healthy life measured by the life expectancy; the ability to acquire knowledge measured by the average and expected years of schooling; and the ability to achieve a decent living standard measured by gross national income per capita (UNDP, 2018, p.1).

The Global Competitiveness Index (GCI) was created by the World Economic Forum (WEF). This composite indicator of the competitiveness of an economy consists of several dozen sub-indicators classified into 12 groups: institutions, infrastructure, macroeconomic environment, labor efficiency, health, primary education, higher education, technological readiness, etc. In this case, statistically significant results are not expected because of the excessive number of different measures included in the variable. Regardless of the expected insufficient statistical reliability, the correlation between investments and these indicators can suggest the general direction of FDI impact on development in the broadest sense.

Correlation with both indexes is calculated with a one-year lag because competent institutions calculate indexes on the basis of the previous year.

Data on the volume of total foreign direct investments in Pakistan is published by the State Bank of Pakistan. Data on Chinese FDI in Pakistan is taken from China investment tracker made by *The American Enterprise Institute and the Heritage Foundation* (2019).

The period included in the analysis is maximum in terms of the inflow of foreign direct investments into the analyzed countries in the period 2005–2017. The exception is the HDI because the UNDP's oldest data for the countries included in the case study is given for 2009, which makes the time series shorter and therefore less statistically reliable.

The period statistically analyzed was longer than the official announcement and the formalization of the Belt and Road project in 2013. The first reason is the fact that the Chinese strategy of investing in infrastructure towards Europe had been adopted and commenced much before its implementation in a clearly defined project. The second reason is that statistical relevance depends on the length of the time series. Twelve years is a sufficiently long period, and the results of investments in the observed countries are shown.

## **4.2. Statistical method**

Since there are several dependent variables involved in the correlation, we will use the *Multiple Variable Analysis*. The Multiple Variable Analysis procedure is designed to summarize two or more columns of numeric data. It calculates correlation and covariance between all the variables with each other (Carey, 1998).

Therefore, it is easy to see all the relationships that mediate or are the result of the main correlation. Correlation coefficients measure the strength of the linear relationship between two columns on a scale from  $-1$  to  $+1$ . The larger the absolute value of the correlation, the stronger the linear relationship between the two variables.

Basically, the Multiple Variable Analysis is a multiplied coefficient of correlation, which relies on the method of ordinary smallest squares (OLS). The method also includes P-value which tests the statistical significance of the estimated correlations. P-values below 0.05 indicate statistically significant non-zero correlations at the 95.0% confidence level.

In the studies of FDI impact on the economy, the application of multiple regression is relatively common, which also includes several variables, but it is not adequate for this purpose. Multiple regression implies a larger number of independent and one dependent variable, while our research has a focus on reverse relations.

Prior to the research, the data panel option was experimentally tested. But similar to the previous studies, by involving a large number of countries in the panel the statistical relevance was getting lower, and the correlation was becoming less logical with every new country included in the panel. This has confirmed the choice of the statistical analysis of individual countries.

## **RESEARCH FINDINGS AND DISCUSSION**

The results of applying the Multiple Variable Analysis to the selected indicators of Pakistan are given in the following table.

Table 1. Effects of Chinese and total FDI on the economy of Pakistan

	Chinese FDI		Total FDI	
	correlation coefficients	P-values	correlation coefficients	P-values
GDP	0.7041	0.0072	-0.2754	0.3625
GDP per capita	0.7117	0.0064	-0.1754	0.0566
Unemployment	- 0.2824	0.3497	0.3874	0.1908
Export of goods	0.3448	0.2487	-0.4382	0.0342
Import of goods	0.5292	0.0503	-0.1184	0.7001
Export of services	0.5000	0.0819	-0.5002	0.0817
Import of services	0.3295	0.2716	0.4801	0.0969
Foreign debt	0.7558	0.2032	0.8270	0.0113
HDI+1	0.0307	0.0133	0.4055	0.0865
GCI+1	0.3515	0.0665	0.6015	0.0817
FDI	- 0.2026	0.5067	-	-

Source: author's calculation

With the statistical reliability of over 95% we can assert that there are:

- A very strong positive impact of Chinese FDI on GDP and GDP per capita;
- Positive effects of Chinese FDI on the import of goods.
- Positive, but not intense, the impact of Chinese FDI on the Human Development Index;
- A significant negative impact of total FDI on the exports of Pakistan's goods;
- A very negative impact of total FDI on Pakistan's foreign debt.

With a slightly lower but still significant statistical confidence of 90%, we note:

- Positive effects of total FDI on the HDI and the GCI;
- Positive effects of total FDI on the import of services
- Negative effects of total FDI on GDP per capita and commodity exports;
- Positive effects of Chinese FDI on Pakistan's Global Competitiveness Index.

*Economic growth* of Pakistan is strongly positively affected by Chinese FDI since the effects of total FDI on GDP per capita are negative. The reason is in different goals of investors. A challenging security environment and infrastructure shortages did not attract investment in production, and investment position of Pakistan was (and still is) very low. Usual sectors for investments in the unsecure environment are finance and trade, which allow quick profit and quick withdrawal. In contrast, investment in infrastructure always raises the level of domestic production.

*The Export of goods and export of services* are both negatively influenced by total FDI, and the export of services is positively affected by Chinese FDI. Export decreases when the MNC affiliation in the host country produces goods for the domestic market. The host country is used as a market, instead as a partner in production. The MNC, in that way, is lowering transport cost and avoids payment of customs duties. If the MNC goods prove to be more competitive than domestic goods, domestic production of related products will decrease as well as exports in the long run.

The impact of Chinese FDI has a positive correlation (but not always positive for the economy) with the *import of goods*. Trade statistics (UN Comtrade, 2019) show that this is not a result of the growth of imports from China as can be expected. A higher import of goods can be a result of increased production and/or increasing living standard.

The *over-indebtedness* as a result of Chinese loans is a potential problem and risk. Pakistan is one of the heavily indebted countries on the New Silk Road, which has already requested the IMF support to repay debts. The correlation between Chinese FDI and Pakistan's external debt is really high, more than 0.75 with not very high statistical significance. But, correlation with total FDI is even higher, and with higher statistical reliability. There are many investors in Pakistan besides China, and even more different mechanisms to transpose FDI into debt, but now the Chinese are in focus.

The potentially negative effect of Chinese FDI on foreign debt is not an insurmountable obstacle for the construction of necessary infrastructure facilities, nor for inclusion in the BRI. These negative effects can be avoided by a careful estimate, and most of the BRI countries have no problem with debt repayment. Eight out of the sixty-eight countries are not able to repay their debts: Pakistan, Montenegro, Laos, etc. (Hurley, Morris and Portelance, 2018, p. 4). These are usually small economies with large infrastructure projects. These investments are necessary for these countries by all criteria, and they alone would not be able to allocate these funds even with a decade of strong economic growth. So, very favorable Chinese loans are a good option. In addition to careful planning of the loan arrangement, these countries should insist on increasing the share of concessions or grants to

the loan in order to reduce the risk of debt repayment, which is also in favor of China (Hurley, Morris and Portelance, 2018, p. 4).

Total FDI has a positive impact on the *Human Development Index*. As it is mentioned, this composite indicator includes GDP per capita, health and educational system. According to the results, total FDI has negatively influenced GDP per capita, which means that a significant portion of foreign investment has been placed in programs for increasing literacy, the popularization of school attendance or health care. In this phase, Chinese investments are not directed in that way. Due to the significant impact of Chinese investments on GDP per capita as one of the Index components, Chinese FDI also has a positive effect on the HDI.

Both total and Chinese investments have significant positive effects on the Global Competitiveness Index. Since that index includes infrastructure, the effects of investments of Chinese companies are clear. High positive effects of total FDI on this index are a result of investment in the improvement of workforce skills, primary education, higher education, health, technological readiness and institutions. All these so-called *pillars* are included in the GCI index (WEF, 2018, pp. 317-319), and generally represent usual fields of interest of investors from the global West.

## CONCLUSION

The infrastructure-led foreign investment has provided significant economic gains. The positive effect of infrastructure development has never been disputed, but in the case of foreign-funded construction of infrastructure, opinions are divided.

In terms of specific research topics, the results show the validity of the hypothesis that Chinese foreign direct investment within the Belt and Road Initiative, has a more positive impact on the economies of the host countries than the usual effects of FDI.

The effects of Chinese investments may vary from country to country to a certain extent. However, as the goals and sectors of Chinese investment are very similar in all countries, the example of the impact on the economy of Pakistan points to the general tendencies and mechanisms that are driving this impact.

What specifically can the countries included in the BRI expect?

The countries included in the Belt and Road Initiative can expect *significant economic growth*, based on highly increased production, especially in the construction sector already known as a powerful economic stimulus.

*The Import of services* can also increase because the term “services” refers to the construction services, apparently provided by Chinese companies. In the case of Pakistan, this tendency is visible in high correlation with this indicator but because of low statistical reliability, this is just a tendency. This is expected, taking into

account the characteristics of Chinese investment to hire mostly their own resources in the broadest sense.

Contrary to that, the growth of *imports of goods* does not coincide with the increase in imports from China. It can be the result of an increase in production and income per capita.

Chinese FDI, usually in the form of a loan, has mixed effects on the *foreign debt* of a host country. Like every loan, there is a risk of over-indebtedness. Large-scale infrastructural projects often require enormous financial resources, and small countries (economically) are in danger of being unable to repay their debts. The credit ratings of countries within the BRI and their Debt/GDP ratio indicate that just a few countries are unable to repay debts to China.

This potentially negative effect is not an insurmountable obstacle for building necessary infrastructure facilities, nor for inclusion in the BRI. Besides careful planning of a loan arrangement, a recommendation is to favor concessions instead of loans in cases of disproportionately large projects in comparison with the size of a domestic economy, which is in the interest of both sides. “If infrastructure is a critical engine of growth in developing economies then debt financing is the fuel for that engine” (Hurley, Morris, Portelance, 2018, p.3).

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## **UTICAJ KINESKIH INFRASTRUKTURNIH PROJEKATA NA EKONOMSKI RAZVOJ ZEMALJA DOMAĆINA**

*Apstrakt:* Ovaj rad se bavi uticajem kineskih investicija u infrastrukturu unutar inicijative Pojasa i puta na privrede zemalja domaćina. Pakistan je izabran kao studija slučaja kao jedna od prvih destinacija kineskih direktnih investicija unutar pomenute inicijative. S obzirom na duži period ulaganja obezbeđena je dovoljna vremenska distanca za istraživanje. Bitan geografski položaj, uz Pojas i put svile, značajan obim kineskih investicija i činjenice o pozitivnim i negativnim posledicama širenja uticaja istočnoazijskog džina, čine polazište za odabir Pakistana kao studije slučaja. Uticaj stranih direktnih investicija (SDI) poreklom iz Kine kao i sveukupni efekti SDI na niz ekonomskih pokazatelja u zemlji domaćinu je izučavan korišćenjem multivarijantne metode analize. Tako su izvršena višestruka poređenja. Rezultati prikazuju snažniji i pozitivniji uticaj kineskih nego ostalih SDI na pakistansku privredu. Istovremeno na osnovu rezultat istraživanja može se zaključiti da je kao rezultat kineskih SDI došlo do značajnog izmena ekonomskih pokazatelja poput porasta uvoza i spoljnog duga prema Kini.

*Ključne reči:* Kina, Pakistan, SDI, Infrastruktura, Inicijativa Pojas i put.

*Received: 6 March 2019*

*Accepted: 4 April 2019*

## BOOK REVIEW

### “CHINA CONNECTS THE WORLD – WHAT’S BEHIND THE BELT AND ROAD INITIATIVE”

Wang Yiwei, *China Connects The World - What's Behind The Belt and Road Initiative*, The Center for International Relations and Sustainable Development (CIRSD), Belgrade, 2018, p.p. 264.

We have in front of us the second Chinese scientific book by Professor Wang Yiwei, entitled *China Connects The World - What's Behind The Belt and Road Initiative* devoted to the study of the Belt and Road Initiative. Professor Wang Yiwei is a professor at the International Studies School and Director of the Institute for International Affairs. He is also a Research Associate and Director of the Center for European/EU Studies and Senior Research Associate at the National Academy for Development and Strategy, as well as an Associate of the Chongyang Institute for Financial Studies at Renmin University of China. The author of this book is also known as “Mister Belt and Road”, due to a significant number of scientific papers he has published about the Belt and Road Initiative. In addition to the scientific work on the Belt and Road Initiative, Professor Wang Yiwei is also the author of the first Chinese scientific book dedicated to the Initiative Belt and Road, entitled *The Belt and Road Initiative – What China will Offer the World in Its Rise*.<sup>1</sup>

The book *China Connects The World - What's Behind The Belt and Road Initiative* is an important book, both to the academic community and to the countries on the Initiative's route in order to properly understand what the Initiative is and what is the most important, what the Initiative offers at the regional and global level. The book consists of a preface, introduction, ten chapters, conclusion and appendix. The chapters are titled as follows: 1. The world is connected, 2. The Belt and Road Initiative - the logic of globalization, 3. The Belt and Road Initiative - Civilization Logic, 4. The Belt and Road Initiative - Strategic Logic, 5. The Belt and Road Initiative - Economic Logic, 6. The Belt and Road Initiative - Political Logic, 7. The Belt and Road Initiative - Diplomatic Logic, 8. The Belt and Road Initiative - Perceptual Logic, 9. Chinese Wisdom incorporated in the Belt and Road Initiative, and 10. Global Wisdom incorporated in the Belt and Road Initiative.

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<sup>1</sup> This book was named book of the year in China in 2015.

To correctly illustrate the purpose of this book, we will first present what the Belt and Road Initiative is. Namely, the main purpose of the Belt and Road Initiative is the revitalization of the Silk Road, which represented the partnership between China and Europe, their cultural and trade exchange, until its break down which followed in the 15th century. The break of cultural and trade exchange between Europe and China was imposed by the Ottoman Empire which cut the Silk Road by the so-called 'Ottoman wall'. The fall of the Silk Road has influenced both the West and the East. Therefore, China believes it has a historical responsibility through the Belt and Road Initiative to renew the Silk Road and bring the center of civilization back to the Eurasian continent. In the past, the ultimate destination of the ancient Silk Road was Europe. Therefore, the focus of the Initiative is the Eurasian connection and cooperation. The Belt and Road Initiative includes 65 countries across Asia, Europe and Africa. The Eurasian connection is based on connectivity, inclusiveness, strategic synergy, cooperation in capacity improvement, mutual market development, business leadership, market functioning, state institutions and international standards. The five main objectives of interconnectivity in the implementation of the Initiative are the integration of politics, infrastructure, trade, finance and the hearts of people. These five objectives are accompanied by the establishment of six major economic corridors or six main areas, among which are: 1. Economic corridor the New Eurasian land bridge, 2. Economic corridor China-Mongolia-Russia, 3. Economic corridor China-Central Asia-West Asia, 4. Economic Corridor China-Indochina Peninsula, 5. Economic Corridor China-Pakistan, 6. Economic Corridor Maritime Silk Road. This multi-dimensional network of connectivity consists of railroads, roads, airlines, maritime routes, oil pipelines, gas pipelines, transmission lines, and communication networks. All this in order to establish a free trade zone, connectivity, inclusiveness and create a Eurasian market.

According to the author, it is China's responsibility to implement the 'New Silk Road' - the Belt and Road Initiative. Why China? China has a multifaceted identity: it is the largest developing country, the largest emerging country, the second largest economy in the world and an eastern socialist country. In the author's opinion, China will become a leading nation in the quest for humanity to create a new civilization through a new form of globalization - Globalization 3.0. Globalization 3.0 is the merging of the Chinese dream with the dream of the whole world, modeled on Confucian teaching. Namely, the new Chinese view of the world implies that all countries belong to the same family. It is the Confucian teaching that views the state as an extended family in which the state is a large family, and the family is a small state. The new form of globalization is Globalization 3.0 - the idea of the Internet for all, smart cities, as well as inclusive technology in which everyone will win. Globalization 3.0 will reduce the gap between the rich and the poor through three principles: 1. sharing - cooperation in which everyone wins, 2. sustainability - balanced development, inclusiveness and 3. internalization – putting down roots. It is China's

responsibility to create a new model of globalization through the restoration of Chinese civilization and other civilizations along the Initiative route. The author believes that the globalization promoted by the West has created such a society in which the rich are even richer, and the poor are even poorer. The expectations of the world from China are, according to the author, the result of a growing disappointment in American hegemony. So, the key issue of the Initiative and the “Dream of Chinese Civilization” is the question: How do we get the United States of America (USA) to accept this? The author believes that the USA would have difficulty reconciling with the rise of China, given that the United States is guided by a religious belief that they “never take the second place”. The author believes that the West is competitive which leads to a “clash of civilizations”. Thus the rise of China has always been seen as a threat. China will run, unlike the West (which is characterized by competitiveness) with the ‘Go’<sup>2</sup> strategy, which gives comparative advantages over the West. The author believes that Europe is a key factor in this idea and believes that “whoever conquers Europe, will conquer the world”.

In addition to everything exposed, we have to emphasize that the entire Belt and Road Initiative is based and leads exactly to the religious values of Confucianism: “Do not do unto others what you do not want done unto you”, Buddhism: “Never commit sin” and Taoism: “Road follows nature”. Namely, the Belt and Road Initiative draws the wisdom from the ‘Book of Change’<sup>3</sup> which is inspired by Confucianism.

This well-written scientific study of the Belt and Road Initiative is certainly significant for academic audiences, researchers of Political Science, International Relations, Politology of Religion, Economics as well as for political subjects who are interested in learning more about this global project. However, we must mention that the author should pay more attention to another “detail”. Namely, the Route of the Belt and Road Initiative includes 65 countries, of which more than 30 countries are Muslim countries. One of the burning issues facing China is precisely the situation in Xinjiang, a Province with a Turkish ethnic minority of Muslim religion – the Uyghurs. We believe China should first find a framework for a dialogue with the Muslim minority in its own country, in order to establish a dialogue, cooperation and connectivity with other countries along the route of the Belt and Road Initiative in which Muslims represent the majority.

*Mirela LONČAR*

<sup>2</sup> Game ‘Go’ is a strategy board game for two players, in which the aim is to surround more territory than the opponent. The game was invented in China more than 2,500 years ago and is believed to be the oldest board game continuously played to the present day.

<sup>3</sup> „Changes that are constantly repeated are called consistency. Encouragement and application are called connectivity” (Review, Part I, „The Book of Changes”)



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Research papers should not exceed 6000 words including abstracts, references, acknowledgements and footnotes.

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Please, provide an abstract of 100 to 250 words in English. The abstract should not contain any undefined abbreviations or unspecified references. Please, provide 5 to 10 keywords which can be used for indexing purposes.

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Tumulty, K. (2006, April). Should they stay or should they go? *Time*, 167(15) Retrieved from <http://content.time.com/time/magazine/article/0,9171,1179361,00.html>

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EC. (2002). Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (Directive on privacy and electronic communications), Official Journal of the European Communities L201 37–47, 31 July (European Commission, Brussels).

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Aleksandar Jazić, *Vanredne situacije i savremeni trendovi razvoja sistema zaštita*, broširano, 2017, 128 str.

Ivan Dujić, *Novi svet i Evropa: od početka procesa globalizacije do globalne finansijske i migracione krize*, broširano, 2017, 322 str.

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