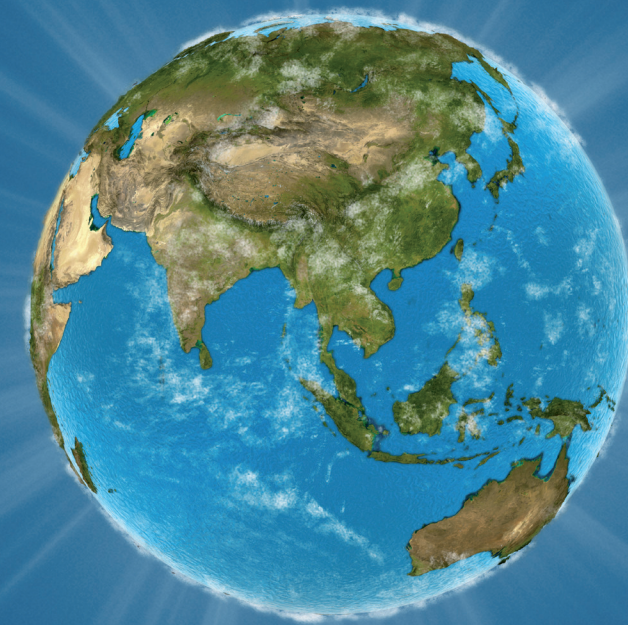


Edited by LUIS TOMÉ

EAST ASIA TODAY



Preface by ROBERT SUTTER

FÁTIMA AZEVEDO ALEXANDRE CARRIÇO MARIA RAQUEL FREIRE CARLOS GASPAR DIANA SANTIAGO DE MAGALHÃES NUNO SANTIAGO DE MAGALHÃES CARMEN AMADO MENDES NUNO CANAS MENDES HENRIQUE MORAIS MIGUEL SANTOS NEVES RUI PAIVA RUI P. PEREIRA JOSÉ FÉLIX RIBEIRO HEITOR BARRAS ROMANA ANTÓNIO EMÍLIO SACCHETTI JORGETAVARES DA SILVA RUI TRINDADE

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EAST ASIA TODAY

«(...) This volume contains many in-depth and well documented assessment that are often theoretically informed. They will be welcomed by other specialists in the field as well as by a wide range of students, journalists, business people, government officials and other interested readers endeavoring to come to better understandings about key regional trends.

This book makes no pretense of answering all the many questions that surround the ongoing debates about developments in East Asia. Rather, it provides portals through which readers can enter and come to a much deeper and clearer understanding about salient trends and issues.

(...) In sum, the reader is encouraged to explore the assessments in this valuable volume with an open mind. The findings here allow for careful and balanced consideration of leading aspects of contemporary East Asia.»

Professor Robert Sutter, School of Foreign Service at Georgetown University (from this book's Preface)

«We cannot be successful today in any political or entrepreneurial activity worldwide if we do not properly understand the dynamics, capabilities and contradictions of East Asia, a region whose importance has grown tremendously in the last 30 years. Though this book does not provide solutions, it presents the different scenarios and opens new perspectives for those who take an interest in this subject. It is indeed an excellent collective research project on contemporary East Asia of utmost relevance. »

General Garcia Leandro, University Professor and Former Macao's Governor



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Preface

Robert Sutter

East Asia attracts growing interest in the West. The region is the world's hotbed of economic growth, led by burgeoning China aided by more advanced Asian economies investing heavily in manufacturing and trading networks involving China. Western entrepreneurs clamor to join the China wave.

Though the West is focused more on security problems in the Middle East and the broader war on terrorism, East Asia looms large in western and international security calculations on account of the on-going crisis caused by North Korea's nuclear weapons development and the on-again off-again tensions in the Taiwan Strait. Both areas deeply involve the United States, the world only superpower, and China, Asia's leading power. The tensions over Taiwan are particularly dangerous as both Chinese and U.S. leaders have made it clear that they are prepared to engage in combat with one another if their core interests are challenged. Such a war between these two great powers would make recent wars in Afghanistan and Iraq seem very small by comparison. Once started, the war would be difficult to bound and would likely have catastrophic effects regionally and globally.

The order in East Asia is in a state of transition and the end point is not clear. Fluidity and flux in such an area of great international importance means that western and other international observers need to watch closely for signs and trends of change that could have important implications in other parts of

the world. Will China's rise undermine the leading position held by the United States in post-cold war East Asia? Will East Asia's economic importance continue to rise at the recently rapid pace, and what will this mean for the developed countries of the West? How will China and Japan, East Asia's major powers, resolve their many contentious differences, and what role will the major flanking powers, Russia and India, play in the evolving East Asian order.

The driving forces behind East Asian developments are the region's independent minded and nationalistic governments. Fortunately, most of them see their interests and legitimacy resting heavily on effective nation-building which requires trade, investment, and stability (North Korea and Burma are notable exceptions to this rule). They tend to remain wary of one another, though they see their interests best served by emphasizing the positive in an ever widening array of regional groupings. The latter are most effective in following and dealing with the consequences of the broadening webs of economic relationships tying together East Asian states. The regional groups also help East Asian governments deal with important transnational issues affecting the well being of the peoples of the region. These issues involve terrorism, energy security, environmental degradation and climate change, and infectious diseases. Despite all the activism in East Asian groupings, the regional governments are reluctant to give up much authority or sovereignty to regional organizations. Thus, despite their growing number, Asian regional groups generally remain weak and prone to decisions reflecting the lowest common denominator of the member states.

Because of rapid change in East Asia influenced by many variables, it is hard to be conclusive about regional trends and developments. As a result, there are serious and on-going debates among specialists on several key matters. Is the United States in decline in the region? Has China's rise reached a point of challenging US leadership in East Asia? Is Japan's greater international activism and assertiveness a reflection of greater power and influence in East Asia? Is the North Korean nuclear issue under control and moving toward resolution or will tensions break out again in the near future? How lasting is the stability in the Taiwan Strait brought on by the election of a more conservative Taiwan president in 2008? What significant actions in East Asia can be expected from rising India and Russia, and such important middle powers as South Korea and Indonesia? Is Asian multilateralism the wave of the future for the Asian order or merely a chimera with little substance?

Against this background, it is most welcome that a well qualified group of specialists from Portugal have joined the array of international experts assessing

East Asian trends and their implications. This volume contains many in-depth and well documented assessment that are often theoretically informed. They will be welcomed by other specialists in the field as well as by a wide range of students, journalists, business people, government officials and other interested readers endeavoring to come to better understandings about key regional trends. First providing broad reviews of the region from security and economic perspectives, the volume then dives into country-specific studies. China looms large here with four specific articles and with China also featured in articles dealing with Russia and Japan. The United States, India, Japan and Russia get one article each and a short survey covers Southeast Asia. There are many trouble spots in East Asia, and four chapters in this volume deal respectively with Taiwan, the Korean peninsula, secure sea communications, and the salient aspects of human security.

This book makes no pretense of answering all the many questions that surround the ongoing debates about developments in East Asia. Rather, it provides portals through which readers can enter and come to a much deeper and clearer understanding about salient trends and issues.

Adding to this collective wisdom, this author would like to remind the reader to keep the recent changes in East Asia in some perspective. In particular, the reader is advised to view with some skepticism forecasts of US decline and the rise of China as the region's leading power.

The decline of the United States as the region's leading power since the end of World War II has been repeatedly forecast, but these forecasts have always been found to be wrong. The United States was seriously challenged by the Sino-Soviet alliance backing North Korea's assault on South Korea in June 1950, by the major defeat of US and allied forces in the wars in Cambodia and Vietnam in 1975, and by Japan's ascendance as Asia and the world's most effective economic power in the 1980s. In each instance, commentators saw the US being displaced by the rising power as East Asia's leader. The commentators tended to focus on the strengths of the rising power (e.g. China, the USSR and later Japan) and on the weaknesses of the United States (e.g. military weakness and failure and economic ineffectiveness). This kind of calculus did not take appropriate account of the weaknesses of the rising powers and of the strengths of the United States.

Similarly unbalanced assessments prevail in discussions of East Asia today. Those seeing decline of the United States highlight the many weaknesses of the US position in the region and highlight the strengths of Asia's rising powers, notably China. What they tend not to do is give careful review

of China's weaknesses and US strengths. In particular, it is true that the United States faces many challenges and complications influenced by prevailing trends in Asia and pressures at home. The US image in the region has declined in recent years and US foreign policy continues to be widely criticized. However, US ability and willingness to serve as Asia's security guarantor and its vital economic partner appear strong and provide a solid foundation for continued US leadership in the region. No other power (including rising China) or any regional organization is even remotely able, much less willing, to undertake these commitments.

In sum, the reader is encouraged to explore the assessments in this valuable volume with an open mind. The findings here allow for careful and balanced consideration of leading aspects of contemporary East Asia.

Introduction

Luis Tomé

The rise in international politics of East Asia - the geographical area including Northeast and Southeast Asia – as a macro-region is a modern and ongoing phenomenon, whose regional identification framework is yet not clearly defined. The crossed influences of History, Politics, Economics and Culture make East Asia a very complex and diversified area. However, and despite the heterogeneous nature of the region and its countries, a regional desire has been emerging to give political and institutional voice to East Asia, though its composition and borders remain ambiguous.

Free of both colonial domination, which lasted centuries, and the influence of the superpowers during the decades of the Cold War bipolarity, East Asia is now in an era that Muthiah Alagappa (1988:4) describes as “post-colonial”. This does not, however, imply going back in time or is a synonym of regional isolation: on the contrary, today the East Asia region and its nations are more connected to other regions and to the global international system at all levels and in all possible dimensions. On the other hand, not only do “foreign” actors (namely, the regional balancer, the United States) have a great influence on regional matters, but East Asian countries (namely the re-emerging China, Japan, Russia and also South Korea, and the ASEAN group) and the region itself are more important in the framework of international relations. Yet, what happens today is that by being more closely linked to the global system, East

Asia is also more autonomous, which implies that its people have more power and control over their interests, objectives and destiny.

For a long time, as John Gerard Ruggie (1993:4) declared, this region was considered an “unworthy” field for theoretical debate on international relations, considering that, in the region, constructs such as the balance of power, hegemony, economic interdependency, identity, social reconstruction, security, State, regional integration or regime theories were not entirely adequate neither to explain nor to foresee the region’s future. Applying any of these theories to the evolution of East Asia is still being tested and debated, due to the region’s extreme dynamics and complexity. However, academics, political leaders, diplomats and journalists have shown an undeniable growing interest in East Asia, since the region is nowadays much more important in the international system, able to deeply influence the world history of the 21st century.

The region’s nations have been taking advantage of the relative regional stability and their economic growth in order to attempt increasing the well-being of their peoples, as well as their political, economic and strategic status. In truth, it’s in East Asia that one is able to see the most rapid growth of power and influence in international politics. Several poles of economic power, each with a different level of impact in global and regional politics, are in the region, namely, Japan, China, South Korea, Russia, Taiwan and ASEAN¹. Three re-emerging powers, historically important and with political and strategic ambitions at a global scale are in that very region, namely, China, Japan and the Russian Federation. Thus, the relations and the exchanges with the region’s nations are today absolutely vital for “foreign” powers such as the US, EU, India and Australia, as well as for other Asian, African, Middle Eastern and Latin American countries.

On the other hand, the great issues in today’s international affairs - from terrorism to environmental degradation, from WMD proliferation to the fight against poverty and sub development, from pandemics and infectious diseases to the unpredictable behaviour of re-emerging powers, from overpopulation and massive urbanization to dependency and energy security, from transnational criminal activity to the weakened/failed States, from the promotion of democracy and human rights to the effects of globalization, from government repression over its population to natural catastrophes – are all present and closely linked to the region, which means that the solutions for world issues are also dependent on East Asia. Today, no one knows exactly what the future

1 *Association of Southeast Asian Nations.*

will be like; yet, we all know that the world's future depends greatly on East Asia, the interaction within and with the region.

East Asia today is marked by an extensive and rather dense network of elements which make this a very complex region, which include:

- the extraordinary economic growth of most of the region's nations and the ongoing increase in regional share in the World GDP, turning East Asia into the most dynamic region in the world, both at economic and commercial levels;
- the promotion of all types of interdependency and the significant increase of multilateralism and regional institutional (ASEAN, ASEAN+3², 6-Party talks³), pan regional (EAS⁴, ARF⁵) and inter-regional (APEC⁶, ASEM⁷, FEALAC⁸, AASROC/NAASP⁹) cooperation, as well the non-governmental process or "Track II" (NEACD¹⁰, Shangri-la Dialogue, BFA¹¹, PECC¹², PBEC¹³, CAEC¹⁴, CSCAP¹⁵),
- an historical legacy of rivalry and suspicion, as well as territorial and border struggles (for example South Kurilles/Northern Territories, the Takeshima/Tokdo islands, the Senkaku/Diaoyutai islands, the Paracel Islands, the Spratley Islands, and the South China Sea)
- persistent stigmas of the Cold War (Korea and Taiwan), which can greatly affect international security;
- the powerful strategic presence of the US, trying to maintain a certain *pax americana*;

2 ASEAN Plus China, Japan and South Korea.

3 Joining the US, China, Russia, Japan, South Korea, and North Korea to solve peacefully the problem of DPRK nuclear program, since 2003.

4 *East Asia Summit*

5 *ASEAN Regional Forum*.

6 *Asia-Pacific Economic Cooperation*.

7 *Asia-Europe Meeting*

8 *Forum for East Asia-Latin America Cooperation*.

9 *Asian-African Sub-Regional Organisations Conference / New Asian-African Strategic Partnership*.

10 *Northeast Asia Security Cooperation Dialogue*.

11 *Boao Forum for Asia*.

12 *Pacific Economic Cooperation Council*.

13 *Pacific Basin Economic Council*.

14 *Council for Asia-Europe Cooperation*.

15 *Committee on Security Cooperation in the Asia-Pacific*.

- the economic, political and military re-emergence of China, affecting the regional and global balance of power;
- the gradual strategic expansion of Japan, which is gradually letting go of its conventional self-restraints;
- the rise of Russia, South Korea and the ASEAN group, as well as that of India and Australia, as main actors in East Asian affairs;
- the increase in the agenda and security concerns, including non-conventional issues such as unregulated population movements, infection diseases, piracy, transnational crime, environment degradation, energy safety, and economic-financial crisis;
- the coexistence of established democracies (Japan), ongoing democratic processes or still relatively frail ones (Russia, Mongolia, South Korea, Taiwan, the Philippines, Indonesia, Thailand, and East Timor), semi-democratic regimes (Singapore, Malaysia, Brunei and Cambodia), formally communist regimes (China, North Korea, Vietnam, and Laos) and military dictatorships (Myanmar), all characterized by a growing nationalistic feeling;
- the general increase in defence budgets and in military capacities in the region;
- a visible and general improvement of bilateral relations and the establishment of new strategic partnerships and new Free Trade Areas (FTAs);
- a greater exposure of East Asian “*developmental states*” to the pressures of globalization, a greater challenge for the region’s governments and peoples;
- and an East Asian self-conscious pursuit and community building efforts among most regional actors.

International order in East Asia has been rapidly and deeply changing. The regional environment is today frankly much more positive than previously but the most optimistic expectations which foresee the 21stc as “the century of East Asia” and the region as “The new gravity pole of world power” coexist with negative scenarios predicting the “Balkanization of East Asia” or portraying the region as “ripe for rivalry”. Within a framework of rapid and deep changes, the political, strategic and economic options both of East Asian countries as well as of other “foreign” actors have been reconsidered. However, the direction of these changes and interactions in the region are still volatile and uncertain.

As a matter of fact, today's uncertainty is still the only certainty in the very confident East Asia.

Defining East Asia

All concepts have their history, geography and, why not, their motives. Throughout the centuries, for instance, the Europeans used to name all the territories beyond the Middle East and the Urals as “Far East”, or simply, “Orient”, and the geographical boundaries were always rather ambiguous, since the denomination was more closely linked to a cardinal direction than to a geographical area. This designation was obviously coming from a European-centred world and where those territories were in relation to Europe, making it impossible to survive History (Tomé, 2001: 18-19; Joyaux, 1991: 15-16). Yet, even if we let go of all old-fashioned and inadequate concepts, there is still a number of possible designations for the Asian sub-regions, which generally leads to confusion and controversy.

Asia is commonly divided into five major regions: Western Asia, Central Asia, South Asia, Northeast Asia and Southeast Asia. Equally common are other references to Asian sub-regions, such as Middle East, Minor Asia, Indian Sub-continent or Indochina. However, the limits and the nations belonging to these regions do not always coincide. They depend on the criteria (geographical/geological, cultural/civilizational, historical-ethnical-linguistic, political, economical and commercial) and the countries included in the regional groups.

The *East Asia* concept has also different connotations. In some cases it designates the countries of Northeast Asia – the UN, for instance, define Eastern Asia in a very restrict way, including only China, the SARs of Hong Kong and Macao, North Korea, South Korea, Japan and Mongolia.¹⁶ In other cases, Mongolia is part of Central Asia, not East Asia or Northeast Asia, while the Russian Federation is more commonly included in the European countries rather than in Central Asia, Northeast Asia or East Asia. On the other hand, East Asia is frequently confused with Asia-Pacific, particularly in American references. In fact, the concept of Asia-Pacific is either more restrict (includes only the countries of Northeast and Southeast Asia) or more enlarged (embracing all the countries of the Pacific Ocean, Asia, America and Oceania, as

16 United Nations, *Composition of macro geographical (continental) regions, geographical sub-regions, and selected economic and other groupings: Eastern Asia*, url: unstats.un.org/unsd/methods/m49/m49regin.htm (consulted in January 3, 2008).

partially happens in APEC), depending on the source. Today, the term East Asia is gradually becoming more usual, namely among the region's nations. Their goal is to build a true East Asia Community, thus setting themselves apart from "other" regions. The truth is that even in those cases the limits of East Asia are still ambiguous. Sixteen countries have participated in the East Asia Summits (EAS), with the inclusion of three "non-residents" - India, Australia and New Zealand - and the exclusion of "resident" countries such as Russia, North Korea, Taiwan, Mongolia and Timor-Leste!

This evidences the great difficulty and variety in defining East Asia, which requires an explanation of our own conception of East Asia in this book.

Considering that our main criterion is geographical, our definition of East Asia includes all the nations whose territory is within Northeast and Southeast Asia, with no "exclusions" or "inclusions" of a political nature or other, thus covering the eighteen countries, from the Russian Far East to Timor-Leste, and two sub-regions: Northeast Asia, including Russia, Mongolia, North Korea, South Korea, China, Japan and Taiwan; and Southeast Asia, including the ten ASEAN countries - Indonesia, the Philippines, Thailand, Myanmar, Malaysia, Singapore, Brunei, Vietnam, Laos, and Cambodia - and Timor-Leste, also seeking ASEAN membership.

Map 1. East Asia



Though the geographical limits of East Asia are hard to define, it is even more difficult to find regional identity features. In fact, the region's defining features are heterogeneity and complexity. Factors such as history, geography, demography, religion, standard of living, political regime, development level, among others, demonstrate the enormous diversity of East Asia, as evidenced in Table 1. So, what distinguishes East Asia in the international system? Though not fully answering this question, there are two key elements we must mention.

Table 1.
East Asia Countries and “Extra-Regional” Main Actors: Comparative data

Country/Group	Area (000 sq km)	Population (million)	Political Regime*	Main Religion	UNDP Human Development 2007-08 Ranking	Life expectancy at birth (years)
EAST ASIA						
Russia	17,075	140.7	Democracy	Orthodox Christian	67	65.0
Mongolia	1,564	2.9	Democracy	Buddhist Lamaist	114	65.9
North Korea	120	23.4	Communism Stalinist	Suppressed - traditionally Buddhist and Confucianist	n.a.	66.8
South Korea	99	49.2	Democracy	Buddhist and Christian	26	77.9
Japan	379	127.2	Democracy	Shinto and Buddhist	8	82.3
China	9,596	1,330.0	Communist	Atheist - mainly Taoist	81	72.5
Taiwan	36	22.9	Democracy	Buddhist and Taoist	n.a.	77.5
Timor-Leste	15	1.1	Democracy	Christian Catholic	150	59.7
Myanmar/Burma	679	47.7	Military Dictatorship	Buddhism	132	60.8
Brunei	6	0.38	Constitutional Monarchy	Muslim	30	76.7
Cambodia	181	14.2	Constitutional Monarchy	Buddhist	131	58.0
Indonesia	1,919	237.5	Democracy	Muslim	107	69.7
Laos	236	6.6	Communist	Buddhist	130	63.2
Malaysia	330	25.2	Semi-Democratic	Muslim	63	73.7
Philippines	300	92.6	Democracy	Christian Catholic	90	71.0
Singapore	0.7	4.6	Semi-Democratic	Buddhist	25	79.4
Thailand	514	65.4	Democracy	Buddhist	78	69.6
Vietnam	330	86.1	Communist	Buddhist	105	73.7
ASEAN GROUP 10	4,495	580.28	—	Buddhist and Muslim	—	69.5
“NON-RESIDENTS” MAIN ACTORS						
United States	9,826	303.8	Democracy	Christian Protestant	12	77.9
India	3,287	1,147.9	Democracy	Hindu	128	63.7
Australia	7,686	20.6	Democracy	Christian Catholic	3	80.9

Note: * The author is responsible for the description of the political regimes and is obviously simplifying a very diverse and complex reality.
Source: CIA *World FactBook*, UNDP *Human Development Report 2007-2008*.

The first is obviously geography: regardless of diversity, the several peoples and nations are all in a certain area of the globe, more precisely, within the space we call East Asia. Historically, the interactions with nearby peoples were always more intense as a consequence of geography, since there are not the constraints associated to the “tyranny of distance”. Geography does not determine identity or the level of interaction among peoples, but since the human being is bound by space and time, being aware that one belongs to a common place does distinguish those who are and those who are not. Thus, a possible means for defining East Asia (as well as Northeast Asia and Southeast Asia) is the separation between those who are geographically “resident” in the region from those who are not. This is linked to a second element, which is what Barry Buzan (1998:70-72) defines as interactions between the composing parts, in four main areas: the type of interaction involved, the attitudes towards that interaction, its intensity and content (or what defines it).

As a matter of fact, despite its extreme diversity, there are certain elements and characteristics – such as common historic experience and memory, the idea of “ourselves” in face of the “others”, the State’s historic role, the *developmental state* character, the concerns with sovereignty and security, political authority, the priority given to stability and economic development, the awareness of common issues requiring regional solutions, the appeal to “Asian values” and the idea of regional “community” – allow us to visualize what we could vaguely call East Asia identification, which goes beyond the fact of belonging to a geographical area. As regional identification/identity is still in its initial stage, it is mostly a result of recent historic experience and geopolitical/geostrategic and geoeconomic ideas. This regional identification/identity is much more consolidated in Southeast than in Northeast Asia due to the ASEAN process.

This is particularly important in our globalized era, since regions and macro-regions have emerged with much more strength and have defined themselves in opposition to others. Thus, the appeal to “Asian values” – in opposition to “Western values” – to the “Asian Century” and the “Pacific Age” or the idea of building an “East Asian Community” both are and reinforce a certain regional identity, i.e. highlight what might be described as the self-reflexive element of regionalism and its inevitable connection to larger global processes (Beeson, 2007: 10). This way, the self-conscious pursuit and the development of regional institutions and dialogue is a defining part of the international order in East Asia today.

Obviously, this does not imply that East Asia as a whole is undergoing a process of regionalization: despite its visible progress in multilateralism and

regional cooperation and the constant appeals to the idea of community, there is still a long way to go before East Asia is truly a unified region, if ever that will happen. Yet, if historically the regional definitions were given by foreigners – with the exception of the ancient sino-centred order and the Japanese “*Great East Asia Co-prosperity Sphere*” – today a kind of regional awareness is growing among East Asian nations while “other” world actors also gradually accept East Asia as a macro-region of the world. On the other hand, the interactions and interdependency among the countries and sub-regions of Northeast and Southeast Asia are increasing significantly, reinforcing a certain identification of East Asia as a region in global context. Paradoxically and simultaneously, the link and relations of East Asian countries, groups and institutions with countries and organizations of other regions are also rapidly increasing, making “regional borders” much more fluid and uncertain.

About this book

The main goal of this book is to characterize and analyze East Asia today through a series of essays written by some of the most prominent Portuguese researchers who have been studying and analyzing the region, some of whom have even worked or are working in that region. The book includes sixteen essays from eighteen experts, as well as the Preface by Robert Sutter.

So as to ensure a variety of themes, the essays are relatively short and concise, though deep and on current East Asia affairs. Our objective is not to impose any specific point of view or methodology, which may lead to different essays evidencing diverse or even contradictory positions. In our opinion, though, this is one of the most interesting features of this book: to be able to make visible the multiple issues of East Asia today through multiple perspectives. The authors’ only concern is to describe the facts and the possible explanation(s) without the restraints of an imposed perspective. We honestly believe this approach benefits the analysis of the complex and diversified East Asia. This also explains the absence of the typical final conclusions: these are left for the readers who will be able to reflect on the present and future path of East Asia based on the several possibilities and explanations the essays propose.

The book is divided into three sections. The First, “*Regional Overviews*”, sets the framework of the region’s current situation. The two essays included are focused on economy and security/geopolitics. In one of them, I characterize and analyze the contemporary East Asian security system and geopolitical

order, evidencing the “two faces” in the region. The other, by Henrique Morais, emphasizes the region’s main economic and trade trends through their description and weight in the global context and showing the most important regional challenges at economic level.

The Second Part of the book is dedicated to “*Main Actors*”. Inevitably, rising China deserves special attention, which explains that four articles are dedicated to this country: Carmen Mendes analyzes national motives, approaches and goals of China’s foreign and East Asian policies; Rui Paiva writes about the economic and financial potential and restraints of present China; Alexandre Carriço explains China’s defence policies and military modernization; and Félix Ribeiro, Fátima Azevedo and Rui Trindade analyze Chinese geo-economic dilemmas on energy. Heitor Romana also writes about China but compares it to the Russian Federation in terms of “techno-nationalism” influence on decision-making processes of both powers. Russia’s policy, priorities and relations with East Asia are the theme of Maria Raquel Freire’s essay, while Miguel Santos Neves dedicates his article to Japan’s foreign and security policy and its implications for relations with China and East Asia regionalism, and Nuno Canas Mendes explains how far the ASEAN group is a “main actor” in East Asia today. Due to their prominence in regional affairs, two “non-resident” main actors will be also discussed in this second part: the United States, whose options and policies towards East Asia are at the core of Carlos Gaspar’s article; and India, the re-emerging neighbouring power whose links and influence in East Asia are the theme of the essay by Rui Pereira.

The Third Part includes four articles on specific issues which have raised “*Discord and Cooperation*”. Therefore, Jorge Tavares da Silva analyzes the quite sensitive and frail *status quo* in the Taiwan Strait; Nuno Santiago de Magalhães debates the “poisoned cooperation” in Korea; Admiral António Emílio Sacchetti describes the sea lines of communication and trade in Asia-Pacific region, clarifying their importance and the challenges they represent to the region’s actors; and, finally, Diana Santiago de Magalhães discusses the potentials and constraints of Human Security in East Asia today.

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Finally, a few words to our readers. We, the co-authors, do not consider this a concluded task but simply a contribution, among many others, that seeks not only to provide substantial analysis but also enhance our own understanding of contemporary East Asian affairs. As a matter of fact, the dynamic region will always demand further and careful investigation, and several of our findings may also require refinement, development and even reformulation. The other contributors and I hope our readers find this book as useful and stimulating as it was for us to produce it.

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Part I. Regional Overviews

Security and Geopolitics in East Asia Today: One Region, Two Faces

Luis Tomé

East Asia's power structure and security parameters are changing at a dizzying speed. Despite its relative stability and obvious emergence in the international scene, order¹ in East Asia is volatile and unpredictable because it is under pressure from complex and sometimes conflicting dynamics. Therefore, security is still a main concern among the peoples in the region.

The problems and prospects of East Asia's security and geopolitics have been addressed around four major issues. Firstly, the region has been studied and quoted within the scope of the widest discussion on the agenda, the concerns, tools and the concept of security itself (Alagappa, 1998: 27-64; see also Dannreuther, 2007; and Baylis *et al.*, 2007). A second debate is that of the evolution and future of East Asia, which pessimists see as a region "*Ripe for Rivalry*" or "*Europe's Past Will Be Asia's Future*" (Friedberg, 2000 and 1993-94) and optimists describe as thriving, saying that the 21st Century is the "East Asian Century", and suggest that the security problems and dilemmas in the

1 No definition of "international order" has been universally accepted by IR scientists. Nevertheless, "international order" in this essay follows Muthiah Alagappa's (2003: 39) definition: «*a formal or informal arrangement that sustains rule-governed interaction among sovereign states in their pursuit of individual and collective goals*» that makes for «*a predictable and stable environment in which states can coexist and collaborate in the pursuit of their national, regional, and global goals, differences and disputes can be adjusted in a peaceful manner, and change can occur without resort to violence*».

region are less serious than conventionally described (Acharya, 2003-04 and 2001). The third discussion focuses on the reasons underlying East Asia's relative and extraordinary stability, the reasons being the balance of power, the role of US supremacy, the importance of the region's strategic history and culture, the democratic evolution, and the priority given to economic development by the referred countries as well as the increase in multilateralism and regional cooperation. Yet, some suspect East Asia's "tranquillity" is just virtual or temporary (on this discussion see, for example, Ikenberry and Mastanduno, 2003; and the "*Strategic Asia*" series from the NBR). And a fourth debate deals with the definition and concept of the regional security system: which is the most appropriate concept to describe security in East Asia - *competitive security*, *cooperative security*, *collective security*, *common security*, *comprehensive security* or *community security*?

There are, of course, several perspectives under which scholars and experts analyze international relations, security and regional occurrences, and in doing so, those debates often reveal a competition among theories/ paradigms, namely among those who propose the triad of realism, liberalism, and constructivism (Katzenstein and Sil, 2004: 3-4). In the past few years, however, an increasing number of authors and works have embraced intellectual differences and more eclectic perspectives, which recognize that studying and analysing East Asian security and geopolitics requires the inclusion of items such as power, interests, material resources, economics and interdependence, international structure, institutions, history, culture, ideas, social factors and identity².

2 As, for example, William H. Overholt (2008), "*Asia, America, and the Transformation of Geopolitics*"; Robert Sutter (2007, 2005 and 2003), respectively "*Chinese Foreign Relations: Power and Policy Since the Cold War*", "*China's Rise in Asia. Promises and Perils*" and "*The United States and East Asia. Dynamics and Implications*"; Bates Gill (2007), "*Rising Star: China's New Security Diplomacy*"; Richard J. Samuels (2007), "*Securing Japan: Tokyo's Grand Strategy and the Future of East Asia*"; Mark Beeson (2007), "*Regionalism and Globalization in East Asia*"; Berger, Mochizuki e Tsuchiyama (Eds) (2007), "*Japan in International Politics: The Foreign Policies of an Adaptive State*"; Joshua Kurlantzick (2007), "*Charm Offensive: How China's Soft Power Is Transforming the World*"; Kenneth B. Pyle (2007), "*Japan Rising: The Resurgence of Japanese Power And Purpose*"; Ash, Shambaugh e Takagi (Eds.) (2006), "*China Watching: Perspectives From Europe, Japan, and the United States*"; Abramowitz and Bosworth (eds) (2006) "*Chasing the Sun. Rethinking East Asian Policy*"; Rocher and Godement (Dir.) (2006), "*Asie entre Pragmatisme et Attentisme*"; David Shambaugh (ed.) (2005) "*Power Shift. China and Asia's New Dynamics*"; Michael Yahuda (2004) "*International Politics of Asia-Pacific*"; Suh, Katzenstein e Carlson (eds) (2004) "*Rethinking Security in East Asia. Identity, Power and Efficiency*"; Ryosei and Jisi (eds) (2004) "*The Rise of China and a Changing East Asian Order*"; Muthiah Alagappa (ed.) (2003, 2001 and 1998), respectively, "*Asian Security Order: Instrumental and Normative Contractual Features*", "*Coercion and Governance: the Declining Political Role of the Military in Asia*" and "*Asian Security Practice. Material and Ideational Influences*"; Ikenberry e Mastanduno (eds) (2003), "*International Relations Theory and the Asia-Pacific*"; Sheldon Simon (ed) (2001) "*The many faces of Asian Security*"; or the so-far seven "*Strategic Asia*" volumes (from 2001-02 to 2007-08) in The National Bureau of Asian Research (NBR)'s Strategic Asia series.

The purpose of this essay is not to take a position in terms of those debates but to characterize contemporary East Asian security and geopolitical order by: a) distinguishing some of the main features of the regional security system; and b) explaining the regional structure of power and security complex. It shows that the emerging order in the region is a very complex and hybrid system that shares elements of balance of power and complex interdependence, competitive security and cooperative security, and multilateralism with bilateralism. Moreover, it shows that “traditional” concerns about security meet “new” ones, and that the elements of anarchy and competition meet elements of order and engagement in the region.

I. The broadening concept of regional security and the emergence of “new” security issues

One of East Asia’s most impressive developments is that the risk of conflict among the countries has decreased significantly in the last two decades. This is something extraordinary for the region. However, a lot of “traditional” security dangers still persist: the concern with China’s re-emergence, Japan’s renewed geostrategic ambitions and the regional status/role of the United States; regional fragmentation risks around the two major competitive axis in the region; historical hostilities; cultural differences and socio-economic gaps; the different political regimes, including some autocratic regimes, all characterized by an increasing nationalism³; the issue of Taiwan; North Korea nuclear arms and the subsequent risks of WMD proliferation; the significant and generalized increase of defense budgets and military capacities in the region, besides the lack of transparency in terms of real military expenses, in particular, by emerging China; the division of the Korean Peninsula; rivalries over diminishing energy resources (from sources rich in carbohydrates to their exploitation and choke-points), including the disputes over the potentially resource-rich South China Sea, an area also crucial for maritime sea lines of actors such as the ASEAN group, China and Japan (see on this Admiral Sacchetti’s essay in this book); the several separatist movements and tendencies (namely, Tibet and Xinjiang in China, Mindanao in the Philippines, and Aceh and Irian Jaya in Indonesia); or even the several border or territorial disputes – particularly, the South Kurilles/Northern Territories (Russia *vs* Japan), the Takeshima/Tokdo islands (Korea *vs*

3 See Heitor Romana’s essay in this book about Chinese and Russian techno-nationalism

Japan), the Senkaku/Diaoyutai islands (Japan *vs* China/Taiwan), the Paracel Islands (China *vs* Vietnam) and the Spratley Islands (concerning China, Taiwan, Vietnam, Philippines, Brunei, Malaysia and Indonesia) in the South China Sea - as well the disputed sovereignty areas in the Yellow Sea, the Sea of Japan, the Gulf of Tonkin, and the South China Sea.

Noteworthy is also the notion that regional security has broadened beyond those “traditional” issues and concerns in order to include a wide variety of “non-traditional” security problems, which “are *primarily non military in nature and constitute a broader set of security considerations relating to survival, resource allocation and the health of the planet. They are, therefore, unlikely to be resolved by military force or ameliorated by traditional security approaches*” (Dupont, 2001: 32). These new security issues include terrorism, transnational organised crime, drug trafficking, sea piracy, cyber crime, human trafficking, arms smuggling, money laundering, international economic crime, energetic dependence and access to energy resources and markets, unregulated population movements, infectious diseases, weakened/failed States, environment degradation, and economic-financial crisis.

Some of these are not really new: namely, since the mid 1970s, there have been innumerable appeals to redefine security so as to include economic, environmental and other “non military” aspects, as well as a more embracing concept of security which already existed in several East Asian countries even during the Cold War, as was the case of Japan or the ASEAN countries. It is certain that broadening the security agenda to include concerns not involving potential violence is controversial. It is true that in different parts of East Asia we find actors embracing quite distinct definitions and priority concerns of security, which depending on each country/community’s own perceptions and each sub-region’s specific conditions: the sense of security/insecurity and security concerns are different, for example, in Taiwan (highly concerned with a potential military intervention and invasion by China), in Indonesia (where the key security threat is not invasion by a foreign power but the desintegration and collapse of Jakarta’s authority), in Timor-Leste (where to consolidate its recent sovereignty and leave the “fragile State” condition is the major concern) or in Tibet and Xinjiang (where both Tibetan and Uigur are trying to preserve their identities and resist to authoritarian China); in the same way, security in Northeast Asia differs in several aspects from that in Southeast Asia. But it is also true in the past years new security issues have gained much more relevance in the regional and national security agendas, and it is due to three fundamental reasons:

- o Firstly, there is greater receptiveness towards a comprehensive view of security which can be traced to a number of *developments at the global level*, including the complexity of post-Cold War international politics and the attempt to control it; globalization and its perceived negative effects in some countries on state autonomy and national values; the fact that today the borders between “internal” and “external” levels of security are increasingly blurred; growing international awareness of the link between security and economic development, as well as of the risks associated to environmental and demographic imbalances; the acceptance of wider concepts of security, such as “human security” (see Anwar, 2003; see also Diana Magalhães’ essay in this book), which privileges individual, ethnic/religious groups or Humankind security rather than that of States, as well as the international recognition of the principle of *Responsability to Protect*; September 11 and the subsequent *Global War on Terror* by the US; a greater international emphasis on crisis and conflict management and country reconstruction; the more relevant role given to other non-state actors in terms of security (International Organizations, NonGovernmental Organizations, transnational terrorist networks, “lords of war”, transnational mafias, humanitarian and “green” international groups/agencies, multinational corporations, including armament industries and private security companies, etc.). Besides all this, the “new” security concerns go beyond local, regional and national borders, which means that the countries of East Asia and the region itself participates and is involved in the world efforts to ease or resolve these problems.
- o Secondly, certain developments and events in East Asia have considerably impacted on the regional security agenda, examples being the 1997-97 financial crisis; the attacks of the “new type of terrorism”⁴, in particular, the attacks of groups such as Jemaah Islamiyah or Abu Sayyaf, which are Al Qaeda supporters in Southeast Asia⁵; the

4 For an extensive explanation of my concept of “New Type of Terrorism” and its differences with the “traditional terrorism”, as well its international security and geopolitical implications see Luis Tomé (2004), *The New World Geopolitical Outline*: 155-224.

5 Southeast Asia governments have for long been faced with several types of terrorism, including rebellion, separatist and pro-independence movements, namely, in the Philippines, Thailand, Malaysia, Burma/Myanmar or Indonesia. However, the need to fight terrorism has gained prominence in the past few years due to two reasons: on the one hand, the American-led “war on terror” that began since the 9/11 attacks and the US pressure on Southeast Asian countries, where a vast number of the Muslim population lives, as well as terrorists groups associated to Al Qaeda; on the other hand, the assumption that the region is

December 2004 tsunami in the Indic Ocean, resulting in 280,000 deaths, mostly in Indonesia (Sumatra Island); the spreading of pandemics such as HIV/AIDS, SARS or the “bird flu”; the re-emergence of ethnic and religious conflicts in Indonesia and the Philippines in the 1990s and early 21st century; the increased demand and dependency of East Asian countries in terms of foreign markets and energy resources, which is associated to the increase in the price of oil; the pre-collapse of North Korea and the use of nuclear blackmailing tactics; Timor-Leste’s difficult independency process (1999-2002) (see Pureza, 2003) as well as the subsequent stability of this weakened state. Due to mutual interdependency, it is today much more obvious that internal conflicts or socio-economic crisis may very easily affect the stability of neighboring countries and regions. Obvious as well is the fact that the region’s relentless population expansion and urbanization, the associated population movements and social tensions, the inter-connected environmental problems (pollution, soil erosion, deforestation, declining air quality and increasing water scarcity) or the increasing dependency on energy resources may derail the entire development-oriented East Asian project and affect regional stability. Alan Dupont (2001) has provided one of the most extensive surveys of the new security challenges and their possible impact on East Asia, but there are many others who consider that *«the most likely long-term threats to East Asian Security come not from the threat of traditional inter-state conflict, but from a new array of transnational issues»* (Beeson, 2007: 92).

- o The third reason for the expansion of the regional security agenda is simultaneously one of its consequences: these “new” *problems and threats are more easily seen as “common” issues and more easily dealt with in terms of regional cooperation*. As these new concerns transcend national borders and may be beyond the control of individual states, the countries of East Asia and their external partners such as the US, India, Australia or the EU not only need to work together to try to solve these “common problems” but they are also more available to do so because of mutual interests and gains. Therefore, and though it is

not only headquarters but a target for Islamic transnational jihad terrorism, which is trying to establish Muslim Caliphate across Southeast Asia and destabilize the region. The news is that in the past few years there has been more cooperation among the ASEAN countries and between foreign partners and the ASEAN countries in the fight against terrorism, as well as the inclusion of regional anti-terrorist effort in the global counter-terrorism efforts.

not possible to completely solve territorial and border issues or resolve differences and conflicting national interests, the regional actors do cooperate in other areas of an enlarged security agenda.

The broadening concept of regional security permits to accommodate many different security concerns, from regime survival (the cases of Chinese, North-Korean or Burmese political regimes) to WMD proliferation, creating a very complex regional security network linking a wide variety of security problems. Consequently, Asian countries, the US, and regional institutions now have a more multidimensional and cooperative approach to security.

At the same time, however, the expanded security agenda demonstrates how varied is security in East Asia, which may make it more difficult to solve so many and different national and regional problems: «*The growing interconnections between domestic and inter-national factors and interconnected traditional and non-traditional factors have made maintaining national security a more challenging task*» (*China's National Defense 2006*, Chap. 1). On the other hand, associated to the expansion of the regional security agenda is the *potential problem of militarize non-conventional security dimensions*, which does not improve the situation but may worsen and/or increase regional insecurity (Wirtz, 2007: 340-341). In fact, “securitizing” certain issues and social, economic, and environmental problems (see Danreuther, 2007; and Baylis et al., 2007), i.e., to assume that certain problems put “national security” and/or regional/international security at risk may motivate some States to use military means to face them, which could poison regional environment.

The broadening concept of regional security also means security boundaries of the region have expanded and become less precise as developments in neighboring regions, such as Central and South Asia, have increasingly begun to impact Southeast and Northeast Asia, and vice-versa. So, traditional geographic subcomponents of Asia are more interconnected and interdependent; other regions’ developments and occurrences must be more taken into account in terms of East Asia international politics; and the regional security is itself more connected with the world as a whole (Yahuda, 2004: 338-341).

II. Economic Growth and Interdependence and Security in East Asia

It is unquestionable that East Asia economic interdependency is larger and deeper than in the past and the countries in the region have high economic growth rates (see next essay in this book, by Henrique Morais).

From a liberal point of view, economic growth and interdependence mitigate rivalries and security competition, reduce the probability of states seeking to resolve conflicts using force, and provide incentives for cooperation, as Kent E. Calder (2004) described as «*Securing Security through Prosperity*». Examples of the benefits of economic interdependence over regional security may include the unprecedented East Asian stability and the development of regional cooperation; the general improvement of bilateral relationships between regional rivals (US-China, Japan-China, Russia-Japan, China-Mongolia, China-India, China-ASEAN, Russia-China, ASEAN-India, China-Indonesia, South Korea-Russia, US-Mongolia, China-South Korea, US-India, China-Vietnam, North-South Korea, Japan-India, Taiwan-China), including new “strategic” partnerships and cooperation agreements; the policies carried out by East Asian countries towards dialogue and interaction at all levels; or the growing regional support to multilateral institutions and processes.

It could be argued that the priorities of most East Asian countries are stability and economic development which, of course, depend on a secure environment. Similarly, economic growth has become the legitimizing basis for many regional governments and regimes, including authoritarian, democratic or undergoing democratization process. On the other hand, globalisation and economic interdependence imply that domestic evolutions are more and more important for regional security and stability - consequently, maintaining domestic stability and avoiding economic crisis are becoming important vectors of regional security, and not only in the case of China or Indonesia but also, for example, the isolated North Korea.

If all that is true, there are further reasons for moderation, cooperation and organization among East Asian countries. However, if the realistic tradition is correct, «*since economic interdependence also brings strategic vulnerability – in that states become dependent on others for vital goods or markets for their survival or prosperity – states become compelled “to control what they depend on or to lessen the extent of their dependency”, thereby creating a situation where interdependence leads “probably... to greater security competition”*» (Tellis, 2006: 5).

Yet, regardless of its bigger or smaller impact on regional security and geopolitics, we must acknowledge that regional growing economic interdependence raises a new set of problems. Firstly, the potential conflict between State and market, since most countries in East Asia adopted a developmental model in which State stands between the population and international economy - the so called “*developmental states*” (Beeson, 2007: 141-183). Therefore, contemporary market forces threaten the autonomy of these States/political regimes,

expose their frailties and inequalities and force these governments to implement reforms which subvert their ability to control or go against their population's expectations. As such, countries/regimes may feel tempted to reinforce their control mechanisms by adopting protectionist policies or by promoting "wild" competition models in international politics, thus increasing the competition with other states.

Secondly, as the neoliberal Joseph S. Nye, Jr. (2007: 212) states «*Even if interdependent countries enjoy a joint gain, there may be conflict over who gets more or less of the joint gain (...) economic interdependence can also be used as a weapon – witness the use of trade sanctions ... economic interdependence can be more usable than force in some cases because it may have more subtle gradations. And in some circumstances, states are less interested in their absolute gain from interdependence than in how the relatively greater gains of their rivals might be used to hurt them.*

Thirdly, some experts argue that monetary and commercial policies will be an increasing source of competition, especially among China, Japan, the ASEAN group, and the US, either because those policies are decisive for what a country may earn within a globalized economy, becoming tools in economic competition with the other countries (Kirshner, 2003), or because there is a structural incompatibility of the "national capitalism styles" (Gilpin, 2003).

Fourthly, the demands of modernization and economic development are leading the countries in the region to depend more and more on energy resources, which are in turn becoming rarer and more expensive. This not only has consequences in terms of maintaining economic growth in the long run, but it is becoming a potential source of conflict for countries which are competing to obtain access and control to those resources. The immediate consequences are, on the one hand, the increase in the price of oil and natural gas due to the increased demand by developing Asian countries (especially, China⁶ and India) and, on the other hand, the new interconnections between East Asia and other areas of the world such as Central Asia, Middle East, Latin America, and Africa. Some argue, though, that this competition may lead to future wars (Klare, 2001).

At another level, East Asia's economic growth generates an "*economic security dilemma*" because it allows its actors to allocate more resources to develop military capacities: no doubt, military capabilities in the region are changing as a result of increased economic growth. Economic strength has always been considered an important component of national power and security:

6 On China's dilemmas on energy, see Félix Ribeiro, Fatima Azevedo and Rui Trindade's essay in this book.

the development and maintenance of military power and the relative positions of States in the international system have depended on their economic health and ranking; and economic power has also been deployed in the form of inducements or sanctions – access to or denial of aid, arms, resources, or markets – in the service of foreign and security policy (Alagappa, 1998: 45). As such, the economic growth of East Asian countries is changing regional and global power balances – and, with it, the dynamics of East Asia as well.

China's growing economic strength and its generated military power and political influence is clearly the principal cause of this kind of concerns, both in Asia and the US. Chinese leaders are well aware of it and have tried to internationally spread the idea of "peaceful rise", though not hiding the fact that China's economic growth is leverage in terms of the country's strategic potential and political influence: «*To build a powerful and fortified national defense is a strategic task of China's modernization drive... China pursues a policy of coordinated development of national defense and economy*» (China's National Defense 2006, Chap. 1).

The truth is that many analysts suspect the motives behind some Asian countries' views on interdependency and economic growth. Ashley J. Tellis (2006: 9-10), for example, considers that «*most of the key Asian nations seem to focus on trade principally as a device for maximizing "power and plenty", that is, as an instrumental mechanism for assuring the fastest increases in GDP, which can then be used by the governing regime to secure whatever goals – domestic or external – that may be of interest to the state... Even in those cases where trade is specifically directed toward mitigating conflicts – as for example in Chinese efforts at attracting Taiwanese and Japanese business investments to the mainland, Southeast Asian efforts at developing tight economic relations with China or Sino-Indian efforts at deepening bilateral trade relations – the calculus in each instance appears to center on how trade and interdependence might be used "strategically" to advance certain geopolitical and geo-economic goals, either domestic or external*».

III. Multilateralism and regional security

On the impact of multilateralism in East Asia, Ikenberry e Mastanduno (2003: 13) provocatively state that «*It is not that regional institutions don't promote stability, but that the region doesn't seem to promote international institutions*». The truth, though, is that multilateralism, regionalism and institutionalized cooperation are, indeed, improving in the region. Comparatively to other regions, like

Europe, multilateralism in East Asia is relatively incipient. Yet, when compared to other times in East Asia's history, it is obvious that multilateral diplomacy and cooperation was never so important in the region as today, by both governmental (or "Track 1") and nongovernmental (or "Track 2") institutions and processes.

The most notorious example is the *Association of Southeast Asian Nations* or *ASEAN*. Established in 1967 by five countries (Indonesia, the Philippines, Malaysia, Singapore and Thailand) ASEAN presently includes ten member nations, i. e. almost all countries of Southeast Asia (the original 5 plus Brunei, Vietnam, Laos, Myanmar and Cambodia) – the only exception being the new state of Timor-Leste, now seeking ASEAN membership (within five years from 2006) as well. Alongside with its enlargement, ASEAN has been going through a development process, institutionalizing new mechanisms and measures to strengthen regional integration and community building, including the ASEAN Free Trade Area (AFTA) and the "ASEAN Community" established in 2003 and comprising three basic pillars: Security, Economics and Socio-Cultural development. At the same time, the ASEAN group continues to develop cooperative relations with its "Dialogue Partners" - Australia, Canada, China, the EU, India, Japan, South Korea, New Zealand, Russia, the US, and the United Nations -, and also promotes a specific cooperation with Pakistan. In addition, ASEAN is at the core of the ASEAN Regional Forum (ARF), the ASEAN + 3 (China, Japan, and ROK), and the East Asia Summit (EAS) processes; and all or most of its members actively participate in other multilateral pan-regional and inter-regional mechanisms.

Another noteworthy example is the *Asia-Pacific Economic Cooperation* (APEC). Since its formation in 1989 APEC is, according to the organization, «*the premier forum for facilitating economic growth, cooperation, trade and investment in the Asia-Pacific region*» established to «*further enhance economic growth and prosperity for the region and to strengthen the Asia-Pacific community*». APEC began as an informal dialogue group with 12 members, but has become a formal institution since 1993 when the first APEC Economic Leaders' Meeting occurred and an APEC Secretariat was established, having currently 21 *Member Economies* representing about 70 percent of global economy: Australia, Brunei, Canada, Chile, PRChina, Hong Kong, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, South Korea, Thailand, United States, Vietnam, and Taiwan - in fact, APEC is one of the few international level organizations that Taiwan is allowed to join, as Chinese Taipei, since 1991 together with PRChina and Hong Kong. And

there are a dozen more countries seeking membership in APEC, including India, Mongolia, Pakistan, Laos, Colombia, Ecuador or even Guam (citing the example of Hong Kong). Key to achieving APEC's vision are what are referred to as the "Bogor Goals" of free and open trade and investment in the Asia-Pacific by 2010 for developed economies and 2020 for developing economies, agreed by APEC Leaders in 1994. To achieve these goals APEC Member Economies created a framework in 1995 which set out three key areas of cooperation, sometimes known as the "Three Pillars" of APEC, of Trade and Investment Liberalisation, Business Facilitation, and Economic and Technical Cooperation. During a September 7, 2007, speech at an APEC conference in Sydney, President Bush called for the creation of a new "Asia Pacific Democracy Partnership" in order to build a stronger network of alliances and partnerships for spreading democratic values, prosperity, freedom and conducting the war on terrorism.

Meanwhile, *cooperation between the Southeast and Northeast Asian countries* has also increased with the institutionalization of the *ASEAN Plus Three* (China, Japan, and the South Korea) process in 1999, when the Leaders issued a Joint Statement on East Asia Cooperation at their 3rd ASEAN + 3 Summit in Manila. Since then, a number of key documents have been adopted to set the guidelines for ASEAN + 3 cooperation, while their relations continue to expand and deepen: there are now 13 meetings at ministerial-level and 48 mechanisms under the ASEAN + 3 process, coordinating 16 areas of cooperation such as security dialogue and cooperation, trade and investment, energy, environment, disaster management, finance and currency, rural development and poverty eradication, culture and education, and social welfare and development. Simultaneously, bilateral and multilateral trading arrangements have been or are being forged between ASEAN + 3 participants, which will become the foundations of an East Asian Free Trade Area (EAFTA), a long term goal.

Another recent multilateral cooperative mechanism is the *East Asia Summit (EAS)*, a pan-regional forum held annually since the end of 2005⁷ by the leaders of sixteen countries of East Asia and neighboring regions: the thirteen ASEAN+3 plus India, Australia and New Zealand (Russia has applied for membership, but was only an observer in the first EAS in 2005). These Summits and the political statements resulting from them on a variety of subjects, from

7 The first EAS was held in Kuala Lumpur, Malaysia on December 14, 2005; the 2nd EAS was held in Metro Cebu, Philippines on January 15, 2007, approximately a month after the original scheduled date, postponed because of the Tropical Typhoon Utor; and the 3rd EAS was held in Singapore in November 2007; the 4th EAS is agreed to convene in Thailand, during 2008.

economy to regional conflicts and poverty decrease, are of the highest importance. Moreover, the EAS participants already agreed to improve cooperation on energy security and environment protection. They also agreed to support the EAS Energy Cooperation Task Force, to launch the Comprehensive Economic Partnership in East Asia (CEPEA), and to establish the Economic Research Institute of ASEAN and East Asia (ERIA).

The *idea of an East Asia Community* has a long history, beginning with the 1930s Japanese imperialist construction of the “*Great East Asia Co-prosperity Sphere*” and up to the 1990 Malaysian proposal of an “*East Asia Economic Caucus*” to create a trade union in the region. Presently, with such recent dramatic regional multilateral cooperation developments, the prospects for establishing an East Asia Community have apparently better chances, maybe as the result of the ASEAN + 3, APEC or EAS processes, but always with ASEAN in its center and as its driving force.

Other forms of multilateral inter-governmental cooperation have emerged in recent years, such as the *Asian-Pacific Partnership on Clean Development (APP)*, an innovative new effort to accelerate the development and deployment of clean energy technologies. Launched in January 2006, APP joins currently seven partners - Australia, Canada, China, India, Japan, Republic of Korea, and the United States - representing about half of the world’s economy, population and energy use, and they produce about 65 percent of the world’s coal, 48 percent of the world’s steel, 37 percent of world’s aluminium, and 61 percent of the world’s cement.

Also at *inter-regional and pan-regional level, multilateral cooperation is, in fact, a reality*, noteworthy with institutions such as the UN Economic and Social Commission for Asia and the Pacific (ESCAP), APEC, the Asian Development Bank (ADB), the ASEAN Regional Forum (ARF), the Conference on Interaction and Confidence Building Measures in Asia (CICA), the Asia Cooperation Dialogue (ACD), the Asia-Europe Meeting (ASEM), the Forum for East Asia-Latin America Cooperation (FEALAC), the Asian-African Sub-Regional Organisations Conference (AASROC) and the New Asian-African Strategic Partnership (NAASP). Similarly, the East Asian countries are also expanding cooperation with other inter-governmental organisations, such as the EU, NATO, the Shanghai Cooperation Organization (SCO), the Economic Cooperation Organisation (EEC), the Gulf Cooperation Council (GCC), the Rio Group, the Mercosur, the South Asian Association for Regional Cooperation (SAARC) and the newly South Asian Economic Union (SAEU), the South

Pacific Forum (SPF), and the EurAsian Economic Community (EurAsEC), among others.

A different approach to multilateralism in East Asia is *the so-called "second track"* or the non-governmental process, such as the Northeast Asia Security Cooperation Dialogue (NEACD), the Shangri-la Dialogue, the Boao Forum for Asia (BFA), the Pacific Economic Cooperation Council (PECC), the Trilateral Coordination and Oversight Group (TCOG) - designed to strengthen the U.S.-Japan-South Korea relationships -, the Pacific Basin Economic Council (PBEC), the Council for Asia-Europe Cooperation (CAEC), or the Committee on Security Cooperation in the Asia-Pacific (CSCAP), which joins committees from many different countries across the region. The aim of this "track 2" is to provide a more structural regional process of a non-governmental nature to contribute to the efforts towards regional confidence building and enhancing regional security and prosperity through dialogues, consultation and cooperation (see Job, 2003).

On the other hand, *regional multilateralism is growing also in the specific field of security*. Once again, ASEAN takes the lead, for example, with the *ASEAN Security Community (ASC)*, the *Concord Declarations*, the *Treaty of Amity and Cooperation (TAC) in Southeast Asia*, the *ASEAN Declaration on the South China Sea*, the *Zone of Peace, Freedom and Neutrality (ZOPFAN)* or the *SouthEast Asian Nuclear-Weapon-Free Zone Treaty (SEANWFZ)*. ASEAN is also proud of its role with the political settlement of the Cambodian conflict, of its support on the independence process of Timor-Leste and its support in the peace process in Aceh (Indonesia). Besides, as ASEAN, like Japan, is one of the regional actors giving more importance to the economic, environmental, social and human dimensions of security, the organization has developed a series of intra-ASEAN activities, as well as others with its partners, to promote regional cooperation in dealing with new transnational security issues.

The *ASEAN Regional Forum (ARF)* is a specific pan-regional security dialogue and multilateral cooperation mechanism. Created in 1994 by ASEAN and its dialogue partners to ease the tensions in the region through multilateral consultations, confidence building, and eventually the prevention of conflict, the ARF has expanded and now includes the following 26 participants: Australia, Bangladesh, Brunei, Cambodia, Canada, China, the European Union, India, Indonesia, Japan, North Korea, South Korea, Laos, Malaysia, Myanmar, Mongolia, New Zealand, Pakistan, Papua New Guinea, Philippines, Russia, Singapore, Thailand, Timor-Leste, the United States, and Vietnam. «*Despite the great diversity of its membership*», the ARF Ministers declared on the tenth year of

ARF, «*the forum had attained a record of achievements that have contributed to the maintenance of peace, security and cooperation in the region*», offering as examples: the usefulness of the ARF as a venue for multilateral and bilateral dialogue and consultations, and the establishment of effective principles for dialogue and cooperation, featuring decision-making by consensus, non-interference, incremental progress and moving at a pace which is comfortable to all; the willingness among ARF participants to discuss a wide range of security issues in a multilateral setting; the mutual confidence gradually built by cooperative activities; the promotion of dialogue and consultation on political and security issues; the transparency promoted by such ARF measures as the exchange of information relating to defense policy and the publication of defense white papers; and the networking developed among national security, defense and military officials of ARF participants (see ARF webpage). In June 2004 the ARF Unit was established to support the enhanced role of the ARF Chair, including interaction with other regional and international organizations, official defense dialogue and “Track 2” organizations; to function as depository of ARF documents/papers; to manage database/registry; and to provide secretarial work and administrative support, including serving as the ARF’s institutional memory (ibid.).

Security dialogue and cooperation is also important under the *ASEAN+3 and East Asia Summit* processes. The ASEAN+3 countries have shown progress, particularly in the field of non-traditional security issues, specially in the threat posed by terrorism and other transnational crimes, having adopted, in 2004, a *Concept Plan* and an *Action Plan* to address transnational crimes in eight areas, namely, terrorism, illicit drug trafficking, human trafficking, sea piracy, arms smuggling, money laundering, international economic crime, and cyber crime. On the other hand, the main issues in terms of security dialogue and cooperation of the East Asia Summit have been that of energy security and environment, as evidenced by the *Cebu Declaration on East Asian Energy Security* (January 2007) and the *Singapore Declaration on Climate Change, Energy and the Environment* (November 2007).

Another example of multilateralism in the field of security is the *Six-Party Talks*, since 2003, which include the PRChina, South Korea, North Korea, the US, Russia and Japan, and whose objective is to find a diplomatic and peaceful resolution to the issue of the DPRK nuclear program. The 6-Party talks were preceded by the Four-Party Talks (involving only the DPRK, the ROK, the PRChina and the US) in 1997-1999 with the purpose to reduce tensions and build confidence on the Korean Peninsula with the aim of putting

a formal end to the hostilities of the Korean War. Currently, the situation in Korea seems to be developing positively: after years of tension, and after North Korea's atomic experiment in October 2006, a DPRK's denuclearization road map is being implemented, under the agreements reached in the Six-party Talks (September 2005 joint statement and the February 2007 implementation agreement). In July 2007, North Korea closed the Yongbyon nuclear facility and, in addition, for the first time in five years, accepted the visits of inspectors from the International Atomic Energy Agency (IAEA) to the facility. DPRK workers began to disable the plant under international technical supervision a few months later, and in June 2008 North Korea demolished a water cooling tower at a Yongbyon facility where officials acknowledge they extracted plutonium to build nuclear weapons. Pyongyang, on the other hand, started receiving energy assistance and part of the economic and commercial sanctions imposed earlier were lifted, and President Bush said he would lift some U.S. sanctions against North Korea and remove the country from the State Department's list of state sponsors of terrorism.

The main objective of the Six-party Talks is still that of completely dismantling all nuclear activities in North Korea by the end of 2008 and obtaining truthful and thorough statements from Pyongyang, in terms of nuclear materials, including highly enriched uranium, plutonium, and nuclear devices. However, and besides this, the Six-party talks have also been crucial for inter-Korean understanding, the establishment of a peaceful relationship between Tokyo, Washington and Pyongyang and a possible Peace Treaty in the Korean Peninsula, one which will finally substitute the 1953 Armistice. The 6-Party talks can therefore become the beginning of a wider multilateral security framework in Northeast Asia.

Meanwhile, other initiatives of multilateral security cooperation have emerged. A noteworthy aspect is the participation of Asia-Pacific countries in the so called US "coalitions of the will", for example:

- in the *stabilization of Afghanistan*, within the US-led international coalition and within the *International Security Assistance Force (ISAF)* led by NATO since 2003, there are more than 40 countries which have or had troops in or supported operations there, including Australia, South Korea and Singapore. In March 2007, Japan and NATO finalized a framework for cooperation in Afghanistan, within which Japan provides up to USD 20 million of financial support for humani-

- tarian projects in support of NATO-led Provincial Reconstruction Teams (PRT's) in this country;
- in the *stabilization of Iraq*, within the US-led coalition or the United Nations Mission (UNAMI) there are also about 40 countries which have or had been participating with troops, including Australia, Mongolia, Japan, South Korea, Philippines, Thailand, and Singapore;
 - in the *Proliferation Security Initiative* (PSI) - a global initiative aimed at stopping shipments of weapons of mass destruction (WMD), their delivery systems, and related materials worldwide, announced by President Bush in May 2003 - there are currently nearly 100 participant nations, including Australia, Brunei, Singapore, Cambodia, Japan, Mongolia, Philippines, and Russia;
 - in the *Container Security Initiative* (CSI) - launched in 2002 by the US Bureau of Customs and Border Protection, an agency of the Department of Homeland Security, with the purpose to increase security for container cargo shipped to the US - there are currently 58 non-US ports from 35 different countries participating (accounting for 85 percent of container traffic bound for the US), including Singapore, Japan, South Korea, Malaysia, Thailand, Hong Kong, Taiwan, and China;
 - or in the *Global Initiative To Combat Nuclear Terrorism* (GI) - launched by President Bush and President Putin in July 2006 - within are currently participating about 75 countries including, besides the US and Russia, also Australia, PRChina, Cambodia, India, Japan, and South Korea.

One of the more salient processes about regional security cooperation in Asia-Pacific is the emergence of trilateralism in recent years. For example, in 1999 the *China-Japan-ROK Leaders' Meeting* was launched to address a wide variety of issues, from trade cooperation to security concerns. This same year the *Trilateral Coordination and Oversight Group (TCOG)* was established among the US, Japan and South Korea. In 2002, the US, Japan and Australia launched the "*Trilateral Strategic Dialogue*" - in May 2005, US Secretary of State Condoleezza Rice suggested that this process be elevated to the ministerial level, and a first ministerial meeting of the Trilateral Strategic Dialogue was held in March 2006 in Sydney between Rice, Australian Foreign Minister Alexander Downer, and Japanese Foreign Minister Taro Aso; on October 17, 2007 the three nations engaged in their first-ever trilateral military exercises. In 2005, the «*strategic triangle Russia-China-India*» began its yearly summits

joining ministers from the three Asian powers in order to develop mutual relations and make “21st Century the Century of Asia” while simultaneously claiming “global multipolarity”. In 2006, Japan proposed a new pan-regional cooperation channel, “*The Arc of Freedom and Prosperity*” open to all countries around Eurasia. In May 2007, the “*Quadrilateral Initiative*” (QI) appeared, which included the US, Japan, Australia and India in an attempt to reinforce practical cooperation and efficiency in terms of response to catastrophe, security in straits in the Indic Ocean and Southeast Asia, energy security and the fight against terrorism, piracy, illegal immigration, WMD proliferation and organized crime – however, the QI must also be viewed as an organization among the four above mentioned powers to control the emergence of China.

According to liberal and constructivist perspectives, institutionalized cooperation and international regimes diminish rivalry, maximize the benefits of cooperation, open opportunities to preventive diplomacy and constructive dialogue, foster shared decision processes and create mechanisms, rules and regulations which define and influence the interaction of actors. The ASEAN experience seems to prove them right: a few decades ago, the Southeast Asian security situation was compared to that in European Balkans; meanwhile, throughout its four decades of existence, ASEAN has significantly contributed to peace and stability among its member countries despite territorial disputes, ethnic, cultural and religious diversity and economic, political and social differences which continue to exist among them. As such, stability in East Asia reflects the positive effects of multilateralism, a kind of snowball effect, in regional perceptions, in actors’ behavior and in the regional security system. We should also emphasize the impact of the so-called “*ASEAN way*” in regional relations or in the behavior of the great powers, such as China or the United States. Amitav Acharya (2003-04 and 2001), for example, suggests that the growing interest China demonstrates towards institutionalized cooperation in terms of security and the US acceptance of ASEAN and ARF cooperative security patterns show how regional multilateral mechanisms allow for initiatives by much less powerful countries, such as those in Southeast Asia, initiatives which may affect the position of great regional powers. Noel M. Morada (2004) considers that the ASEAN approach in terms of relations with China, including ASEAN + 1, ASEAN + 3 and ARF processes, has been crucial for China to proceed with its “*peaceful rise*” policy and for Southeast Asian countries to lose insecurities in their relations with China, a neighbour power they traditionally fear. In fact, many believe in the “persuasion” effect caused by the socialization of regional multilateral boards, viewing processes like ARF as not only enabling China’s

involvement but also “socializing” its good behavior, as ASEAN countries and other countries wish: «*China’s involvement in the ARF and related processes seems to have led to the emergence of a small group of policy-makers with an emerging, if tension-ridden, normative commitment to multilateralism because it is “good” for Chinese and regional security (...) Even Chinese ARF specialists have noted that the institutional culture of the ARF requires them to adjust the tone and tenor of their discourse*» (Johnston, 2003a: 132). Therefore, ARF’s role is so important that Alastair Ian Johnston (ibid.: 123) considers it a «*counter-realpolitik institution*».

However, if the progress on multilateralism in East Asia is unquestionable – which is even more remarkable in such a diverse macro-region with no tradition of institutionalized multilateral cooperation, and where bilateralism has always prevailed – we must acknowledge that the majority of Asian countries still have traditional views on sovereignty, resist to assign responsibilities to supra-national levels, to establish a compromise or abide to foreign strict rules and regimes which reduce their leverage or to accept international institutions “intruding” on their “home affairs”. Asian nations are embracing multilateralism and institutionalized cooperation but they do so with an “open regional” spirit, particularly in terms of security, since their agreements are rather superficial and are not enforced.

For this reason, many analysts, specially IRrealist ones, emphasize the limits of the “*ASEAN way*” model, once that the typical decision by consensus standards, the absolute safeguarding of the non-interference principle, opting for informal and flexible approaches, the scope and superficiality of subjects, not dealing with more difficult issues, though is more “comfortable” for the regional countries, it makes multilateral institutions in East Asia have little effectiveness and little influence in State behavior or regional security. Therefore, ASEAN initiatives like ZOPFAN or SEANWFZ, for instance, are described by critics as contradictory and unrealistic, since they tend to limit extra-regional intervention while at the same time ASEAN encourages great powers to become involved in economic and security issues of Southeast Asia (Collins, 2003: 161). Similarly, the resolution of the Cambodian issue is mostly seen as a consequence of the end of China-URSS “cold war” and the fact that China and the US share interests which allowed for ASEAN to apparently have a prominent role (Smith e Jones, 1997).

The same reasoning and criticism exist in terms of ASEAN failures or “absences”, such as, for instance, during the 1997-98 financial crisis; the ethnic and religious conflicts and separatism in Indonesia; in Myanmar’s political

issues; its inability to solve the conflicts in the South China Sea; its inability to respond quickly and in an organized way to the tsunami in December 2004; its alienation in Timor-Leste's independence process (see Pureza, 2003) and in the 2006-2007 crisis in Timor-Leste; or its secondary role in the peace process in Aceh, Indonesia. These two last examples clearly demonstrate ASEAN limitations. Timor-Leste became independent (2002) after a long period of occupation by Indonesia (1975-1999) and is now trying to join ASEAN. ASEAN did not want or was not able to react to the social political crisis in 2006 in that small country, which led to "foreign" countries (namely Australia and Portugal) to ask UN and supply the means to stop disorder and imminent civil war. In the peace process between Indonesian Government and the Free Aceh Movement (GAM), it was the European Union which developed *Aceh Monitoring Mission* (AMM, from December 15, 2005 to December 15, 2006) - only five ASEAN countries (Thailand, Malaysia, Brunei, Philippines and Singapore) supplied monitors for EU's AMM. Therefore, there are those who claim that ASEAN is not solving conflicts; it's avoiding "subjects" (Smith e Jones, 1997: 147).

On the other hand, processes such as ARF, ASEAN+ 3 or the East Asia Summit include so many participants, with differences in terms of priorities and security concerns and opposing views on security issues, that their impact on real issue resolutions is very little. Often, the dialogue and cooperation mechanisms on East Asia security seem like *talking shops*, a place where Asian leaders greet and make speeches but where they avoid discussing problems they consider politically difficult or sensitive. This suggests that Asian countries and, in particular, some great powers are increasing their participation and involvement in multilateral processes mainly to prevent such mechanisms from taking decisions or evolving against their interests, to prevent them from being geopolitical tools in the hands of regional opponents and to promote their own interests and influence.

This has led us to think and draw the following conclusions as far as the relationship between multilateralism and regional security:

- o we have witnessed East Asia's speedy emergence in terms of a wide range of mechanisms and regional multilateral processes, both formal and informal, governmental and non-governmental;
- o multilateral cooperation is predominantly in the economic and commercial fields; however, it is increasing in terms of security and, in this field, it is becoming easier and it has been progressing more rapidly as far as non-conventional security issues;

- the impact of multilateralism is much more sensitive in Southeast Asia than in Northeast Asia, due to ASEAN and its initiatives;
- the impact of multilateralism is limited when it comes to solving some real “hard questions”. Yet, even so, it has contributed to: a) a growing collective approach to certain security issues, as a complementary channel to bilateralism; b) preventing some disputes from accumulating and breaking out; c) generating mutual trust and a clearer regional atmosphere; d) gradually increasing regional cooperation habits;
- the growing sense of “community” among ASEAN countries, the increased relations among ASEAN+3 participants, the success of the Six-party talks or the relative regional peace and stability illustrate the positive effects of multilateral cooperation in East Asia;
- “pragmatism” is a key-word in regional cooperation approaches, due to the many different security issues, the region’s historical and strategic circumstances and the suspicion of the real motivations behind certain East Asian actors and their positions in multilateral processes and mechanisms as being essentially linked to traditional power logic;
- multilateralism is improving but it does not substitute the weight and significance that some bilateral relations still have in regional order and security – the news is that conventional bilateralism is now being followed by multilateral arrangements;
- multilateral institutions and agreements are forms of cooperative security rather than of collective security. In the region, an order of cooperative security is emerging based on the closer net of bilateral and multilateral relations in a joint effort to support and/or promote regional security and stability. This has contributed to rapid and sustained regional economic growth and social progress.

IV. The Geopolitical Game: Uni-Multipolarity, “*Congagement*” and “*Hedging*”

In a context characterized both by the expansion of the concept of regional security, of security concerns and the increase of all types of interdependency linked to a growing multilateralism, the East Asian geopolitics can be defined through three inter-connected characteristics: i) a uni-multipolar structure of power; ii) simultaneous control, containment and engagement in the interactions among main actors; and iii) the use of a hedging strategy.

Uni-Multipolarity

The power structure in East Asia may be defined as uni-multipolar⁸, i.e., a hybrid system that includes the supremacy of a superpower, the United States, and other significantly powerful poles which are, however, very different among themselves in terms of their capabilities, nature, instruments and regional and global impact - such as, mainly, the great resurgent China and the newly strategically ambitious Japan, as well as resurgent Russia and India and the more confident ASEAN and South Korea. In fact, the geopolitical game involves all nations of the region as well some “non-resident” powers since that, even in a more peaceful environment than in previous eras, all regional actors in general are using and increasing their economic, military capabilities and political influence in defense or promotion of their own interests and values. However, as Avery Goldstein (2003: 171) alerts, understanding the significance of regional structure of power for East Asia’s security and stability requires more than a straightforward inventory and comparison of national capabilities.

Whether «*the United States is in relative decline*» in the region (Shaplen and Laney, 2007: 82) or «*Winning Asia*» (Cha, 2007), the truth is that the US is still alone in its position of world supremacy and the East Asian structure of power, grounded in its military superiority and vast strategic presence (from Guam to Afghanistan, including many thousand troops in Japanese and South Korean territories, as well in the Pacific and Indian Oceans), its old and renewed system of alliances (with Japan, South Korea, Thailand, Singapore, the Philippines, Taiwan, Pakistan, Australia and New Zeland, as well the Afghanistan post-taleban), its strategic cooperations and dialogues (with China, Mongolia, Indonesia, Russia and ASEAN group, as well with India), its huge political influence (both towards Asia-Pacific governments and regional and international institutions), its advanced science and technology (in all domains civilian, military and spacial), and its large economic and trade weight. Though the US have now an impressive foreign debt and huge trade deficits with most East Asian countries where China, Japan and Korea together represent almost half of USD 2.2 trillion total of US debt (which is a major concern in Washington), the American economy is still the biggest and most influential in the world and it represents more than 1/5 of the world GDP adjusted for purchasing-power parity (it increases up to 1/4 if measured by USD weight). The US is one of the

8 In my point of view, the uni-multipolar structure is the one that best characterizes the world order with, on the one hand, the *hyperpuissance* US and, on the other hand, some other regional great powers with international relevance such as the EU, China, Japan and India, plus many other regional powers (the UK, France, Germany, Brasil, Australia, Indonesia, Pakistan, South Africa, Israel, Iran, Saudi Arabia, Egipt, etc). See on this Tomé, 2004 (namely *Part I*), and 2003.

main foreign investors and trade partners of virtually all Asia-Pacific countries: as of 2006, the US was Japan and ASEAN's 1st trade partner (representing 18,7% e 12,5% of Japan and ASEAN's total external commerce, respectively), the 2nd of the PRC (15,9%) and India (10,4%), the 3rd of ROK (12,6%) and of Taiwan, the 4th of Australia (10,9%), the 5th of Russia (3,6%) and the 6th of Mongolia (4,6%) (European Commission – *Trade Statistics*). The US is, indeed, the only superpower, combining huge “hard power” with vast “soft power”. Moreover, it is more and more frequently using its hard power for soft-power purposes as it did, for example, in response to the December 2004 tsunami⁹: as Victor D. Cha (2007: 100) demonstrates «*no other nation, and no international organization, could have coordinated such a response*».

In East Asia (as in the World), the US is trying to maintain its supremacy and the “pax americana”, while simultaneously is safeguarding its interests related with security, prosperity, and democracy and human rights. The US is also interested in taking its due advantage from the economic development of East Asian countries; avoiding the creation of a competitive Asian strategic axis (joining, for instance, China, Russia, and India or even Iran); and controlling China's rising power and influence (see also Robert Sutter's Preface and Carlos Gaspar's essay in this book). Therefore, the US consider crucial the “global alliance” with Japan – America's most important ally in Asia-Pacific – and the strategic articulation with other allies and partners (such as South Korea, Australia, Mongolia, Taiwan, ASEAN, and India), while it is also embracing and cooperating with China and Russia. With its supremacy, its hub-and-spokes strategy and in its interests promoting process, the US is also contributing to regional security order.

East Asian countries continue to differ as far as the role and strategic weight of the US in the region. China and Russia, namely, but also North Korea and Myanmar, all encourage a gradual weakening of the US position while most other Asian countries continue to support a strong American presence in the region. The truth is that the US is still fundamental as a “regional balancer”

9 Within 48 hours of the disaster, the US had enlisted Australia, India, the EU, and Japan and organised the largest emergency relief mission in modern history, sending over 16,000 US military personnel, two dozen ships, and 100 aircraft as part of its immediate USD 346 million relief package, followed by an additional US commitment of USD 600 million (Cha, 2007: 99-100). Plus, it dispatched the USNS *Mercy* which, equipped with 12 operating rooms and 1,000 hospital beds, treated almost 10,000 patients and performed close to 20,000 medical procedures. Washington sent the *Mercy* again to give humanitarian aid in 2006 into South and Southeast Asia: in just five months, its crew treated almost 200,000 patients, performed more than 1,000 surgeries, and trained more than 6,000 local medical professionals, while small teams from the US Naval Construction Force also made repairs or improvements to medical centers, schools, and other infrastructure onshore (Shaplen and Laney, 2007: 95).

and “Asia’s security guarantor”, helping to ensure the stability and geopolitical equilibrium in East Asia. Despite significant progress in their mutual relations and the relative regional peace, Asian countries do not trust one another enough – as such, they feel much more comfortable and at ease in their relations, in accepting emerging powers, in accommodating each other or in the resolutions of their many different security issues, knowing that the US “is around”.

However, although all the US huge hard and soft power and supremacy, the regional structure of power is not really unipolar – there are limits of what the US can do, and it is far from being the only relevant actor or even the principal determinant of regional order. It is, indeed, a situation of «*incomplete hegemony*» as Michael Mastanduno (2003) put it.

With its high national potential¹⁰, «*China’s rapid rise over recent years as a regional political and economic power with growing global influence is an important element in today’s strategic landscape, one that has significant implications for the region and the world*» (US DoD, 2008: I). Though China’s growth undoubtedly includes huge internal and external dilemmas and constraints, China’s share of global GDP adjusted for purchasing-power parity has grown from around 2% in 1980 to 12% in 2008 (see IMF, 2008), which means that China ranks second just after the US - and is now Japan, South Korea and Mongolia’s number 1 commercial partner, the EU and Russia’s number 2, and the US, India and ASEAN’s number 3 (see more on this in Henrique Morais’ and Rui Paiva’s essays this book). Its defense budgets have increased annually in two digits in the last 20 years, and it’s probably the world’s 2nd ranking in military expenses. Its Popular Liberation Army (PLA) is the biggest army in the world with more than 2 million soldiers and it’s rapidly being modernized – namely in terms of “mechanization” and “informationalization”, air and naval power, force mobility and missile and satellite systems (see on this US DoD, *Military Power of the People’s Republic of China* 2008 and 2007; see also Alexandre Carriço’s essay in this book). China’s ability to project military power over vast distances remains limited but, as noted in the US 2006 Quadrennial Defense Review Report”, it «*has the greatest potential to compete militarily with the United States and field disruptive military technologies that could over time offset traditional U.S. military advantages*».

10 It is the world’s most populated country, with 1,330 million inhabitants, which corresponds to 4 times the population of the US and ten times that of Japan; its territory is 9.6 million square km large, it has a continental dimension, from Central Asia to the Pacific Ocean and includes a huge geographic and weather diversity, as well as many natural resources; its history and civilization dates back a 4500 years old; and it is the new star in Asian and world economy, whose growth rates have been close to 10% annually over the last 30 years.

Meanwhile, China began participating in joint military exercises (mainly with Russia and Central Asian countries bilaterally and within the SCO framework, but also with India, Pakistan, Southeast Asian countries, the UK, the US, and France), thus putting an end to decades of the ban on that type of cooperation and involving more and more of its troops in United Nations' peace operations: there were 1,955 Chinese UN peacekeepers as of May 2008, being that date the 13th in the ranking of troop contributors to UN operations, much higher than any other East Asian country - by December 2001, for comparison, there were only 129 Chinese UN peacekeepers, 44th in the rank (UNDPKO webpage). Its major political influence is now becoming visible not only in East Asia but beyond, in particular in Central and South Asia, and also in Africa, in the Middle East and in Latin America, as well as in all the forums and multilateral mechanisms it participates in.

Asia is obviously the priority in terms of China's international relations¹¹. Using its "good neighborhood" policy, Beijing has signed treaties on 20,222 km of its borders, specially with Russia and the former soviet republics of Central Asia and produced a vast number of declarations aiming at the peaceful resolution of present border disputes with India, Japan, Buthan, Vietnam and some other ASEAN countries. China has simultaneously intensified its involvement in regional multilateral institutions and dialogue, while fostering bilateral relations with its Asian neighbors and the US, skillfully making all of them its productive partners.

Beginning in 1997, Beijing articulated a «*New Security Concept*» for «*establishing a more just and equitable international order*», that was given formal standing in China's first Defense White Paper the next year. China has declared that its major strategic objective is «*to build a moderately prosperous society in an all-round way and a socialist harmonious society*» while is also «*moving toward multi-polarity*» (China's National Defense 2006: Chapter 1). Therefore, its foreign policy aims at developing relations that will allow the country to strengthen its military and economic power as well as its political influence, i.e., its «*comprehensive national power*». China continues its national long term «*great strategy*», in which the growth of its «*comprehensive national power*» will allow a more and more favourable «*strategic configuration of power*». This is then a pragmatic and patient «*wait and see*» strategy, based on the idea that its «*in an all-round way growth*», if wisely used, will maximize its power as well will lead

11 About the Chinese Foreign and Asian Policies see Carmen Amado Mendes' essay in this book. See also, for example, Sutter, 2008 and 2005; Gill, 2007; Kurlantzic, 2007; Tomé, 2006 e 2001; and Shambaugh, 2005.

China to a new position in the power ranking (Tomé, 2006). In this regard, «*China is less a “responsible” power – fully embracing international norms in security and political affairs – and more a “responsive” power, carefully maneuvering to preserve long-standing interests in changing circumstances*» (Sutter, 2005a: 16).

Japan is another fundamental player of East Asian geopolitics. Japanese domestic economic troubles in the 1990s, together with the continuous rapid economic growth of China, have reduced Japan's economic status compared to what the country enjoyed in the 1980s. Yet, its economy is still one of the most advanced, powerful and influential in the world, Japan is one of the major investors in foreign countries and a crucial economic and commercial partner of most East Asian countries, the US, Australia, India, the EU, as well of the most Middle Eastern, Latin American and African countries. Japan is also advanced in terms of science and technology, including in the military field - though relatively small with only 240,000 troops, Japanese Self-Defense Forces (SDF) are extraordinarily well-equipped in terms of technology. And even if its defense budget is not above 1% of its GDP, it is the 5th in the world.

Though Japan maintains its “comprehensive security” as well as economic and cooperative security approaches, the most relevant for East Asian security and geopolitics today is the change and expansion of its security profile (see, for example, Pyle, 2007; and Samuels, 2007; see also Miguel Neves' essay in this book). This is not entirely new as, specially since the end of the Cold War, Japan has gradually tried to become a “normal country”: it has applied for permanent membership in the UN Security Council since 1991 and it has reinterpreted its Constitution to enlarge the scope of action of its SDF and its participation in peace and security missions abroad. Yet, the Japanese predisposition towards strategic expansion and institutional reform has increased recently and the country has relinquished several self-imposed restraints which characterized its “institutionalized pacifism”. For example, in January 2007, it upgraded the Self-Defense Agency and once again Japan has a Ministry of Defense for the first time since the World War II. Meanwhile, the Japanese Constitution has been subject to revision, namely aiming at amending the famous Article 9, which states that «*the Japanese people forever renounce war as a sovereign right of the nation and the threat or use of force as means of settling international disputes. In order to accomplish the aim of the preceding paragraph, land, sea, and air forces, as well as other war potential, will never be maintained. The right of belligerency of the state will not be recognized*» - in May 2007, the Japanese Diet approved that a referendum will be held in 2010 on the Constitution. Besides, Tokyo has been

developing its capability to project power and, in the end of 2007 the Japanese Diet voted to allow Japan to use outer space for military purposes.

Simultaneously, the alliance with the US is reinforced and is moving towards a true collective self-defense, both parts declaring it a “global alliance”. Washington and Tokyo agreed to downsize the US force stationed in Japan (around 8,000 marines positioned at Okinawa are being relocated to Guam) and that the Japanese troops should have increased responsibility. Besides, joint military exercises between American and Japanese have multiplied and intensified, greatly improving the level of integration and inter-operationality between the two armies; Japan joined the US in developing a ballistic missile defense system for the region; and starting in 2008, the US is basing a nuclear-powered aircraft in Japan, for the first time. In Iraq, Japan has deployed its SDF for humanitarian operations, flown C-130 supply missions, and become the second-largest donor to Iraqi reconstruction¹². Within the “Contact Country” framework, Japan has improved its relationship with NATO, establishing dialogue and cooperation on a vast range of topics related to international security: for example, in Afghanistan, Japanese are providing financial, humanitarian, medical and logistical support for the NATO-led International Security Assistance Force (ISAF) there: in March 2007, Japan agreed to provide up to 2 billion yen (around USD 20 million) of financial support for humanitarian projects in Afghanistan, particularly in the areas of primary healthcare and education. Japanese SDF are also involved in anti-terrorist and counter-proliferation activities in the Indic as well Pacific Oceans, and is one of the most active participants in the American-led *Proliferation Security Initiative* and *Container Security Initiative*. Similarly, Japan, together with the US and Australia, participates in the “*Trilateral Strategic Dialogue*”, launched in 2002. And together with the US, Australia and India Japan is also participating in the “*Quadrilateral Initiative*” (QI) which was launched in May 2007 - it was within the scope of this initiative that the Japanese naval forces participated in the naval exercises in the Bengal Bay, the Indic Ocean, in October 2007.

Meanwhile, since 2006, Tokyo has proposed and attempted to promote, as a pillar of «*Japan's Expanding Diplomatic Horizons*», a new pan-regional cooperative channel called “The Arc of Freedom and Prosperity”, involving all Eurasia and «*the outer rim of the Eurasian continent*»¹³.

12 In July 2006, Japan has completed a full withdrawal of armed forces from Iraq.

13 «*The basis of Japan's foreign policy is to strengthen the Japan-US alliance, as well as a strengthening of our relationships with our neighboring countries, such as China, ROK, and Russia. (...) First of all there is “value oriented diplomacy,” which involves placing emphasis on the “universal values” such as democracy, freedom,*

Russia¹⁴ must also be taken into consideration as far as regional geopolitical strategy, since it is geographically in Northeast Asia¹⁵ and has all the features of a great power by its geographical dimension (it is, by far, the largest country in the world, about 1/8 of the planet's terrestrial surface, more than China and India together, and 75% of its territory is in Asia), its location (the "heartland" of Eurasia) and its military capacities – it has one of the biggest defense budgets and armies in the world and has the second most important nuclear arsenal (Russia was the only heir of the Soviet Union's powerful nuclear arsenal) after that of the US. Russia inherited the place the Soviet Union held in the UN Security Council (1991) and became a member of G8 (1997) and of APEC (1998), and should soon join the WTO. Above all, it is a great energy power: it is the second major oil producer (after Saudi Arabia) and the biggest outside OPEC, it is estimated to have about 7% to 10% of world oil reserves; it is the major natural gas producer and exporter, it is estimated to have about 1/3 of world gas reserves; it also has 20% of the world heavy coal reserves, besides great amounts of uranium, steel, iron, wood, water, etc. After a difficult post-soviet transition period, Russia is now re-emerging as a great world power, as a result of its internal stability and its taking advantage of the increase in demand and in the price of oil and natural gas to improve its economy¹⁶ (Russia's annual growth rates range between 6% and 7.5% since 2000) and promote its political influence.

Paradoxically, Russia's geopolitical importance goes beyond Northeast Asia but its weight is greater in world or Asian terms than in the East Asian region¹⁷. In fact, Russia's external priority is not East Asia as a whole or Northeast Asia, where she is physically resident, but Central Asia and Eurasia.

human rights, the rule of law, and the market economy as we advance our diplomatic endeavors. And second, there are the successfully budding democracies that line the outer rim of the Eurasian continent, forming an arc. Here Japan wants to design an "arc of freedom and prosperity". (...) take a look around the outer edge of Eurasia - just follow that line all the way around. This belt has seen great changes upon the end of the Cold War as the curtain was being drawn on the confrontation between East and West. It is these countries in which we hope to help build "the arc of freedom and prosperity"» (Aso, 2006).

14 About Russia as main actor in East Asia and its relations and policies in the region see Raquel Freire's essay in this book.

15 It is noteworthy that, unlike what happened in Europe, in Caucasus or in Central Asia, where newly independent post-Soviet States emerged, the Russian Far East é geographically identical to the old Soviet Far East, having borders with Mongolia, China, Korea and Japan.

16 Russia, for example, has already fully paid its external debt to the Paris Club, which was, in 1998, USD 158 billion, having today a so-called "Stability Fund" of about USD 100 billion.

17 In fact, Russia lost the control over Mongolia, which it had more than a century; it has a limited relation with Japan because of their differences about the South Kurilles/Northern Territories (Etorofu, Kunashiri, Shikotan e Habomai Islands) – although their relations are now closer, Moscow and Tokyo have not signed a Peace Treaty since WW II; its influence over Korea is rather limited, much more limited than that of the US, China or Japan; though it is one of the Dialogue Partners of ASEAN (since

Russia's Asian policy seems to be China-oriented: the two powers have a strategic partnership since 1996, confirmed by the 2001 Treaty of Good-Neighborliness and Friendly Cooperation; in 2005, they definitely solved border differences of part of the 4300 km of common border; since 2005, they have organized bilateral military exercises, as well as others within the scope of the Shanghai Cooperation Organization (SCO); they have both promoted and developed SCO, cooperating towards the stability of Central Asia; bilateral trade has increased about seven times since 2000, making China Russia's second biggest commercial partner, after the EU. Besides, China is by far the largest buyer of Russian armament and military equipment (since 1992, 85% of Chinese weapon imports are from Russia) and it is also one of the greatest markets for Russian energy: Russia is nowadays China's first supplier of natural gas and the third supplier of oil, after Saudi Arabia and Angola.

China is crucial for Moscow but Russia's Asian policy is more than China: besides the post-soviet states of Central Asia and of the Collective Security Treaty Organization (CSTO), the dialogue and strategic cooperation with Iran and India are also very important for Russian leadership in its Asian policy and particularly in its attempt to restrain the US prominence in Asia-Pacific and the world (Tomé, 2007a). For example, the old proposal by former Russian foreign minister Evgeny Primakov who, in 1998, envisioned the creation of a «*strategic triangle Moscow-Beijing-New Delhi*» has apparently now become a reality with the ministerial summits Russia-China-India since 2005, an annual routine whose aim is to promote trilateral cooperation but also "multipolarity".

Thus, Russia can be seen as a more important player than a few years ago in East Asia, namely in Northeast Asia, and especially if more weight is given to Central Asia, its energy resources and routes. As an example, in the 1990s Russia was marginalized from the 4-Party talks (US, China, South Korea and North Korea), whereas in this last crisis (2003-2007) it was immediately included in the 6-party talks.

Another actor of increasingly more importance in East Asian geopolitics is South Korea, presently much more confident due to several factors: its contin-

1996) and participating in ARF, its influence is very small in Southeast Asia. Russia's limitations in status and influence in East Asia are visible, for example, in its absence at the ASEAN+3 process (why not an ASEAN+4 with Russia?) or at the *East Asia Summit* – even though it geographically belongs to this region, Russia was only an observer in the first EAS (it was invited by the host country, Malaysia), while other "non-East Asian countries" such as India, Australia or New Zealand are active participants in the EAS. Russia's relations with the US and China and India are also much more due to its position and influence in Eurasia rather than in East Asia.

ued economic growth (it is now the 7th biggest economy in the world) and the country's progress and consolidation as a democracy; the fact that its relations with China have significantly improved; that it still has its alliance with the US and a good relation with Japan, now increasingly closer relations with Russia, as well as with ASEAN and India; the probable denuclearization of North Korea and growing peace in the Peninsula, and the increase in inter-Korean dialogue and reconciliation (see on this Nuno Magalhães' essay in this book). Moreover, South Korea is becoming more "autonomous" in its relation with the US, both in economic and commercial terms: in 1991, the US accounted 26% of South Korea's exports; by 2006, that share decreased by just 15%; at the same time, the commercial balance between the two countries is still increasing favorable to ROK. In military terms, American military presence has been reduced and the South Koreans have now increased capacities and responsibilities: it is estimated that, from 39,000 American stationed in 1990, these will be reduced to 25,000 by the end of 2008, and it has also been agreed that 59 US camps under the present *Status of Forces Agreement* should be returned to South Koreans and the current *Combined Forces Command* be dismantled by April 2012, which will result in the US' handing over wartime operational control of ROK troops on the Korean Peninsula to Seoul. Meanwhile, the South Korean Ministry of National Defense has demanded an increase in the defense budget by 11% until 2015 and by 9% between 2015 and 2020.

This is why South Korea is now much more at ease in its relations with North Korea, with its powerful neighbors China, Russia and Japan or with its American ally. For all of them, as well as for the ASEAN group, South Korea is nowadays an actor to take into consideration in terms of economy, politics and strategy.

The ASEAN group is also increasingly as an important actor in East Asia geopolitics (see also on this Nuno Canas Mendes' essay in this book). ASEAN is obviously a different kind of actor, since it is not a state but an inter-governmental organization which includes ten very different countries. Moreover, ASEAN countries still do not fully agree on how they face and relate to the great powers such as China or the US, which means that it is vulnerable to the great powers' strategic games and it is difficult for ASEAN to be seen as a regional united "actor". However, as a group, ASEAN is indispensable when it comes to regional geopolitics.

Firstly, in a definition of East Asia which embraces Northeast and Southeast Asia, an "ASEAN Community" which includes all Southeast Asian countries (except Timor-Leste, for now) has to be taken into consideration in

regional geopolitical strategy. Secondly, the ASEAN countries together account for a population of about 580 million, a total land area of 4.5 million square kilometers, a combined GDP of almost USD 1,300 billion estimated in 2008 (from about US\$ 645 billion in 2002), and a total trade of more than US\$ 1,500 billion in 2007. Thirdly, as other actors, ASEAN countries have taken advantage of their economic growth to improve their military capacities and increased their defense budgets: the 10 ASEAN countries combined account, in 2008, a total number of armed forces of almost 2 million and a defense expenditure around USD 34 billion. All these aspects make ASEAN group a significant actor in East Asia as well for its dialogue partners.

On the other hand, the capacity of ASEAN group is today more relevant in regional geopolitics due to its level of integration, which attempts to set the basis for a true “security community” in Southeast Asia while is using its “soft power” spreading that ideal of “community” to all East Asia. As a consequence, ASEAN has tried to increase its “weight”, its political influence and its international leverage both by increasing its bilateral relations with its “Dialogue Partners”, drawing them to the “ASEAN vision”, and by leading the efforts towards regional “accommodation” and cooperation, in particular through ARF, ASEAN+3 and EAS, establishing “minimum common denominators” in the mutual interests connected with peace and development. In the past, Southeast Asia was a focus of competition and conflict among regional and world great powers; nowadays, ASEAN has managed to establish a greater autonomy for Southeast Asia towards “foreign powers” and be considered an effective partner in regional geopolitics, an actor to take into account by major powers.

In the region’s geopolitics, other non-resident powers (besides the US) are also becoming more relevant, as is the case of Australia and India.

Australia is a US ally, a Strategic Partner of Japan and India, and a Dialogue Partner of ASEAN. It participates in ARF, APEC and in EAS, and it has become more influential in East Asia, namely in Southeast Asia: for example, it is the key contributor for the International Stabilization Force in Timor-Leste. Meanwhile, in May 2007 Australia joined the US, Japan and India in the so called “*Quadrilateral Initiative*”, while participates in the “*Trilateral Strategic Dialogue*” (*US-Japan-Australia*) launched in 2002.

India has re-emerged as an economic power (with an annual growth of about 8% in the last 20 years, an economy based on high technology, and representing 4.7% share in the world GDP based on ppp in 2008), as a strategic power (it has nuclear power since 1998 and a powerful army of more than 1.2 million troops) and it has promoted its political influence very much

beyond South Asia. Nowadays, it is a crucial strategic partner of the US and China, as well as of Russia, Japan, ASEAN, Australia and Iran. India is also a member of the WTO since its creation in 1995 and has applied for permanent membership of UN Security Council; it participates in the East Asia Summit and is a possible candidate for accession to SCO and APEC. India's major geopolitical importance is visible in the dispute of Russia-China and US-Japan axis to attract India's cooperation: thus, India has participated in the trilateral, Russia-China-India, ministerial summits since 2005, and, since May 2007, it has participated in the US-Japan-Australia-India «*Quadrilateral Initiative*». In face of all of this, geopolitical strategies on East Asia take emerging India more and more into consideration, while India views the "Look East Policy" as increasingly more important in its geopolitical perspectives (see also Rui Pereira's essay in this book).

Table 2. Defence Expenditure and Armed Forces in East Asia

	current USD m			Defence Expenditure			Number in Armed Forces (000) 2008
	2001	2004	2006	2001	2004	2006	
EAST ASIA COUNTRIES							
Russia	46,100	59,600	70,000	318	414	493	1,027
Mongolia	23	17	19	10	6	7	9
North Korea	4,500	n.a.	n.a.	201	n.a.	n.a.	1,106
South Korea	11,919	17,463	24,645	252	361	505	687
Japan	40,496	45,152	41,144	320	355	323	240
China	43,551	87,150	121,872	34	20	27	2,105
Taiwan	8,223	7,542	7,738	368	332	336	290
Timor Leste		n.a.	n.a.	n.a.	n.a.	n.a.	1
Myanmar/Burma	4,941	5,889	6,920	103	127	147	406
Brunei	277	298	328	826	815	864	7
Cambodia	83	105	123	6	8	9	124
Indonesia	4,360	2,568	3,645	21	11	16	302
Laos	12	11	13	2	2	2	29
Malaysia	1,921	2,742	3,206	81	117	131	109
Philippines	1,155	825	909	15	10	10	106
Singapore	4,369	5,102	6,321	1,061	1,172	1,407	73
Thailand	1,739	1,954	2,275	28	31	35	306
Vietnam	2,220	2,781	3,439	28	34	41	455
ASEAN GROUP 10	21,077	22,275	27,179	—	—	—	1,917
EXTRA-REGIONAL MAIN ACTORS							
United States	305,500	455,908	535,943	1,073	1,556	1,796	1,498
India	14,368	19,821	22,428	14	19	20	1,288
Australia	7,028	13,907	17,208	361	698	849	51

 Fonte: International Institute for Strategic Studies (IISS), *The Military Balance 2008 and 2004-2005*.

Congagement

In this uni-multipolar order, most actors compete with and hold each other in check, but they also maintain coordination and practical cooperation in their mutual relationships, in a regional pattern of mixed and mutual control, containment and engagement.

The prominent US and resurgent China are “natural” strategic rivals. For this reason, there have been many suggestions for an American containment policy against China¹⁸ and for a Chinese policy for containment of American hegemony or even a certain revisionist behaviour destined to enforce alterations that are favourable on the regional power scale¹⁹. This environment of mutual containment is sustained by strong oppositions on many issues ranging from the Taiwan question to the human rights situation in China or the huge American trade deficit and consecutive confrontation or mutual provocation episodes²⁰. At the same time, China and the US compete economically and commercially for markets and energy resources, for military capacity and not only power and influence on East Asia and other regions, but also regional and international institutions that both are part of.

However, US-China mutual containment and competition constitute only one part of the relationship. The other part refers to their increasing cooperation based on mutual interests related to economic development, stability and security. For example, even though the US trade deficit with China (averaged around 233 billion USD in 2006) is a source for concern in Washington, US-

18 For example, the adjustments of positions with Japan, South Korea, Taiwan, ASEAN, Russia as well as with India, Australia or the EU, have “surrounded” China; the protection of Taiwan and the fact that advanced weapons continue being delivered into Taipei (despite the US having repeated its “one China” policy many times); the aid and support of Chinese “dissidents” and human rights and pro-democracy organisations in China; the boycott on China of arms sales and hi-technology with a “two-fold function”; maintaining the old system of alliances and powerful military disposition in all of the Asia-Pacific region; the pressure for China to change its political system, to respect human rights and conform to International norms and regimes.

19 For example, by denouncing American hegemony and accusing the US of interfering in its “internal affairs”; its pressure aiming at multipolarity, including the strategic partnerships with Russia and India; constantly threatening to resort to force in relation to Taiwan; massively buying weapons from Russia and modernizing its PLA; maintaining good relations with North Korea, Myanmar, Sudan, Venezuela, Cuba or Iran, all pertaining to the US list of proscribed countries; by significantly increasing (although very transparently) its defense budget and military capacities; maintaining territorial and frontier reivindications with many of its neighbouring countries; increasing its bilateral relations and becoming more actively involved with multilateral mechanisms not only to defend its interests but also to promote its influence so as to prevent becoming geopolitical instruments of other powers, starting with the US and Japan.

20 As for instance, the Taiwan Strait’s crisis in 1995-96, the bombing of the Embassy of China in Serbia in 1999, the incident about the collision of a U.S. EP-3 surveillance plane and a Chinese fighter jet in 2001 or the rhetorical discourse and threats towards Taiwan, including some “legislation” and “war games” in the Strait.

China bilateral trade grew from USD 64 billion in 1996 to USD 343 billion USD in 2006, in which China represented the greatest source of American imports and the US was the major export partner of the Chinese. Another example: immediately responding to the earthquake in Sichuan Province, China on May 12, 2008 the U.S. Government (USAID plus DoD) provided humanitarian assistance rounding USD 4 million, as of June 2008, encouraged cash donations and other assistance to Chinese authorities and also shared satellite images to help rescue efforts and reconstruction.

Without always pursuing the same policies, the fact is the US and China cooperate and adjust their positions on the most varied issues: stabilizing Iraq and Afghanistan (through the UN); preventing the proliferation of WMD, not only concerning the desingularization of North Korea but also the solution to the nuclear program in Iran; reforming the United Nations; pacifying and stabilizing regions such as Korea, Central Asia and South Asia; fighting against terrorism and organized crime; building energy security; reducing the risks of pandemic disease and environmental degradation; supporting multilateralism, regional and pan-regional cooperation, etc. In the meantime, the US (and Japan) have helped China fulfil its desire of entering the WTO (2001) and even China itself has participated in one of the “coalitions of the will” devised by Bush’s administration, the *Container Security Initiative (CSI)*. Indeed, Beijing is making an effort to demonstrate its “peaceful rise” and that it is a stabilizing power, while Washington encourages China to become a “*responsible stakeholder*” as it in turn becomes a major global player.

Washington and Beijing have adjusted their positions as a way of avoiding disputes from accumulating or breaking out on escalation, particularly on such a delicate subject as that of Taiwan. For example, during the early months of his Administration in 2001, President Bush has declared that the US would «*do whatever it takes*» to protect Taiwan and he followed that assurance by approving the largest arms sales package to Taiwan in nearly a decade - going significantly further than his predecessors had, despite Beijing’s protests. However, that pro-Taiwan stance appeared to change dramatically in December 2003 during a visit by Chinese premier Wen Jiabao when President Bush publicly admonished Taiwanese President Chen Shui-bian for seeking to change the *status quo* unilaterally and emphasized Washington’s opposition to any unilateral actions, an attitude which pleased Beijing. In fact, so long as the Taiwan’s independence claim is not placed within a legal framework, the US and China have decided that, however galling, they can live with it.

China and Japan are historic rivals which have maintained mutual suspicion towards each other's strategic ambitions. Oppositions and disputes between the two East Asian great powers still prevail and are based on a series of aspects that sustain competition: competition for markets and energy resources that are vital for the two economies - in this case, Japan is more apprehensive about China's control over important navigation routes in East and South China Sea and its growing influence in Central Asia; competition over greater influence in Korea, South East Asia and South Asia; different perspectives towards the situation in Taiwan²¹; the dispute over the Senkaku/Diaoyutai islands; the interpretation of History, in which Beijing is constantly accusing Japan for not recognizing its mistakes and atrocities and seems to instrumentalize anti-Japanese feelings in the region; very distinct perspectives towards the presence and role of the US in the region; differentiated political and social models. In fact, Japan seems to participate in the US-lead regional efforts to "contain" and control China's rising, while China seems to oppose US-Japan "global alliance" and Japanese political and strategic expansion, as exemplified by Chinese opposition to the possibility of Japan becoming a permanent member of the UN Security Council. In other words, both are in mutual fear of each other and compete in terms of power and regional and international political status.

At the same time, however, China-Japan bilateral relations have improved significantly in the past years with visible and increasing mutual adjustments that include the stabilization of the Korea Peninsula, the cooperation within new security domains, the cooperation in institutions and multilateral regional processes (APEC, ASEM, ARF, 6-Party talks, ASEAN+3, EAS, and China-Japan-ROK Leaders' Meetings) and the development of economic and commercial ties: in 2007, for the first time since WW II, trade between China and Japan overtook trade between the US and Japan. When the Chinese President Jiang Zemin visited Japan in 1998, both sides declared the establishment of *Partnership of Friendship and Cooperation for Peace and Development*. During Japanese Prime Minister Abe's visit to China in October 2006, the creation of a China-Japan «*mutually beneficial relationship based on common strategic interests*» was announced. As such, on the 30th anniversary of the signing of the Treaty of Peace and Friendship between Japan and China of 1978, mutual relations seem better than never: during his official visit to China at the end of

21 Taiwan is a less problematic issue in China-Japan relations than in Sino-American relations. However, Taiwan is a former Japanese colony (1895 to 1945) and Beijing never stopped protesting against Tokyo's relations with Taipei or accusing Japan of interfering in a "Chinese matter". Beijing fears the possibility of Japan providing support to Taiwan and USA in case of military confrontation, while Tokyo fears a Chinese military intervention in Taiwan which would destabilize the region.

December 2007, Japanese Prime Minister Yasuo Fukuda underlined «*the three pillars that form the core of this relationship, namely the pillars of “mutually-beneficial cooperation”, “contributions to international society”, and “mutual understanding and mutual trust”*» (Fukuda, 2007). The fact is Japanese and Chinese governments use a variety of frameworks today to increase relations and mutual trust

US-China-Japan relations are obviously crucial for security and geopolitics in East Asia. In the midst of this game of containment and engagement, the situation seems to be satisfactorily balanced: «*when US-Chinese ties are strained, Beijing sees US-Japanese cooperation as an effort to contain China, but when the US-Chinese relations are good, Beijing tends to view the US-Japanese alliance as a check on Japan’s regional ambitions (...)* Historically, Asian states have become concerned whenever the US has grown close to Japan in order to contain China or close to China at the expense of traditional US allies and smaller regional powers. The situation today – a cooperative US-Chinese relationship, a strong US-Japanese alliance, and good relations between Japan and China – is a viable equilibrium» (Cha, 2007: 102-103).

This behavioral pattern is the core feature of what we can call “*conengagement*”, a major trace of the regional geopolitical system where most of East Asian actors simultaneously practice policies of “containment” and “engagement” in relation to each other. Indeed, “conengagement” is visible in practically all relations and goes well beyond the US-China-Japan triangle.

For example, Russia and Japan are historic rivals and relations between the two countries had not fully been normalized once there was no Peace Treaty concluded to this date after 63 years since the end of the World War II, largely due to the ongoing dispute over the South Kurilles/Northern Territories. Moreover, although the complementary potential of the two economies, Japanese-Russian economic/commercial relations are very limited. On the other hand, they seem still to belong to opposing “axis” - Japan is the key ally of the US in Asia-Pacific while Russia has a strategic partnership with China.

However, Russia-Japan bilateral relations continue to develop with negotiations that aim at establishing a Peace Treaty, solving the territorial dispute and increasing bilateral trade and investment. Japan has several assistance programs to support democratization and transition processes for Russia’s market economy, as well as humanitarian and technical assistance, elimination of nuclear weapons, nuclear power plant safety and energy security. There are also a series of bilateral agreements that aim at revitalizing economic exchange between Japan and the Russian Far East region. Additionally, Moscow and Tokyo have been cooperating at both a bilateral and multilateral frameworks

(6-Party talks, ARF, APEC or the UN) on specific common concerns ranging from WMD non-proliferation and denuclearization, stability in Northeast Asia and on the Korean Peninsula, counter-terrorism, energy, fisheries or environmental protection.

The same may be said of US-Russia relations. At one level, both powers compete to each other for greater political influence in the world, namely in the vast Eurasian region (see Tomé, 2007). In fact, the US and Russia have many conflicting goals as there are substantial divergences between them over many issues: NATO's enlargement and its "out of area" expansion; Kosovo's independence; "frozen conflicts" (Transnistria in Moldova, South Ossetia and Abkhazie in Georgia; Nagarno-Karabach in Azerbaijan and between Azerbaijan and Armenia); Russian minorities status in the three Baltic States (now that they have joined the EU and NATO); the political situation in the Ukraine, Georgia, Belarus or Uzbekistan; oil and natural gas exploration routes; level of threat and objectives of Iran's nuclear program, as well completely different relationships with Tehran from each other; also different views over, and relations with, Hezbollah, Syria, Lebanon, Saudi Arabia, Egipt, Israel, Palestinian Authority, and Hamas; Russian "incomplete democracy" and rolling back of human rights and press freedom; American "hegemonic behavior" and its intervention in Iraq; Russian arms sales to China, Iran or Syria; Russian instrumental policy with its energy resources and prices; American ballistic anti-missile defense system; American support to "colourful revolutions" and "regime change" pressure, particularly along Russia's periphery; Russia's not yet accession to the WTO; etc. In the end, Russia is trying to contain American hegemony (the "strategic triangle" with China and India is an important tool for that purpose) while the US is trying to contain Russia's resurgence and diminish its imperial sphere of influence. As such, confrontational and mutual containment strategies have been implemented in Eastern Europe, Balkans, South Caucasus, Caspian and Black Sea, Middle East, Central Asia, South Asia, and Northeast Asia.

At the same time, however, the US and Russia are also trying to articulate their positions and to enhance practical cooperation in a huge range of issues, from the fight against terrorism, narco-trafficking or WMD proliferation to energy security, environment protection, crisis management and conflicts resolution, reform of the United Nations or space matters - bilaterally and within international organizations (such as the UN, the OSCE, the APEC, and the ARF) or other multilateral frameworks (such as EAPC/PfP and NATO-Russia Council mechanisms). For example, as far Iran nuclear's program concerns they are trying to be cooperative working along with the IAEA and the UE and

within UN Security Council framework to find a peaceful solution; on North Korea's nuclear program they both are part of the 6-Party talks; they both cooperate in the peace process in the Middle East as part of the "Quartet", along with the EU and the UN; they are also articulating efforts to stabilize the Balkans, Iraq and Afghanistan and to find a solution (or, at least, to avoid dangers escalations) to the "frozen conflicts" in Eastern Europe. Moreover, on May 2002 President George W. Bush and President Vladimir Putin signed the Moscow Treaty on Strategic Offensive Reductions (SORT), while it was created the NATO-Russia Council; on July 2006 the US and Russia launched the *Global Initiative To Combat Nuclear Terrorism*; and on May 6, 2008 was signed a U.S.-Russia Agreement for Cooperation in the Field of Peaceful Uses of Nuclear Energy ("*123 Agreement*"²²) - provoking a huge discussion in the US Congress because Russian nuclear assistance to Iran. The fact is, up to a certain level, Russia and the US cooperate in the same regions and issues in which they also compete, working together with other great powers and actors. As Secretary Rice (2007) recognizes «*America's relationship with Russia will remain large and complex: a mix of cooperation and competition, friendship and friction*».

China and India are old Asian rivals which maintain territorial disputes (Aksai Chin and Arunachal Pradesh) and have apprehensively witnessed each other's resurgence. We must add that China is Pakistan's ally, India's main opponent - New Dehly has accused Beijing to arm Pakistan with nuclear weapons and missiles and to try to open a new Chinese flank against India via Myanmar - and that India is presently much closer to the US and Japan than in the past: when in 2007 started the exploratory "Quadrilateral Initiative", Beijing was quick to see the apparition of an "Asian NATO". So, up to a certain point, China and India compete for greater influence in all of Asia while suspecting each other's strategic ambitions.

At the same time, however, China and India have maintained a strategic partnership since 2003 that envisages the promotion of the "Asian Century". A significant increase in bilateral trade has been registered since it multiplied seven times since 2002, with future prospects of an increase of over USD 40 billion before 2010. Meanwhile, China-India cooperation has extended to other areas including the anti-terrorist fight, energy security or disaster response as they have been adjusting their positions to stabilize Myanmar and South Asia, including Nepal, Bangladesh and Pakistan. The positive development of Sino-Indian relations has lead India (which has always supported the Tibetan cause

22 A "123 Agreement" refers to Section 123 of the U.S. Atomic Energy Act of 1954, which indicates the terms that must be included in U.S. agreements for nuclear cooperation with other states.

and where more than 100 000 exiled Tibetans live, including the Dalai Lama) to “assume” Tibet as a part of China and China to support the entrance of India as a permanent member of the UNSC. Moreover, India has supported China’s entrance into the WTO and holds the status of observer in the SCO which is led by China; China has supported the entrance of India into APEC and it had also previously supported Indian participation in the ASEM besides motivating India’s accession to the SCO; and among other pan-regional forums, both have cooperated in the ARF and the EAS. The two great Asian powers have also begun joint military exercises and both participate in trilateral ministerial meetings with Russia, adjusting positions in favor of “multipolarity”.

The US and India have a history of relatively distant relations which has been furthered by India’s strategic partnerships with Russia, China and Iran, which suggest India’s position on a anti-US Asian axis, not to mention that the US is Pakistan’s ally (even though it has never supported Islamabad against New Dehli and has always maintained a neutral position in relation to India-Pakistan conflicts).

Nowadays the US and India are real strategic partners which collaborate in many areas, ranging from the fight against terrorism and WMD counter-proliferation to the stabilization of South/Southeast Asia or disaster response. These positive relations are evident in delicate topics such as that of nuclear domain: in July 2005, President George W. Bush and Prime Minister Manmohan Singh announced a broad slate of initiatives as part of the new commitment to a comprehensive bilateral relationship, including the launch of a *Civil Nuclear Cooperation Initiative*, reaffirmed it in March 2006 with the *Civil Nuclear Cooperation Agreement* (also known as the “Hyde Act”); on August 3, 2007 both countries signed the US-India “123 Agreement”. Meanwhile, Americans and Indians completed over more than fifty joint military exercises between 2003 and 2007 and, in May 2007, India became part of the “Quadrilateral Initiative”, which suggests the existence of a cooperative American-Indian strategy to control China’s rising.

ASEAN tries to limit China’s influence in Southeast Asia and fears Chinese resurgence, thus considering that territorial disputes in the South China Sea between China and several ASEAN nations are not resolved, and occasionally flare up (mainly over Paracel and Spratleys Islands, which are also rich areas in terms of oil and gas resources), besides other potentially disturbing aspects concerning mutual relations may be added: several Southeast Asian nations have bad historical memoirs with China, including political domination, military conflicts and Chinese past support of communist insurgency;

the Southeast Asian countries and China are critically dependent on regional sea-lanes for trade - China in particular is becoming more dependent upon critical sea lanes for its energy imports and thus more encouraged to control the Malacca Straits, through which 80 percent of China's crude oil imports passes through; China and ASEAN are also direct competitors for foreign investment, rather than significant investors in each other economies; there are some problems with large overseas ethnic Chinese communities in several Southeast Asian nations; and several ASEAN members are still US allies or strategic partners.

Despite these challenges, China-ASEAN cooperation covers practically all areas, ranging from Cambodia's peace process to economy and trade, the socio-political crisis in Myanmar, disaster response, counter-terrorism or fighting sea piracy. In fact, Southeast Asian Countries are priority targets of China's charm policy, which aims at presenting China as a "benign power" and a "friendly elephant", while ASEAN proceeds with its closer engagement policy and objective of drawing China closer. Since China was accorded full ASEAN's Dialogue Partner status in 1996, bilateral cooperation has been greatly improved and China has entered into a number of agreements with ASEAN both in economic and security issues. In November 2004, an ASEAN-China *Agreement on Trade in Goods of the Framework Agreement on Comprehensive Economic Cooperation* was signed, giving a further significant impetus to a trade relationship on which the 10 ASEAN members have become increasingly dependent, particularly since the 1997-98 Asian financial crisis. This occasion was also a major step towards the realisation of an ASEAN-China Free Trade Area (ACFTA), which is set to be established by 2010 - following a proposal by then-Chinese Premier Zhu Rongji at the ASEAN-China Summit in November 2000. As such, ASEAN trade with China is rapidly overtaking trade with the US, with Japan and with the European Union.

ASEAN and China have also reached several agreements in the area of political and security cooperation, including the *Joint Declaration on Cooperation in the Field of Non-traditional Security Issues* and the *Declaration on the Conduct (DOC) of Parties in the South China Sea* (2002), the *Joint Declaration on Strategic Partnership for Peace and Prosperity* (2003), and the *Memorandum of Understanding Cooperation in the Field of Non-traditional Security Issues* (2004). China was also the first Dialogue Partner to accede to the *Treaty of Amity and Cooperation in Southeast Asia* (2003) and has expressed its willingness for its early accession to the Protocol to the Treaty on Southeast Asia Nuclear Weapons-Free Zone. Besides this ASEAN+1 channel, China also participates in other ASEAN

initiatives such as ASEAN-PMC, ASEAN+3, ARF or EAS, as well as cooperate with most ASEAN countries in the APEC and ASEM.

Meanwhile, the engagement and cooperation between great powers has had positive outcomes in other historically tense bilateral relations.

For instance, not only does the Korean Peninsula remain divided but Pyongyang and Seoul also both maintain their suspicions and reservations towards each other as they compete over international status and recognition. However, by taking advantage of the positive US-China relations and the framework of the 6-Party talks, inter-Korean relations have progressed well and have become more cooperative. In the October 2-4, 2007 inter-Korean historic Summit, in Pyongyang, ROK's President Roh Moo-hyun and DPKR's leader Kim Jong-il signed the *Declaration on the Advancement of North-South Korean Relations* and committed to combining efforts in a mutually reinforcing manner for a permanent peace regime and eventual reunification on the Korean Peninsula, moving inter-Korean relations to a higher stage, based on the Joint Declaration of June 2000 and the spirit of "*by our nation itself*".

In relation to the Taiwan question (see more on Jorge Silva's essay in this book), of all the three parts involved, the US is obviously the most interested in the *status quo* and has often said it opposes attempts by either side – China and Taiwan – to unilaterally alter the *status quo* in the Taiwan Strait area. For their part, Beijing and Taipei's dissatisfaction with the *status quo* has increased in the last two decades: Taiwan's two former Presidents (Lee Teng-hui and Chen Shui-bian) have frequently asserted that Taiwan is a state separate from China, sovereign and independent, as also proclaimed a *taiwanese identity*; China's leaders have repeatedly asserted "the sacred One China Principle" and have threatened to use force to achieve unification, as also indicated that "indefinite delays" could justify its military intervention; Taipei has continued to acquire weapons (mainly from the US) and modernize its armed forces to dissuade China from attacking – between 1998 and 2005, USD 13.9 billion of military weapons were sold to Taiwan; and China's military buildup is mainly oriented to expand its options for an armed conflict against Taiwan and has deployed ballistic missiles and assault capabilities along the Taiwan Strait.

Especially since Chen Shui-bian's election for President of Taiwan in 2000, the tension between Beijing and Taipei has increased. Chen's persistent pro-independentist manoeuvres (including a vigorous diplomatic campaign to make Taiwan member of the United Nations and his proposed referendum – that took place in March 2008 – asking whether the government should bid to join the UN under the name of "Taiwan" instead of "Republic of China") has

alarmed Mainland China that, in response, announced increasing willingness to consider using force - as it did in the *Anti-Secession Law* approved in 2005. In fact, Chen's actions has led Beijing to escalate its threats, at a minimum, to avoid taiwanese definitive movement toward independence. At the same time, the US has admonished Chen Shui-bian's for its provocative and dangerous moves and not to risk putting the *status quo* at stake.

Despite this permanent diplomatic-military tension, Taiwan's defense budget dropped 25 percent between 2001 and 2006 and economic and trade exchange have increased significantly: China-Taiwan bilateral trade went from USD 8 billion in 1991 to USD 115 billion in 2006; Taiwanese investment in Mainland China represents more than half of Taiwan's overseas investment, placing Taiwan on the top ten of foreign direct investors in China; and China has become Taiwan's top trade partner. Moreover, Mainland China and Taiwan (as "Chinese Taipei") participate and are both part of some international institutions such as APEC (since 1991) and WTO (since 2001).

Above all, besides the "official" rethoric from both sides of the Strait, the direct contacts between Beijing and then Taiwan's opposition KMT/Nationalist Party in the past few years are of significant importance, founding common cause in their opposition to President Chen Shui-bian and the so-called taiwanese "Pan-Green Coalition". This aspect is even more important considering that KMT won landslide victories in legislative elections in January 2008 and Presidential elections in March 2008 against the Democratic Progressive Party (DPP) of Chen. In other words, the closer engagement policy with Mainland China, a more cautious approach in dealing with Beijing and the *chinese identity* are indeed winning room in Taiwan - as well as the conscienceness of to rebuild trust with the US.

This does not mean, of course, that the "problem of Taiwan" is to be settled soon - Taipei-Beijing and the US-China mutual distrust still prevail, there are still many dangers, and the situation need to be carefully handle by all the three parts involved. But it seems now that there are better chances to ease tensions and maybe to start gradually changing the *status quo*.

Finally, this logic of competition and engagement has overtaken bilateral relations. For example, the Russia-China axis competes with the US-Japan axis and both "camps" try to attract India into their own sides. But the network of relations is much more complex and contains many cooperative elements: the US, China, Russia and Japan cooperate in the 6-Party talks and in APEC; China, Japan and India participate and cooperate in the EAS framework; and all these great powers are ASEAN Dialogue Partners and participate in the

ASEAN-PMC and ARF, cooperating in the most diverse areas that range from trade to counter-terrorism, from the fight against poverty and undevelopment to nuclear counter-proliferation, energy security, environmental improvement, and disaster response.

“Hedging”

At the same time, all East Asian actors are putting into practice the so called “hedging” strategy. Robert Sutter is probably who best explains and summarises the meaning of hedging: *«using more diversified diplomacy, military preparations and other means to insure that their particular security interests will be safeguarded, especially in case the regional situation should change for the worse»* (2003: 199); *«Hedging in this regard involves pursuing various paths to secure a nation’s interests in an uncertain environment. Thus, while pursuing détente with a former adversary, a nation may continue to pursue military modernization and improved relations with the adversary’s neighbors as a means to keep the adversary in check should the détente fail. It also means that a country’s ostensible foreign policy approach may have varied and sometimes hidden objectives, allowing the country to benefit under varied circumstances in a fluid regional context»* (2005a: 273). In other words, East Asian countries do not put “all the eggs into the same basket” but instead, play in all directions and in all possible fields.

A part of this hedging strategy is based on a game of control, containment and engagement between the powers previously mentioned in this paper: for example, the US about China formally assumes *«hedging against the unknown»* (USDoD, 2008: I). The balance between bilateral relationships and multilateralism should also be considered as part of regional hedging strategy. But there are other illustrative examples of hedging practices in the region.

Mongolia (the seventh largest country in Asia for its territory, which covers an area of 1,564.100 sq. km, larger than the overall combined territory of the UK, France, Germany and Italy, but with a population of only 2.9 million), land-locked between Russian Siberia and Northern China, approached the US with the objective of freeing itself from its geopolitic constraints: since the establishment of diplomatic relations between the two countries in 1987, and particularly after the “democratic revolution” in 1990, the bilateral relationship has developed dynamically. The US has actively supported Mongolian democracy and reforms: the US Agency for International Development (USAID) is providing assistance to Mongolia, totalling about USD 150 million, all in grant form during 1991-2005; between 1993 and 2005, Washington provided food aid to Mongolia under the Food for Progress programs; Mongolia was

granted permanent normal trade relations (NTR) status and generalized system of preference (GSP) eligibility in June 1999; the *Trade and Investment Framework Agreement* was signed between the two countries in July 2004 to promote economic reform and more foreign investment. The US has also supported defense reform and an increased capacity by Mongolia's armed forces to participate in international peacekeeping operations.

For these reasons, Mongolia has demonstrated that it is an interesting strategic partner for the US, contributing with more than 1000 troops in 8 rotations to coalition operations in Iraq since 2003. As a form of recognition, President Bush visited Mongolia in November 2005. Similarly, Mongolia and the U.S. jointly hosted "Khan Quest 06," the Asian region's premier peacekeeping exercise in 2006.

However, at the same time, Mongolia has incremented its bilateral relations with China (its first trade partner, representing half of the Mongolian trade), with Russia (its second trade partner), as well as with Japan (its third trade partner). Furthermore, Mongolia holds the status of observer and has applied for membership in the SCO, lead by China and Russia.

Seoul fears China's resurgence and its future behavior towards the Korean Peninsula. However, as mentioned earlier, South Korea has improved its relations with China. Since 2004, for instance, China has overtaken the US by becoming South Korea's major trade partner: in 1991, a year before the normalization of China-South Korea diplomatic relations, China accounted for just over 1% of South Korea's exports; by 2006, China accounted for almost 22%. At the same time, and in addition to the positive bilateral relationships with Beijing, Seoul has participated in the China-Japan-ROK Leaders' Meetings, in the ASEAN+3 process and in the EAS, which China participates in but the US does not. Moreover, there is the improvement in Seoul's relationships with North Korea as well as the development of its bilateral relations with the Russian Federation, Japan or ASEAN.

Despite the improvement of its external relations and the existence of a more peaceful external context, Seoul intends to increase its defense budget in the next decade by about 10% a year. On the other hand, although it is closer to China, South Korea has also become more independent in relation to the US as previously discussed, both at an economic and military level. However, in June 2007, Seoul and Washington signed a far-reaching free-trade agreement (FTA) that became the largest bilateral FTA ever signed by the US with a total trade valued annually at over USD 80 billion. Additionally, the alliance with the US not only has remained solid but has also expanded: for example,

South Korea has provided the third-largest contingent of troops in Iraq; Seoul has contributed with financial and logistic support for the NATO-led ISAF in Afghanistan and also for its Provincial Reconstruction Teams (PRTs); and South Korea is now a NATO's "Contact Country".

The truth is that Seoul knows that despite the current peacefulness and good relations with North Korea, China, Russia and Japan, South Korea may lose its status and may be treated differently by its powerful neighbouring countries without American support.

Despite their fear of China, ASEAN countries have tried to attract and develop relations with Beijing by means of mechanisms such as ASEAN+1, ASEAN+3, ARF, APEC ou EAS. At the same time, the majority of ASEAN countries support a strong strategic American presence in the region and some of them are indeed US' allies. In this East Asian sub-region, the US signed a strategic framework agreement on security cooperation with Singapore in 2004; it strengthened its political and military ties with Indonesia as a result of the post-tsunami help; it further developed US-ASEAN enhanced partnership to address a series of matters; and it sustains high-level military cooperation and continues to provide military training and equipments to several Southeast Asian countries.

In the meantime, as it tries to balance its relations with China and the US, ASEAN continues developing its "bilateral" relations with all its other Dialogue Partners (Australia, Canada, the EU, India, Japan, South Korea, New Zealand, Russia, and the UN) as well as with other intergovernmental regional groups. On the other hand, as they try to limit external influence of great powers and increase their own margin of political manoeuvre, ASEAN countries also try to attract Washington and Beijing to the "ASEAN vision" and put the idea of an East Asia Community into effect. At the same time, ASEAN countries expenses and military capacities have increased despite the relatively stabilized and moderate context. All this is "hedging"...

Even the small and recent State of Timor-Leste has put the hedging strategy into practice. If, on the one hand, it tries to affirm its independence in relation to its two powerful neighbours, Indonesia and Australia, on the other, it accepts the presence of an important Australian military contingent on its territory and has applied for membership in the ASEAN which is led by Indonesia. At the same time, Timor-Leste has remained under the protection and vigilance of the United Nations and has strengthened its ties with Portugal (it held colonial power in the country until the Indonesian invasion in 1975 and was the main supporter of Timor's self-determination and independence, from

1999 to 2002) and with the other members of the Community of Portuguese Language Countries (CPLP).

India is another paradigmatic case of hedging strategy performance. As previously mentioned, India is part of the «*Quadrilateral Initiative*» (QI): within this frame, in September 2007, Indian navy forces joined American, Japanese, Australian and Singaporean forces for a joint exercise in the Bay of Bengal. Almost simultaneously, the Indian Minister of Foreign Affairs, Pranab Mukherjee, participated in the third ministerial-level meeting Russia-China-India (October 2007), while the Indian military was training Iranian troops and New Dehli was closing energy purchase agreements with Iran within the framework of the India-Iran strategic partnership. All this went on at the same time that India affirmed itself as leader of the “Global South” in the WTO round negotiations of Doha. Pure hedging...

Finally, a good indicator of the complexity of regional order and of hedging strategy is the fact that East Asian budgets and military capacities continue to increase within a more moderate context of greater regional cooperation, multilateralism and economic interdependence.

Conclusion

There are three key words, all of them closely interconnected, which help define the security and geopolitics in East Asia today:

- *Expansion*: the expansion of security concerns, which combine “new” security issues and dangers with “traditional” security threats and dilemmas; expansion of regional border security - Northeast Asia and Southeast Asia have become more inter-connected and East Asia as a whole has not only become more connected with neighbouring regions such as Central and South Asia, but with the global system as well; expansion of bilateral interaction and interdependence as well as multilateralism and regionalism; expansion of China’s influence, of Japan’s strategic role and the geopolitic importance of other regional (Russia, ROK, Mongolia and ASEAN) and “extra-regional” (US, India ou Australia) actors; and the expansion of East Asia’s impact on international politics.
- *Pragmatism*: pragmatism in the way East Asian actors develop their bilateral relations and promote multilateralism; pragmatism in the type of multilateral regional cooperation, maintaining the decision by

consensus, safeguarding the principle of absolute non-interference, giving preference to informal and flexible approaches that do not imply great concessions from national entities or very rigid compromises; pragmatism in the use of instruments for promoting stability, security and economic development, creating a very dense and complex network of relations and institutions of different kinds and levels, with distinct compositions and objectives; pragmatism in the way East Asian actors promote, adjust, and deal with their interests, cooperating when and where it is possible and putting any stronger issues or divergences aside; pragmatism may also be attributed to regional actors not only in the simultaneous exercise of containment and mutual engagement, but also for the way the hedging strategy is put into practice.

- *Control*: each nation controls its own aspirations and ambitions without attempting against other nations's interests but also without giving up their own vital positions; control of adversary and partner's policies, strategies and capabilities as well as control over the regional situation. More than just containment, mere engagement or a combination of "conengagement", what becomes significantly noteworthy is a regional policy of mutual control, in which actors try to guarantee that the situation develops favourably and that their positions are safeguarded in case the situation deteriorates.

All powers and regional actors give great priority to stability and economic development and as such, they feel the need for a peaceful environment. This constitutes an incentive for them to look for possible adjustments in their structures of power and come to terms in relation to their diverging interests. In the same way, the fact that all of them are faced with common dangers and security problems provides additional motivation to find common answers and solutions. For this reason, actors and powers operating in East Asia have tried to develop confidence building measures and strengthen mutual political and economic ties by means of a pondered approach which aims at stabilizing regional order.

At the same time, however, there are re-emerging powers with uncertain future behavior; traditional and new security problems are increasing; divergences of interest exist among great powers; budgets and military capacities continue to increase; the balance of power scale, the hierarchy between great powers and the role/status of actors are not consolidated as also are under

pressure and undergoing great changes, causing uncertainties and insecurities about the future order in East Asia.

The result of all this is an environment which is certainly more peaceful than in the past, but it is also more volatile, uncertain and unpredictable.

On the other hand, instead of a defined system of security in East Asia, what exists today is a security complex made up of co-existing systems, such as *competitive security* (based on self-help security and with competitive axis, where actors fear each other and formulate their security in distributional terms), *cooperative security* (in general, perception of immediate threat from potential adversaries is inexistent and actors cooperate with each other to solve common security problems) and *common security* (based on the premise that the security of one country depends on the security of another even if they fear each other), while there is also a *security community* (based on a cultural-institutional context where political survival is guaranteed by all partners and in which the use of force as a political instrument between members becomes more and more illegitimate) which is building in East Asia and it is particularly evident in Southeast Asia.

There is containment and mutual control in East Asia today but there is also engagement and cooperation. There is multilateralism but it does not affect the weight of bilateralism. There are many security problems but there are also more instruments and “pillows” to help solve them. There is anarchy in the sense of an arena where all play against each other in a very dynamic and constantly changing situation, but there is also more order with more regimes, institutions, conventions, treaties, agreements and joint declarations. For all these, East Asia is, undoubtedly, a region with two faces.

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Economic Dynamics in East Asia Today

Henrique Morais

Introduction

East Asia is a huge market of 2.24 billion people which includes countries such as the People's Republic of China, with its 1.32 billion inhabitants, and tiny Brunei, where no more than 400,000 people reside.

East Asia represents around 34% of the world population, undoubtedly the most populated region. It is also one of the areas in the world with the highest rate of young population, along with Africa and Latin America.

However, there are significant and extreme economic and social differences in the region. In economic terms, more advanced economies, as is the case of Japan (the world's second world economy, right after the USA), South Korea (as well as Singapore and Taiwan) coexist with very poor countries like Timor-Leste, Myanmar, Cambodia or Indonesia.

Considering this diversity, which hides fundamental and sometimes irreconcilable differences in terms of religion, culture and lifestyle, it is difficult to define an unique scenario for the region. In fact, besides the differences among the countries in the region, there are even specificities within the same country. China, which will be analyzed in detail in this text, is an example of this.

On the other hand, within the present context of apparently inevitable globalization, it is important to analyze how far the region has adapted to recent trends.

East Asian Economies: adjusting to new challenges

East Asian countries in general seem to have adapted perfectly to an increasingly more dynamic world, in which change occurs at a sometimes too fast a pace¹.

The fact that many of East Asian countries are small open economies, naturally very much dependent on international trade, but in a very good position to compete in current global markets, has contributed to the easy adjustment to globalization.

Asian countries greater openness to international trade has also its disadvantages, namely, it makes them more dependent on the world economic conjuncture (i.e., more exposed to recessions imported from abroad), as well as on sometimes less positive evolutions of international markets, for example, as far as exchange rate variation is concerned.

The Asian financial crisis in the summer of 1997 is an obvious example of this external dependency and how events spread at a sometimes uncontrollable pace. As soon as the crisis began in Thailand (as a result of the difficulties in the balance of payments due to an overrated *bath*), its consequences to other countries in the region were unpredictable.

In Asia, very few economies remained unscathed by the crisis. There were only three exceptions: China, due to the self-imposed isolation the country was in at the time; Hong Kong, because of the financial power of its monetary authority, and Taiwan, since it realized it was not possible to prevent the approaching “avalanche” and quickly and decisively devalued its currency. Even the Japanese economy was affected. The Asian crisis has probably significantly determined what would become a decade of mild economic growth in Japan and, especially, of deflation.

Economists almost unanimously agree that the effects of the Asian crisis were not limited to the region. On the contrary, the Russian crisis (in the following year) would largely be the result of the deterioration of the Russian balance of payments, which was a response to the decrease of demand from

1 It seems that many East Asian economies are, in fact, some of the biggest “winners” of globalization.

Asia². In fact, some global instances of the crisis are visible, such as, the decrease in global demand, specially of goods, as well as the decrease in the price of raw-materials, such as oil and copper, and, in general, of farming goods.

The Asian crisis seems to have been caused by the sudden shift in investors' feelings as far as privileged destinations of international capital influx are concerned. However, the structural reasons of the crisis were deeper and related to the inefficiency of most financial systems of the region, which would lead to bad credit, lack of prudent and operating banking supervision and, above all, inadequate exchange regime, i.e., the dollar peg³ exchange rate regime.

The exchange rate regime was decisive for the evolution and scope of the crisis. As the maintenance of local currencies connected to the dollar was causing persistent imbalances in the trade balance, which were financed by external capital influxes (especially from countries where the interest rates were lower), it became clear for international investors that, sooner or later, these currencies would suddenly suffer devaluation. From that moment onwards, it was only a question of time for foreign investors to abandon the region and for the 1997 Asian crisis to begin.

Therefore, one may conclude that, with the exception of Thailand, there was at the time no real macroeconomic global imbalance in East Asia, which would be accountable for the financial crisis. On the contrary, most of the economies in the region were growing steadily and had budget and trade surpluses.

As such, the structural reasons behind the crisis, besides the problems related to the currency exchange structure, should be found elsewhere rather than in the regional economic scenario.

At the time, the organization of the productive system in most of East Asian countries was rather deficient in areas such as management and control, as well as in exchange of information.

The Asian companies were managed using “corporate socialism”, which led to the existence of technically bankrupt companies still operating. The companies' control was in the hands of managers, often linked to shady lobbies, who were not concerned with the real interests of the stakeholders.

2 Though the problems Russia went through in 1998 were not due to this phenomenon, they were also linked to the negative evolution in terms of exchange rate, especially because its currency, the ruble, was artificially strong.

3 The peg basically consisted in a very close connection to the USD, i.e., when the USD valued or devalued in terms of the yen, for example, the local currency would suffer the same evaluation or devaluation as the USD.

This scenario, particularly for foreign investors, was ripe for doubt on the solidity of the East Asian business (and financial) system. As there were failures in terms of information exchange⁴, it is not surprising how fast and intensely the financial crisis spread in the region.

In a few short months, capitals started disappearing from East Asia and local currencies began to devalue strongly: between 30 June and 31 December 1997, the Thai bath devalued 88%, the Philippinean peso 51%, the Malayan ringgit 54% and the Indonesian rupee 126%!

The economic consequences were soon visible as there was a decrease in family demand (due to the high rise in the price of imported goods) and consequent decrease in production, followed by business deterioration. Finally, public finance, which had been strong up to then, also collapsed.

The 1997 Asian crisis, due to its historic closeness and, in particular, the lessons it entails, is a good example of how certain models of economic growth, too externally based, are precarious.

This is the context underlying this essay, in which a scenario of the region's current economic situation will be drawn.

Eastern Asia Today: Some economic indicators, facts and figures

The lessons learned in the nineties were very efficient and ten years later, Asia is again the most dynamic region in the global economy. In particular, Eastern Asia's⁵ growth in the last 10 years has been remarkably strong and with the exception of Japan, it clearly surpasses the world average.

4 These, in fact, still persist, which is made evident by the quality (?) of the official statistics in countries like the People's Republic of China.

5 In this group, we considered Japan, Korea, Singapore, Taiwan, Brunei, China, Cambodia, Indonesia, Lao, Malaysia, Myanmar, Philippines, Thailand, East-Timor, Vietnam and also Russia and Mongolia.

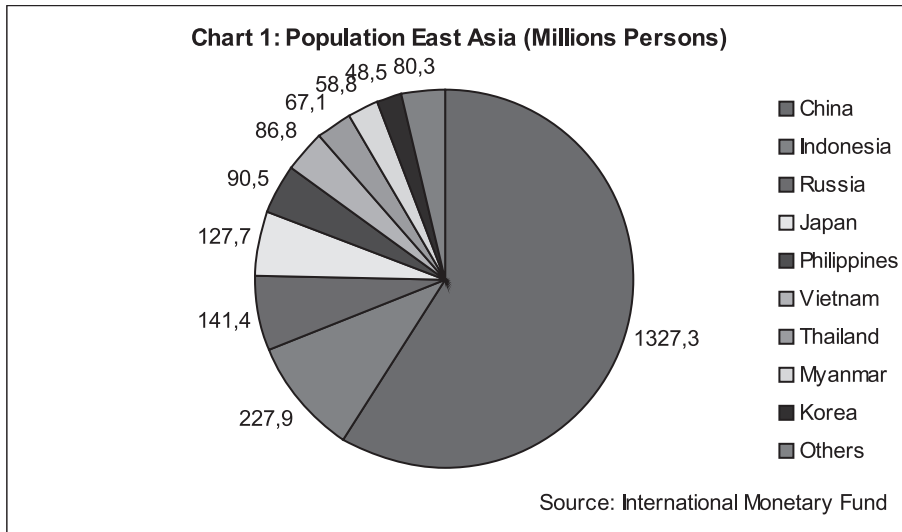


Table 1 shows that, within the four Asian countries that are considered advanced economies (Japan, Korea, Singapore and Taiwan) only one – Japan – has grown below the world average growth of **Gross Domestic Product (GDP)** in the last twenty years. Notably, the three Asian tigers have not only grown stronger than advanced economies, but also stronger than the average of emerging markets and developing countries.

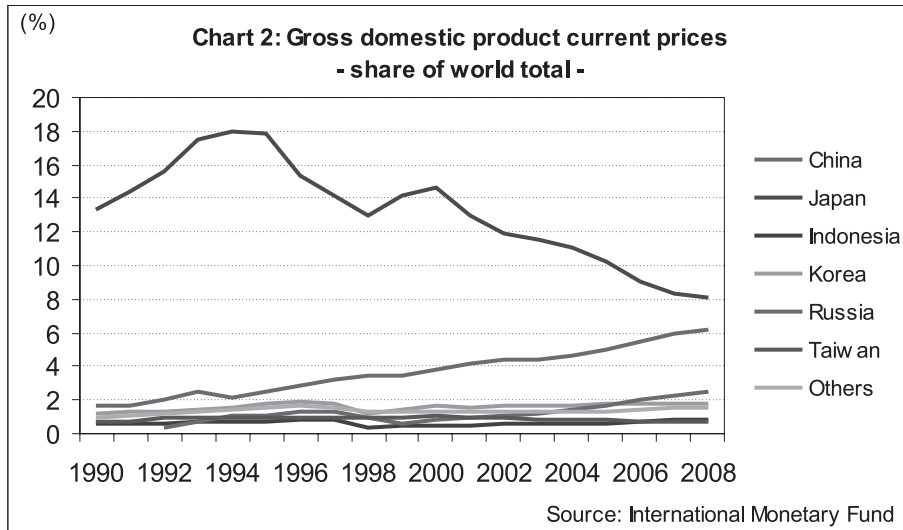
Table 1: Financial and Economic Indicators – Real Gross Domestic Product

	Ten-Year Averages											
	1989-1998	1999-2008	1999	2000	2001	2002	2003	2004	2005	2006	2007 ^P	2008 ^P
Real GDP (annual percent change)												
World	3,2	4,4	3,8	4,8	2,5	3,1	4,0	5,3	4,8	5,4	5,2	4,8
Advanced economies	2,7	2,6	3,5	4,0	1,2	1,6	1,9	3,2	2,5	2,9	2,5	2,2
Japan	2,0	1,5	-0,1	2,9	0,2	0,3	1,4	2,7	1,9	2,2	2,0	1,7
Korea	5,9	5,5	9,5	8,5	3,8	7,0	3,1	4,7	4,2	5,0	4,8	4,6
Singapore	7,8	5,8	7,2	10,1	-2,4	4,2	3,1	8,8	6,6	7,9	7,5	5,8
Taiwan	6,8	4,0	5,7	5,8	-2,2	4,6	3,5	6,2	4,1	4,7	4,1	3,8
Other emerging market and developing countries	3,8	6,4	4,1	6,0	4,3	5,0	6,7	7,7	7,5	7,9	7,5	7,1
Brunei	-	2,6	3,1	2,9	2,7	3,9	2,9	0,5	0,4	5,1	1,9	2,3
China	9,6	9,7	7,6	8,4	8,3	9,1	10,0	10,1	10,4	11,1	11,5	10,0
Cambodia	-	9,6	12,1	8,8	8,1	6,6	8,5	10,3	13,3	10,8	9,5	7,7
Indonesia	4,8	4,8	0,8	5,4	3,6	4,5	4,8	5,0	5,7	5,5	6,2	6,1
Lao	6,6	6,7	7,3	5,8	5,7	5,9	6,1	6,4	7,1	7,6	7,1	7,6
Malaysia	7,4	5,5	6,1	8,9	0,3	4,4	5,5	7,2	5,2	5,9	5,8	5,6
Myanmar	5,3	11,1	10,9	13,7	11,3	12,0	13,8	13,6	13,6	12,7	5,5	4,0
Philippines	3,0	4,9	3,4	6,0	1,8	4,4	4,9	6,4	4,9	5,4	6,3	5,8
Thailand	5,8	4,8	4,4	4,8	2,2	5,3	7,1	6,3	4,5	5,0	4,0	4,5
Timor-Leste	-	5,6	-	15,5	16,5	-6,7	-6,2	0,3	2,3	-2,9	27,4	3,8
Vietnam	7,7	7,4	4,8	6,8	6,9	7,1	7,3	7,8	8,4	8,2	8,3	8,2
Russia	-	6,7	6,4	10,0	5,1	4,7	7,3	7,2	6,4	6,7	7,0	6,5
Mongolia	-0,3	6,2	3,2	3,9	1,9	1,8	5,4	13,3	7,6	8,6	8,5	7,5

Source: IMF - World Economic Outlook (October 2007)

Over the past twenty years, the eleven Eastern Asian countries (including Russia and Mongolia) have also performed quite well economically: with the exception of small countries such as Brunei and Mongolia, all others have had an average GDP growth of over 4 percent. Countries such as China, Cambodia, Lao, Myanmar and Vietnam were net contributors for the strong growth in Eastern Asia, notably in the last ten years.

However, there are differences in the growth patterns between Eastern Asian economies. Japan, for instance, has lost some economic share worldwide, and its GDP will probably represent around 8 percent of world GDP in 2008. In the beginning of the 1990's, it was 13 percent and, in 1994 it was over 18 percent.



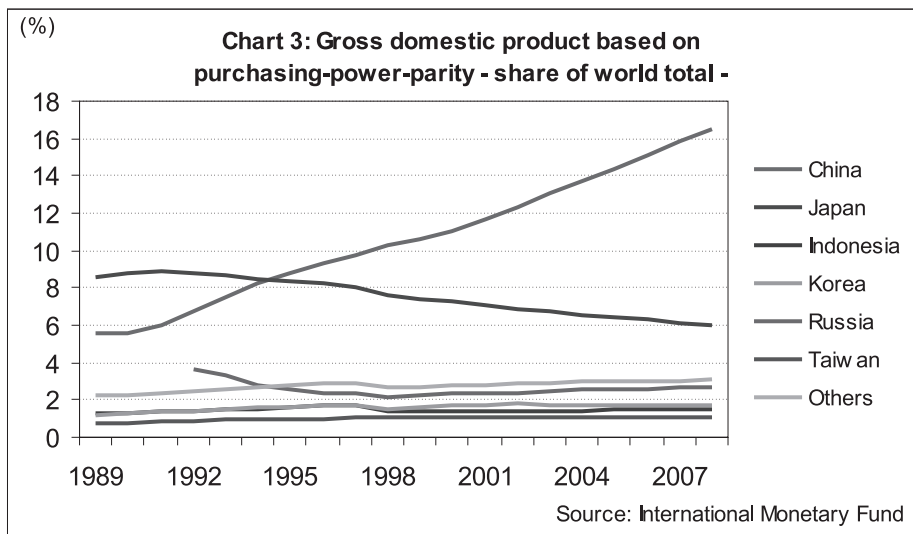
This relative weakness of Japanese economy was responsible for the low Eastern Asia weight in the world economy: in 1996/97, Eastern Asia share was 25 percent of world GDP, a weight that fell to 22.3 percent in 1998, in the aftermath of the financial crisis. Surprisingly, if we don't take the Japanese situation into account, the weight will probably represent 23.2 percent in 2008.

The weakness of Japanese economy was mainly the result of less favourable economic and monetary policies which lead to a bubble in asset markets (especially in the housing market and stock market) in the end of the 1980's. Later on, the fall of those markets provoked an explosive reaction from households, leading consumer standards to unprecedented restraint levels leading

the country back into the deflation process it had been recovering from since 2006.

On the other hand, most of the Eastern Asian countries have GDP weights between 0.5 percent and 2 percent revealing substantial stability along the last 20 years, although the trend seems to be for a slight increase.

Finally, two countries should be mentioned for the amazing share growth in world economy: China and Russia. In the beginning of the 1990's China represented just 1.7 percent of the world GDP; now its share is around 6.2 percent of the world GDP! However, China's strong economic increase is better understandable if we use the GDP based on purchasing-power-parity methodology⁶: in 1990, China GDP was 5.6 percent of the world GDP, in 2008 it would represent 16.6 percent. According to the International Monetary Fund in its recent World Economic Outlook, China GDP passed over the Euro zone GDP in purchasing-power-parity, for the first time ever (15.1 percent against 14.7 percent) in 2006 and was just a few notches below the United States which represented 19.7 percent of world GDP.

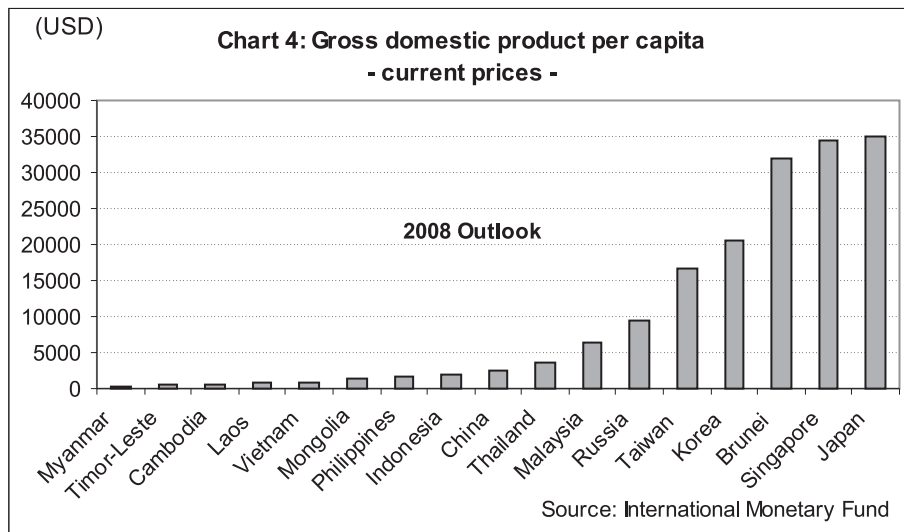


Russia is another successful country, at least in terms of its GDP growth: in 1992 (first year that we have records) its share of world GDP was 0.4 percent;

6 The purchasing-power-parity GDP is the best indicator to conduct international analyses between countries that have very significant differences in living standards and purchasing power. It would give us a realistic scenario in terms of the effective GDP of each country.

in 2008 it will be over 2.5 percent. However, in terms of purchasing-power-parity, Russian GDP actually decreased, from 3.7 percent of world GDP in 1992, to the current 2.7 percent of world GDP.

On the other hand, considerable inequality across countries in terms of gross domestic product per capita is still verified. Once again, IMF forecasts that next year, Eastern Asia GDP per capita will vary from the unbelievable 242 US dollars in Myanmar to the more than 34.8 thousands in Japan. China continues to be just the nineteenth country in the rating but the GDP per capita has grown an amazing 6.5 times since 2000!



Another curious indicator is the **current account balance in percent of GDP** (shown in Table 2). The situation is quite similar to that observed about the Gross Domestic Product, meaning that the majority of Eastern countries have posted a strong and structural positive balance, with the exception of the small and poor countries already referred to in the GDP situation.

Table 2: Financial and Economic Indicators - Current Account Balance

	Ten-Year Averages											
	1989-1998	1999-2008	1999	2000	2001	2002	2003	2004	2005	2006	2007 ^P	2008 ^P
Current account balance (percent of GDP)												
Advanced economies	0,0	-1,0	-0,4	-1,0	-0,8	-0,8	-0,7	-0,7	-1,3	-1,4	-1,3	-1,4
Japan	2,3	3,2	2,6	2,6	2,1	2,9	3,2	3,7	3,6	3,9	3,9	3,6
Korea	0,1	2,0	5,5	2,4	1,7	1,0	2,0	4,1	1,9	0,7	0,3	0,0
Singapore	13,5	20,7	17,4	11,6	14,0	13,7	24,2	20,1	24,5	27,5	27,1	26,6
Taiwan	4,0	6,2	2,7	2,8	6,3	8,7	9,8	5,7	4,6	7,1	7,1	7,1
Other emerging market and developing countries	-1,6	2,4	-0,3	1,4	0,6	1,2	2,0	2,4	4,1	4,8	4,0	3,7
Brunei	59,1	49,6	33,7	48,6	51,5	42,5	49,6	47,9	56,0	55,2	55,2	55,9
China	1,4	5,4	1,4	1,7	1,3	2,4	2,8	3,6	7,2	9,4	11,7	12,2
Cambodia	-5,4	-3,1	-5,0	-2,8	-1,2	-2,4	-3,6	-2,2	-4,2	-2,0	-2,8	-4,4
Indonesia	-1,6	2,7	3,7	4,8	4,3	4,0	3,5	0,6	0,1	2,7	1,6	1,2
Lao	-7,5	-13,0	-4,0	-10,6	-8,2	-7,2	-8,1	-14,3	-20,2	-13,3	-22,9	-21,1
Malaysia	-3,3	12,8	15,9	9,4	8,3	8,4	12,7	12,6	15,3	17,2	14,4	13,3
Myanmar	-10,7	1,5	-5,9	-0,8	-2,4	0,2	-1,0	2,4	3,7	7,2	6,9	4,8
Philippines	-3,4	0,5	-3,8	-2,9	-2,5	-0,5	0,4	1,9	2,0	4,3	3,8	2,6
Thailand	-4,0	3,4	10,2	7,6	4,4	3,7	3,4	1,7	-4,5	1,6	3,7	2,2
Timor-Leste	-	38,1	2,1	-60,2	-52,8	-37,2	-25,4	30,4	83,6	118,2	149,7	172,2
Vietnam	-7,0	-0,9	4,5	2,3	1,6	-1,9	-4,9	-3,4	-0,9	-0,3	-3,2	-3,2
Russia	1,1	9,8	12,6	18,0	11,1	8,4	8,2	10,1	11,1	9,7	5,9	3,3
Mongolia	0,1	-3,9	-5,8	-5,0	-6,6	-8,5	-6,8	1,5	1,3	7,0	2,1	-18,0

Source: IMF - World Economic Outlook (October 2007)

It's interesting to observe that even advanced Asian countries have revealed strong current account surpluses, which not only reveal the strong competitiveness of these economies in world trade but also their potential dependence on the evolution of world trade itself.

Insofar as the most significant balance within the current account balance is concerned, that is, the **trade balance**, immediately noteworthy is the preponderance of Eastern Asia countries in the context of global Asia trade. In 1995, East Asia share in the exports coming from Asia was 80.7 percent, a share that had been increasing in the last 10 years, to 83.1 percent observed in 2005. In that same period, the share of Eastern Asia countries exports in world exports, increased from 23.9 percent to 26.2 percent. Finally, the share of Asia exports also rose strongly, from 29.5 percent of the world exports in 1995 to 31.6 percent in 2005.



One last word on the increasing importance of China in the commercial front: between 1995 and 2005, China's export shares increased from 12 percent of the total Eastern Asia export's, to 28 percent! In less than 10 years it became the first Asian exporter and, according to recently data published, it could be now the first world exporter, replacing Germany's long-term leadership!

Finally, a quick look at imports indicated that, contrary to common belief, Asia, Eastern Asia, is not only an export region, close to the world trade when it came to buy in external markets. Some numbers are quite significant: As a

whole, Asia, represents roughly 28 percent of world imports (almost the same as in 1995) and, in 2005, 78.1 percent of their imports were made by Eastern Asia countries (against 76.7 percent in 1995).



However, it should be noted that a substantial share of the imports is based on intermediate goods (and not final goods), meaning that the endorsement of some Asian countries in imports is more related to its export efforts than to a true engagement in world trade. That is indeed one of the reasons why the share of regional trade flows in world merchandise exports is quite significant in Asia: 14.1 percent, compared with only 8.1 percent, for example, in North America.

Table 3 shows the **inflation evolution** over the last 20 years. In general, the disinflation process that has taken place in emerging markets and developing countries in the last ten years is remarkable: between 1999 and 2008, the average inflation will probably reach 6.2 percent, decreasing from 53.8 percent in the ten year average between 1989 and 1998.

Table 3: Financial and Economic Indicators – Consumer Prices

	Ten-Year Averages											
	1989-1998	1999-2008	1999	2000	2001	2002	2003	2004	2005	2006	2007 p	2008 p
Consumer prices (annual percent change)												
World	20,5	3,8	5,0	4,2	4,0	3,3	3,5	3,6	3,7	3,6	3,9	3,6
Advanced economies	3,5	2,0	1,4	2,2	2,1	1,5	1,8	2,0	2,3	2,3	2,1	2,0
Japan	1,5	-0,2	-0,3	-0,8	-0,7	-0,9	-0,3		-0,3	0,3		0,5
Korea	6,2	2,7	0,8	2,3	4,1	2,8	3,5	3,6	2,8	2,2	2,6	2,7
Singapore	2,2	0,9		1,3	1,0	-0,4	0,5	1,7	0,5	1,0	1,7	1,7
Taiwan	3,3	0,8	0,2	1,3		-0,2	-0,3	1,6	2,3	0,6	1,2	1,5
Other emerging market and developing countries	53,8	6,2	10,2	7,0	6,5	5,7	5,7	5,4	5,2	5,1	5,9	5,3
Brunei	-	0,5	-	1,2	0,6	-2,3	0,3	0,9	1,1	0,2	1,2	1,2
China	9,4	1,6	-1,4	0,4	0,7	-0,8	1,2	3,9	1,8	1,5	4,5	3,9
Cambodia	-	3,4	4,0	-0,8	0,2	3,3	1,2	3,8	5,9	4,7	6,5	5,5
Indonesia	12,2	9,7	20,7	3,8	11,5	11,8	6,8	6,1	10,5	13,1	6,3	6,2
Lao	18,3	22,0	128,4	23,2	7,8	12,1	15,5	10,5	7,2	6,8	4,0	4,5
Malaysia	3,7	2,1	2,7	1,6	1,4	1,8	1,1	1,4	3,0	3,6	2,1	2,4
Myanmar	28,3	23,1	10,9	-1,7	34,5	58,1	24,9	3,8	10,7	25,7	36,9	27,5
Philippines	10,1	5,0	6,4	4,0	6,8	2,9	3,5	6,0	7,6	6,2	3,0	4,0
Thailand	5,5	2,2	0,3	1,6	1,7	0,6	1,8	2,8	4,5	4,6	2,0	2,0
Timor-Leste	-	10,8	-	63,6	3,6	4,8	7,0	3,2	1,8	4,1	5,4	3,9
Vietnam	26,9	4,8	4,1	-1,6	-0,4	4,0	3,2	7,7	8,3	7,5	7,3	7,6
Russia	-	20,6	85,7	20,8	21,5	15,8	13,7	10,9	12,7	9,7	8,1	7,5
Mongolia	-	7,1	7,6	11,6	5,6	0,9	5,1	8,3	12,7	5,1	6,7	7,2

Source: IMF – World Economic Outlook (October 2007)

As previously mentioned in reference to GDP development, there are substantial differences in the path of the inflation across countries: once again, countries such as China, Thailand or Philippines are good examples of a well succeeded fight against inflation, but in Lao, Myanmar, Indonesia, Cambodia and even Vietnam, inflation continues to be a major problem and this is particularly dangerous because it is taking place during a time of global decrease of inflation.

Eastern Asia: challenges ahead

The strong dynamics of East Asian economies was made evident in the previous part of this essay. This demonstrates that these economies have learned their lesson with the financial crisis of the 1990s, namely, by trying to modernize production and to improve the financial system. In certain cases, they have even abandoned the peg dollar exchange rate system and adopted more flexible exchange rate regimes.

On the other hand, some countries have adopted the inflation targeting regimes, which have significantly strengthened the economy, since they have allowed monetary authorities to more closely control price evolution. Besides this development in the monetary policy, budget policy has become less “lascivious”, so as to ensure the control of public accounts, i.e., that public debt evolved positively.

Finally, the gradual improvement of international competitiveness of most East Asian economies has allowed for the continuing accumulation of reserves in foreign currency, later applied in the public debt markets of more advanced economies. This would ensure a reasonable capital return and make possible a more adequate evolution of their own local currencies⁷.

All this has contributed to an improvement of the region’s economies, which have become more resistant to eventual external crises. 2007 was an example of this: when the sub-prime crisis broke out in the US, European markets shook, but the Asian financial system in general, as well as its economies, continued strong.

Therefore, economic evolution in this area of the globe is very positive and, considering what is known thus far, East Asia will likely become the world’s major growth booster.

⁷ Once more, China is an example. Together with Japan, they are the countries which invest the most in the American public debt market.

However, it is important not to ignore the fact that there are risk factors, which may play a non-negligible role and condition the region's positive scenario.

In the short run, the main risk factor is related to the situation in international financial markets, especially in the US and Europe, vis-à-vis the signs that the credit crisis following the problems of the sub-prime market in the US is far from over. This concern takes on a new dimension as the possibility of an economic recession in the US becomes more and more probable, the side effects and consequences of which are still difficult to assess right now.

From a medium and long-term perspective, risk factors take on a different dimension. Although the challenges faced by Asian economies are vast, we feel they may be divided into four main areas: economic growth, capital flows, international trade and production patterns and social changes and greater inequality

We will now analyze each of these factors individually.

Economic growth models of Asian economies are based on the external sector, with the strong contribution of exports, which have significantly increased in the past decades. It is understandable that as the quota of exports on a world scale increases, it becomes increasingly more difficult to sustain the rates of export growth.

This predictable draining of the external sector requires that economic policies focus more on the need to improve internal demand, possibly by reinforcing their main component, i.e., private consumption.

Asia in general and the countries further east, in particular, still tend to be quite conservative as far as consumption is concerned. Even in Japan, an advanced economy and still the world's second economic power, private consumption does not represent more than 56% of the respective gross domestic product, which is as a rule lower than that seen in other advanced economies.⁸

If we add to this apparent "caution" of Asian families in relation to consumption the fact that, in many of the societies in question, there are profound imbalances in terms of income (with the exception of the four advanced economies in the region) which may lead us to the conclusion that the process of strengthening private consumption in these economies will be a slow and difficult process.

The second component of internal demand which might also serve to boost GDP is investment. Investment has recovered since the strong break

⁸ In the US private consumption represented 71% of the GDP in 2006, in the Euro areas it fell by 57%, remaining above the figures presented by Japan.

resulting from the Asian crises in the 1990s. However, with the exception of China, investment in East Asian countries has remained weaker than in other regions of the globe, lagging behind what economic premises seemed to suggest.⁹

Some economists¹⁰ believe that the weak investment in Asia is due to internal and external constraints. Internally, it could result from a change in investment patterns, previously directed at the manufacturing sector, and which are now shifting to the services sector with great focus on less capital intensive sectors. Another possibility could be the change in the production cycle meaning that the current technological cycle would be reaching its limit and that, in this context, companies and citizens waiting for technological developments might be holding back on investment decisions.

Other constraints on investment may also be expected from abroad, especially those related to the incredible attractiveness of China to international capital, which would serve as a factor of relocation of investments that would be directed to the other remaining eastern Asian countries.

Empirical studies do not fully reveal any of these hypotheses and as such, the reasons for the decrease of investment in Asia remain a mystery. However, the need for measures to help strengthen investment is undeniable, especially improvements that are required in terms of the legal framework and of companies (namely in as regards their management), organization of the financial system and macro-economic policies.

The second challenge is closely related to what has been mentioned about investment and has to do with capital flows.

The past years have witnessed a significant increase in speculative capital flows, also known as carry trades, which consists of looking for funds in markets with lower tax rates and applying them in markets which yield higher tax rates. Some Asian countries have relatively low interest rates (the most flagrant is Japan) and so they are frequently used by speculators as financing instruments for these activities.

Speculative movements have also reacted to the development of economic and business cycles: the disclosure of less favorable economic data in the US, the decrease of third quarter results pertaining to an important group

9 Even in Japan investment continues to face serious difficulties, recovering from the sharp slowdown and, in the last 12 years, the investment average growth rate was -0.1 percent!

10 David Burton, Director, Asia and Pacific Department International Monetary Fund, at the Singapore Press Club, Singapore, June 5, 2007.

of companies, consumption prices revealing inflation pressures - all of this is sufficient to bring about a massive reversion of carry trades.

As a consequence, the foreign exchange market has become highly volatile.

Besides international speculation, the globalization of financial markets – notwithstanding its inevitable advantages in terms of the diversity of sources of funding and greater risk coverage – has led an increase in the volatility of foreign exchange flows and, as a consequence, in foreign exchange rates.

In conclusion, today eastern Asia countries are faced with the need to monitor these movements, which potentially place pressure on their own currencies. For example, the sudden “arrival” of foreign capital creates the conditions for speculative bubbles in debts or stock markets. On the other hand, the outflow of this capital is normally reflected in heavy losses in terms of the local currency value.

The solution for these distortions is complex. If it could be argued that the imposition of limits to capital flows, albeit temporary, could dissuade speculative movements, it is also true that these types of obstacles to the normal market functioning may, as a rule, discourage direct foreign investment, basically due to investors’ apprehensiveness in relation to economic and financial objectives imposed by countries.

The third challenge is related to the need for Asia to change its production and exportation patterns. Eastern Asia is a complex production system, the centre of which is occupied by China, the great factory of the region, producing final goods that are exported to the rest of the world. As a consequence, the production of other economies in the region has increased the added value chain.

However, the situation in China has been changing progressively with evident use of intermediate goods that are manufactured internally, contrary to what happened in the past. On the one hand, this phenomenon reflects the growing productivity and technological capacity of China while on the other, it penalizes the remaining economies in the region. Within this scope, it is important to note that China’s trade surplus in relation to the US and the EU is on the increase while in the past years its trade deficit vis-à-vis other Asian countries has decreased.

These developments in China represent additional challenges for the other eastern Asian countries and to some extent, they may jeopardize the

regional economic integration of the last decades¹¹, redirecting some countries to foreign markets in other continents.

Finally, the distribution of income in East Asia remains very high, even when the region is compared to some of the areas where these imbalances are the highest in the world¹².

Although this problem may be typical for countries that are shifting into new phases of the production cycle, namely when industrialization overtakes agriculture, and later on when tertiarization substitutes the capital-intensive industries, the growing inequality is a problem for East Asia, as it may place in jeopardy social cohesion and interrupt the region's integration process in the midst of the advanced economies.

The solution for problems of inequality has been profusely analyzed by economic theory (and other areas of social sciences) and in general, it seems to be unanimous in terms of all the changes that have occurred in educational systems, in the social security system (especially regarding support to the elderly and most needy), in job creation in rural areas, and in the integrated development of urban areas, among others.

Economic theory also teaches us that development at this level is not always easy. This, unfortunately, is due to the fact that economic growth does not always go hand in hand with economic development.

China, the special one!

China naturally deserves special attention in the Eastern Asia countries especially because of its extraordinary economic growth during the last two decades that is unprecedented in any other country in the world.¹³ Moreover, China shows the ability to join two different economic systems, capitalism and socialism, in a single country. Finally, China is definitely the Asian country (or even the world country) that will face more challenges in the first decades of the 21st century.

We will try to analyse these challenges in the next paragraphs.

11 It should be noted that the weight of the intra-regional trade in Asia is today far greater than in the US.

12 Currently, the imbalance in the distribution of income in China is higher than in the US or Russia.

13 If the current average growth rates remain stable, the nominal GDP in China will reach European Union GDP in less than 10 years, and it will be necessary to wait a little more than 20 years to see China become the first world economy.

The first one is related to China's growth sustainability. In a country where most of the population continues to live near the poverty limit, it is almost mandatory that the GDP should continue to grow on average above 10 percent a year. However, the authorities have stressed the dangers of excessive growth, namely the increase of inflation verifiable in the past months.

The second challenge concerns the growth paths. The growth engine has been the external sector. Although China has been too dependent on its companies' ability to continue to export faster, independently of the fact that authorities indicate that they don't desire a long-term surplus but a healthy trade balance.

As we know, it is very difficult for an emerging economy to jump into the advanced economies group without developing internal demand. Although investment has grown rapidly, savings, especially in the corporate sector, have grown even faster. Therefore, China's needs are to reduce the rapid investment growth as well as net exports, and to encourage consumption, which has shown slower growth rates than expected.

The third challenge is a technological one.

China intends to implement science and technological projects in sectors such as energy, water resources, environment, biotechnologies, health care, new materials, space technologies, among others. At the same time, they intend to increase the country's expenditure on science and technology to account for 2.5 percent of the GDP by 2020.

According to data from 2004, China currently spends 1.2 percent of its GDP on research and technological innovation (compared to only 0.7 percent in 1997), the highest percentage among developing countries. However, this is very low when compared to the leading European economies, such as Germany, which spends 2.5 percent of its GDP on R&T innovation, and France, which spends 2.2 percent.

On the other hand, China has tried to acquire advanced technologies abroad, namely through joint ventures with multinationals within China or through mergers and acquisitions.

However, China's exports remain labour intensive and the country imports are mainly capital intensive. On the other hand, around 2/3 of Chinese exports are from foreign companies operating in China, and serious doubts subsist regarding the destination of their profits. Indeed, there are no strong signs that the profits have been allocated to research and technological development.

The fourth challenge is related to energy resources, energy policies and environment.

China's capacity to maintain a strong economic growth had been based on a gradual turn towards oil imports from the late 1970s, up to its current second position as the world's largest consumers (after the United States). However, coal continues to be the main energy resource. In 1990, coal represented around 76 percent of the energy consumed in China and, in 2005, the share was still 69 percent. There are obvious problems related to the use of coal as a major energy resource. Firstly, coal is one of the energies which represent the highest hazard risks to the environment. This problem is further aggravated in China because of coal flows from the North to the South, although water comes from the South to the North (not surprisingly, China has become the first source of SO₂ in 2007); secondly, there are problems in terms of energy security, namely with mining accidents that have killed thousands of Chinese in the past years; finally, China is consuming its coal reserves at a growing speed, more than any other country in the world.

In this context, the strategy that has been implemented does not seem to be the most accurate. In fact, in spite of the bet on clean energies, such as nuclear or wind energies, authorities have massively been trying to use clean coal and fuel. The latter is also the main issue for Chinese authorities when it comes to deciding on the patterns of the diplomatic and economic relations with African and Middle East countries.

The economy future of China, as well as its position among the world's nations, will largely depend on the answers to these challenges.

Conclusions

In less than ten years, Eastern Asia has been able to cross a major financial and economic crisis and become the main engine of world economic growth. Today, countries such as China, Singapore and Vietnam have the highest GDP growth rates, and they have amazingly increased their shares in world trade and foreign direct investment.

The future for almost all the countries in the region seems bright. However, in the next years they should be able to manage significant challenges, related not only to international environment and the globalization shifts and advances, but especially with their policies regarding economic growth, educational system and social cohesion, among others.

The challenges remain large and difficult, and the poorest Asian countries are not yet prepared to cross the way and correctly manage all the problems they face.

But if Eastern Asia intends to become the heart of world economy, it has no alternative but to face the challenges, modernize the economy and develop social infrastructures.

Otherwise, the main countries in the region may never be other than paper tigers and dragons.

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Part II. Main Actors

National Motives, Approaches and Goals of China's Foreign Policy

Carmen Amado Mendes

Introduction

Today's importance of the People's Republic of China as an international actor is unquestionable. Its emergence goes beyond the economic field. Besides its prominence in commercial terms, China has consolidated its military power and actively developed diplomatic relations both with Asian as well as African and Latin American countries, as well as strategic partnerships in Europe. Therefore, an analysis of Chinese foreign politics is of extreme importance, a strategy craftily implemented using *soft power* strategy and conditioned by strong national interests.

Soft power implies the ability to influence through persuasion rather than through coercion, i.e., using all activities which are not within the scope of security, whether it is humanitarian aid, culture, bilateral and multilateral diplomacy and economic investment (Kurlantzick, 2006: 1). Before signing those treaties China considers "unequal" (19th century), when the Middle Empire dominated Southeast Asia using a taxation system, it would resort to soft power: the ideals of Confucius and commerce functioning as attracting elements (Terril, 2005: 52). Noteworthy is the fact the hegemony of the

Middle Empire was not solely based on peace and that soft power was often complemented by military interventions (Godement, 2006: 51-52).

This historical argument may explain Chinese present tendency to dominate the region of Asia-Pacific no longer through Confucianism but through economic power, considering that an East Asian economic system is emerging with China as its center (Terril, 2005: 52 e Kurlantzick, 2006: 1). Commerce and economic integration are much safer ways for growth than military domination (Mahbubani, 2005: 49). China's commercial and financial influence guarantees the country some soft power. Its growing internal market, tourism, media and language are poles of attraction, especially in countries which identify with Asian values. In the case of China, soft power has a different connotation from that of European soft power: it means embracing civilization, education and culture, democratization of international relations and a harmonious international society based on Confucian values (Godement, 2006: 60).

This paper will focus on Chinese foreign policy and its actual trends, and will analyze China's policy for Asia. It argues that Chinese foreign policy is based on internal concerns: political stability, economic development and regional security. Finally, it will analyze China's use of soft power, either in isolation or combined with hard power, to meet those objectives.

Internal political stability

Chinese leaders have mostly resorted to nationalism to ensure internal political stability. There are two reasons for this: history – the refusal to accept subordination to powers responsible for past Chinese “humiliation” – and ideology – progressive reform from communism to nationalism, since communism has lost its “legitimacy” after the dissolution of the Soviet Union. Nationalism, whose origins lie in the treaties China considers “unequal” (19th century) and the occupations by foreign powers, leads to the need to recover from those humiliations, making it a priority in Chinese foreign policy (Zhao, 2005: 79). After a century of misfortune, also filled with internal convulsions and civil war (Mahbubani, 2005: 51), China's emergence poses a dilemma: whether it should attempt to recover imperial supremacy in Asia or join the international community (Terril, 2005: 52). This dilemma is visible in many of China's foreign policy, which moves forward in both directions.

Ideology, as instigator of nationalism, has been used by the Chinese Communist Party (CCP) as an element of national union and as means to ensure it remains in power and preventing possible protest against a regime not sanctioned by elections (Terril, 2005: 54). Therefore, part of Chinese assertiveness in the international scene is motivated by insecurity about its authoritarian regime (Friedberg, 2007). As such, nationalism may be seen as a stabilizing factor internally and externally, since it fosters moderate behavior by Chinese leaders in order to attain a power status in the international scene (Shen, 2007).

Thus, if we analyze China's bilateral relations with its neighboring countries and its involvement with multilateral military institutions in Asia, it is obvious that the country has tried to have the responsible-actor position, which has contributed to boost its national pride. In the 1980s, the adoption of a new foreign policy, "a policy of peace and independence", was simultaneous to the changes in relations with other Asian countries. As a consequence, China has no declared enemies (Terril, 2005: 56). This situation resulted from the normalization of China's relation with the Soviet Union and the control division of Central Asia, the relation with Indonesia and the recognition of South Korea, and the active participation in regional and international organizations (Terril, 2005: 56).

Chinese nationalism, however, has its less positive sides, such as its control policy over Tibet and Xinjiang (Terril, 2005: 52) and its attitude towards Taiwan. Taiwan has been subjected to both China's soft and hard power, through the growing reinforcement of Chinese military capabilities and its recurring threats to use force (Godement, 2006: 58). This increase in China's military power has affected Taiwan's foreign policy and contributed to the decline of the pro-independence Taiwanese movement (Ross, 2005: 81). Yet, recently Chinese policy towards Taiwan has been more constructive (Lampton, 2005: 80). Preferring soft power over hard power, China expects that the intense economic and commercial relation will bring them closer and avoid the use of force (Mahbubani, 2005: 56). Meanwhile, Taiwan's internal policy and the United States and Japan's position regarding this issue may develop in favor of PRC's interests; China expects to use these factors so as to attain a better military positioning and thus meet its objective (Terril, 2005: 58).

Despite Taiwan's apparent tolerance, if it decides on a unilateral declaration of independence, the CCP is left with at a dead end. If the Chinese leaders retaliate, the US may respond, if they don't, they may lose legitimacy both internally and externally and risk their own survival (Ross, 2005: 82, 85-86).

Whenever the independence movements in Taiwan gain visibility, Chinese leaders feel compelled to emphasize that if Taiwan declares its independence, China will militarily retaliate (Mahbubani, 2005: 56). In fact, this policy has been useful for China: on the one hand, it keeps the status quo, on the other, it legitimizes international acknowledgement of the “One-China principle”

Though Chinese foreign policy towards neighboring countries has been very pragmatic, that is not true as far as Taiwan and Japan are concerned. In this case, nationalism is also manipulated by the CCP as source of legitimacy to remain in power and leads not to pragmatism but to assertiveness in Chinese foreign policy: due to strong internal interests, China cannot show flexibility towards these two. For the Chinese leaders, Taiwan is an internal affair which should not become part of the international agenda (Wang, 2005: 46 e Gode-ment, 2006: 58).

As far as Japan is concerned, the bad Sino Japanese relations have fueled Chinese nationalism and united the population around the CCP. The Japanese leaders have avoided taking political stands on Taiwan publicly as these may worsen the already rocky Sino Japanese relations, even though they support the cause of Taiwan (Mahbubani, 2005: 57). Japanese openness to Taipei’s pro-independence movement, evident by the visit of the president of Japan, Lee Teng-hui, in December 2005, is one of the many distabling factors in the relations between the two countries (Wang, 2005: 44).

So far, the commercial relations between the two countries have not been affected (Pei e Swaine, 2005: 1), but they both fear the other’s military capabilities and are involved in territorial disputes (Zissis, 2006: 1). Despite their economic relations, Japan and China view each other as hostile, competing for political influence and economic interests in Asia, in an environment of uncertainty in terms of the strategic balance in East Asia (Pei e Swaine, 2005: 1). Political antagonism has increased due to a series of incidents, such as the visit of Japan’s Prime Minister Koizumi to the “Yasukuni Shrine”, where the criminals of war are buried who committed atrocities in China during the Second World War. There is a new version of history books in Japan which omit these atrocities (Zissis, 2006: 1). The Chinese leaders have made use of its historical conflicts with Japan to boost nationalism (Chung, 2005: 90). The demonstrations against the Japanese history books, for example, were tolerated (or even incentivated) by the Chinese government (Mahbubani, 2005: 57).

Besides these badly resolved history issues, Japan and China have been involved in territorial disputes on natural resource exploration in the East China Sea (Zissis, 2006: 1). Sino-Japanese relations have deteriorated due to

some incidents or political mishaps on both sides: in November 2004 a Chinese submarine entered Japanese territorial waters without permission (Wang, 2005: 44). Moreover, China has already expressed its intention to veto Japan as a member of the United Nations Security Council (Garten, 2005: 3). Japan, on the other hand, did not respond to the institutionalization of economic cooperation in East Asia as China expected (Wang, 2005: 44). So as to restrain China, though not in an explicit way (Chung, 2005: 90), Japan has reinforced its cooperation with the United States, becoming their main ally against China (Ross, 2005: 82).

Economic growth

In our analysis of nationalism as a conditioning factor in Chinese foreign policy, we realized that internal political stability is a major concern of the Chinese government. The other priority is continuing economic growth, which, internally, has served as a source of legitimacy for the CCP, both because the population's standard of living has substantially improved and because it is a source of national pride and thus feeds nationalism (Terril, 2005: 54). Externally, this growth is the basis for the emergence of China as an international great power (Zhao, 2005: 82).

Therefore, the second type of internal motivation of China's foreign policy is realistic. As Friedrich Ratzel suggested (see *Leis do Crescimento Espacial dos Estados*, 1895), the state's "appetite" increases according to its power and its need for resources (Friedberg, 2007) justifies attempting to expand "vital space". As such, Chinese economic growth increased its "appetite" for influence and control and led to the desperate search for resources. One of China's greatest internal challenges is precisely the fact that its natural resources are insufficient (Zheng, 2005: 21). As a consequence, one of the objectives of Chinese foreign policy is to recover territories Peking claims already belong to China. Taiwan and several other islands rich in natural resources, in the Yellow Sea, in the South China Sea and in the East China Sea (Terril, 2005: 58) are not only valuable in themselves but also represent additional territorial waters.

However, the desire to ensure continuing growth will not necessarily result in *realpolitik* but may rather lead to an essentially defensive foreign policy. This perspective views China as recovering from being economically behind and having a weak position regarding the United States, as a member of several international organizations just to keep their agendas far away from its interests

(Terril, 2005: 51). Therefore, after many years of negotiations on the South China Sea disputes, a “Declaration on the Conduct of Parties” (Godement, 2006: 60) was issued in 2002.

Besides political stability and economic growth, China’s foreign policy is also influenced by feelings of vulnerability and insecurity. On the one hand, Chinese leaders feel strong because of the country’s economic growth, on the other, they feel vulnerable due to the risk of Taiwan unilaterally declaring its independence. There is a third motivation behind China’s foreign policy, though: security at a regional level, as means of not placing the other two priorities in danger. Without border security, China will experience difficulties in keeping its levels of economic growth, which have functioned as guarantee of political stability. These secondary internal motivations have led to great pragmatism in China’s relations with its neighboring countries, namely, with India and Russia (Mahbubani, 2005: 55).

Regional security

With the rapid growth of its economy, India has become more appealing, extending its relationship to several strategic partners, including China and the United States, and promoting some hegemonic ambitions (Wang 2005: 43 and Chung, 2005: 92). With the standardization of Sino-Indian relations, in the wake of decades of animosities, India and China intensified economic and commercial ties and established bilateral strategic and military dialogues (Atal, 2005: 104 and Godement, 2006: 64). As a nuclear, military and economic power, India plays a strategic role in regional equilibrium. From the North-American point of view, it helps to counteract Chinese expansion in South-East Asia and in the Indian Ocean (Chung, 2005: 92 and Godement, 2006: 69-70). However, India does not openly support contention measures against China (Godement, 2006: 69-70), although it is deeply drawn by Chinese economic development. From the Chinese point of view, India neutralizes the North American influence. Russia shares the point of view of the United States and China: it sees in India a form of stabilizing China’s power and of limiting the United States’ power in the region (Atal, 2005: 103).

In 2005, China and Russia granted India observer status in the Shanghai Cooperation Organization (SCO) in an attempt to prevent tight Indo-American ties from developing (Atal, 2005: 104). However, to make up for the possible creation of an Indo-Russian bloc that would place its own interests in

jeopardy, China also pressed for Pakistan to be given observer status. Besides playing in favor of maintaining regional equilibrium, the bringing in of India to the SCO also contributed to the efforts of China and Russia in the control against terrorists and on energy talks – it should be noted that India imports two-thirds of the oil it consumes (Atal, 2005: 103). Nonetheless, in the energy sector, China's negotiations with SCO countries have been bilateral, which has enabled the organization to remain ambiguous in its goals and results achieved (Godement, 2006: 67). Despite the economic, military and political cooperation between China and Russia, strategic competition persists.

According to Chinese leaders, "peace and development" are the key goals of its foreign policy. But are they not instead the means to reach other goals (Terril, 2005: 52)? China's true goals are unknown, as a result of the secrecy of the Chinese regime, but they clearly involve keeping the US at bay and preventing alliances between other Asian powers, namely Japan, India and Russia, in order to reach supremacy in East Asia and in continental areas (Friedberg, 2007). Several obstacles to Chinese expansionism have been raised: the collision of economic and cultural interdependency with political paternalism; the US, Japan, India, Russia and the other powers may not permit a new Middle Kingdom and China knows this (Terril, 2005: 52 e 61).

In a realistic approach, from a security point of view the goal of China's foreign policy is of supremacy in relation to Japan and India, and replacing the United States as the prime influence in Asia – what some authors call "Chinese Monroe Doctrine" in East Asia (Kurlantzick, 2006: 4 and Terril, 2005: 56). This goal, of subordinating the region's interests to China rather than to the US, seems to be reaching its end: the leaders of South-East Asia no longer question the emergence of China and give its elites the treatment previously reserved for the United States (Kurlantzick, 2006: 4). China has replaced the US as the main agent responsible for the economic growth and political stability of the region (Ross, 2005: 81).

All of the countries in South-East Asia recognize the "One China" policy and only Singapore maintains (unofficial) ties with Taiwan (Chung, 2005: 94). Burma and Laos have clearly entered China's sphere of influence and the same may happen to Thailand and Malaysia (Terril, 2005: 57). Vietnam and Indonesia have put aside their protracted differences and have strengthened economic relations (Chung, 2005: 89). In the case of Indonesia, these relations are fuelled by the abundant natural resources that are used to satisfy China's requests. The tightening of political ties between the two countries hinders Indonesia's cooperation with the United States and with Australia. In this

way, China is able to discretely counteract Australian and US influences in the region (Chung, 2005: 93).

The competition between China and other key partners in Asia extends to the United States, made worse by the ideological differences between the two countries, including issues on democracy (Friedberg, 2007). Chinese leaders criticize North American unilateralism and defend the “democratization of international relations”, despite the fact that in practice they attempt to implement the American model of power and influence (Godement, 2006: 56) and to pass the image that China is not on a lower standing than the United States in the hierarchy of international relations (Terril, 2005: 57).

The September 11 and the invasion of Iraq have numbed the United States’ concern with the rise of China (Mahbubani, 2005: 59). During a period of repose, the North American policy centered on economic cooperation, on the fight against terrorism and on stability in the Taiwan Strait. Currently, however, the unfavorable consequences of China’s economic and military growth for US safety are once again on the North American agenda (Ross, 2005: 81). Chinese leaders look down upon stepping up their military expenses, when compared to the military capacity and the hard power of the United States, and defend their strategy of soft power, based on the North American precedent (Godement, 2006: 56). They see the United States – a country able to exert strategic pressure on China – as a threat to the internal security and stability (Wang, 2005: 39). The US policy for Taiwan, for example, is viewed with great mistrust by China and all that is needed is a diplomatic slip for it to turn into a real threat to Sino-American relations (Mahbubani, 2005: 55).

The US have in fact been the power that has most pressured and destabilized China, leading it to seek forms of counterbalancing the North American power (Mahbubani, 2005: 49 e 57). An example of this destabilization is the manner in which they reinforced their main alliances in the Pacific, causing Japan, Australia and several ASEAN States to view China as a threat (Chung, 2005: 88). Sino-American cooperation is well accepted by China as it not only helps to ensure the aforementioned economic growth priority, but it is also beneficial to the United States (Wang, 2005: 39). In fact, for the United States it would be far better to prevent the deterioration of Sino-Japanese relations and to integrate China in the regional security structure, the best guarantee of regional and worldwide equilibrium (Lampton, 2005: 79). This would not prevent them from containing China’s soft power in situations where it is manipulated to satisfy the hard power goals that threaten US interests. For example, situations that place in jeopardy territorial integrity and the

democratization of countries in South-East Asia and that put in danger the regional support of the US in the event of conflict, namely the Taiwan Strait (Kurlantzick, 2006: 6).

China's cooperation in the "six party talks" for the denuclearization of North Korea is of crucial importance to the United States and has increased the strategic value of China. Besides continued strong tensions between Washington and Pyongyang (Wang, 2005: 45), China is the only country with persuasive power over North Korea, as the sole supplier of oil and provisions to this country (Chung, 2005: 91). In response to the request by the United States in March 2003, China cut supplies for a few days. The importance given by the United States to the North Korean issue and the manner in which they depend on China for its resolution has brought about a change in Sino-American relations, giving China bargaining power (Mahbubani 2005: 58).

China disagrees with pressure politics and sanctions against North Korea, stating that the best way to resolve the nuclear conflict is through persistent diplomacy and Inter-Korean economic ties (Chung, 2005: 91). The Chinese policy of obtaining peace by keeping the status quo does not correspond to the interests of the US, who clearly prefer the imposition of sanctions (Terril, 2005: 56). Despite its long-standing alliance with the United States, South Korea agrees with the Chinese position and has refused sanctions.

Convergence with China, which extends beyond purely economic field, has led South Korea to abstain from adopting positions that contradict the Chinese policy (Chung, 2005: 91). This convergence has also been seen on China's side, taking advantage of South Korea's differences with the United States in the "six party talks" (Friedberg, 2007). China is more interested in the unification of North and South Korea than Japan or the United States and South Korean leaders trust China's policy for North Korea more than that of the United States, thus weakening the alliance with this country (Chung, 2005: 92). Nevertheless, the nuclear issue of North Korea and the consequent arms race in North-East Asia is a source of common concern for Beijing, Tokyo and Seoul and could lead to a convergence of the three countries in the search for common solutions (Zissis, 2006: 1).

The non-interference position in the internal affairs of other States, applied in the negotiations with North Korea, has also benefited China in its relationship with countries afraid of international sanctions, such as in Africa and Latin America, and has led China to opt for multilateralism. In soft power diplomacy, if in Central Asia China participates in the SCO, in East Asia it has become a member of all of the organizations: Asia-Pacific Economic

Cooperation (APEC), Association of Southeast Asian Nations (ASEAN), ASEAN Regional Forum (ARF), Council for Security Cooperation in Asia-Pacific (CSCAP) (Godement, 2006: 64). On the other hand, most Asia-Pacific countries have tightened diplomatic and economic ties (Wang, 2005: 43). In short, also in South-East Asia one of China's primary goals has been to ensure peace, so as not to interfere with its economic growth (Kurlantzick, 2006: 4).

Conclusion

This article has looked at how China's internal priorities, namely political stability, economic growth and regional security, condition its external policy. It argues that nationalism, while a source of legitimacy of the PCC on an internal level, has served as a factor of internal political stability. At a regional level, it has contributed to the accountability of China, both in terms of its bilateral relations and in multilateral terms; on the other hand, it has worsened relations with Japan and the ongoing tension in the Taiwan Strait. The second priority, keeping up the pace of economic growth and the consequent need to access natural and energy resources, has brought a certain amount of pragmatism to China's relations with its neighbors, namely Russia and India. To ensure internal political stability and economic growth, China seeks a peaceful regional framework, a fact which is reflected in its demarches to guarantee regional security, giving rise to theses on its peaceful rise.

This pacifism may however be no more than a means to a very assertive end. Doubts remain as to China's options in the security area and their consequences to regional equilibrium. Many Asian countries strive to counteract the growth of the Chinese power with other strategic relations, albeit not an alliance against China (Godement, 2006: 70). In fact even those that are most suspicious of China's strategic ambitions have not openly drawn up a contention strategy (Chung, 2005: 94).

A series of factors, such as the political regime and the unexpected economic success, have brought about a change of paradigm in the manner in which the world sees China: from the paradigm of a weak, politically fragile China with a transition economy, there has been a shift to the paradigm of a strong China, of a rising and highly competitive power (Lampton, 2005: 73-74). As a result of some blunders by the United States, namely the delayed reaction to the Asian financial crisis and the obsession with the fight against post 11 September terrorism, and the growth of China's soft power, South-East Asia

currently views China as the greater regional power (Kurlantzick, 2006: 1). Asian societies, with the exception of Japan and Taiwan, have a more positive image of China than the United States (Shambaugh, 2005).

Economic development and a more sophisticated diplomacy have led to the generalized acceptance of the growing influence of China in the region (Chung, 2005: 94). The strategies of the neighboring Asian countries have been centered around commercial ties with China and the benefits of Chinese economic growth to the region (Chung, 2005: 88).

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China's Rise and the World Factor: Financial Risks and Virtues

Rui Pava

« Le Paradigme de la Chine »

« Le paradigme de la Chine tient en peu de mots : beaucoup d'espace, beaucoup de gens, beaucoup de temps. Elle est, à nul autre pays pareille. On peut ajouter à sa singularité : beaucoup d'agriculture, beaucoup de cohérence culturelle, beaucoup d'influence sur ses voisins et sur le monde».

Pierre Gentelle¹

1. Introduction

This essay aims at evidencing the main pillars of the Chinese economic (apparent ?) success, from the Chinese conceptual and pragmatic model of development to other sources of interest, but at the end of the day, stressing the role of the heart of the financial system, its (not so matured) banking system.

1 *Chine, peuples et civilisation*, (sous la direction de P. Gentelle), (2004), Paris, La Découverte, p.26.

In overseeing China's future status as one of the biggest countries in the world, I will try to clearly describe the virtues and the fragilities of this big, powerful and still unpredictable country.

Although the China Factor is usually the target of studies on China, my point of view reflects my almost daily observation of this country living in a different dimension, and therefore giving a special attention to the World Factor, not seeing it as the reverse but as the very same side of the coin.

Three main aspects will be explored:

- China as a country with a different dimension;
- The World Factor and its interaction and pressure over China;
- The Financial Sector, as the heart of China's development (and fragilities).

2. Global Structure is affecting China's future.

• International Scene and Its Constrains

The Financial Crisis² in the Globalization Context

- From sub-prime crisis to stock exchanges bubbles, and possible other shocks

The world was suddenly shaken last year by the Mortgage related financial crisis. In the UK a whole bank fell down, the Northern Rock. What was considered, at a first glance, as a controlled problem, has spread over the markets quicker and more deeply than expected. A more speculative mortgage market was created and at the same time the financial markets were experiencing the salt & pepper of the *ambiance* through structured and more complex financial instruments. More and more complex financial packages, through securitization processes, were setting great enthusiasm and producing higher and higher profits (and bonus). But what could be at first stance the market-driven way, following the intensive deregulation, instead, became a nightmare.

2 We should have a look at American politics: the United States of America (USA) elections in 2008 will be relatively important, but not much regarding China's "eco-financial" future social and foreign policy. The major points of friction are there and it's understandable that any American President will follow the "rules". If Barack Obama wins, what is getting closer to reality, will he be more or less assertive towards China? And how will the Iraq case be dealt with? Is Iran a future target? Iran, in a not new strategic move, got some more calm waters for a short period, but is a complicated and sensitive matter to deal with. Well, this is the rational. But in another way, what can be felt is that the eventual victory of Obama, after the victorious trip to Afghanistan, Middle East and Europe, will take to the world scene a new and dynamic pace. The American "National Interest" will be reshaped, and a new America will show its new face. In that case, Obama will have no time to waist. I will show that both future will a closer one.

Losses, up to the end of the first quarter of 2008, of around € 129 000 million originated by the credit mortgaged-related crisis, and over 34 000 employments cut in just nine months are, these days, the most visible present consequences.

The mortgage crisis spread to the so called *monolines*³ (the strong bond insurers) and is spreading around the world markets. It is very difficult to assess its real impact and harmful effects. And the Money Market Funds are also under intensive pressure because of the low interest rates.

Then, the hot point is that the sub-prime is not yet accurately quantified, with the analysts thinking that there are other wave(s) to come, and the banking institutions and brokerage companies are showing huge losses. Bets are thrown to the air, forecasting⁴ (in a soft way) that the crisis will be solved in 6, 8, more months, or even a few years.

Another fact to deserve our reflection, is the role played by the rating agencies, since analysts considered that they didn't take the right action when were coming to the markets riskier, more complex (and opaque) deals or financial products (in those very sophisticated packages). A relevant report, prepared by the Financial Stability Forum⁵, FSF, was disclosed in March, 2008, issuing recommendations on how to improve the global finance Scene. And a very relevant point was the recognition of the negative role of the rating agencies. "The report argued that one reason for the recent turmoil was a loss of investor confidence in the ratings of complex products"⁶. Then, calling for the rating agencies to introduce a new system giving different types of ratings to structured products. The first answer to the proposal came from Moody's, the largest rating agency, defending a different solution: the introduction of the "so-called 'volatility scores' and 'loss sensitivities' that indicate the level of uncertainty that surrounds the ratings of structured credits, and the impact of a small change in assumptions about collateral (say, mortgage loan defaults)"⁷. Later Moody's admitted that an external investigation proved that members of

3 *Monolines* are suffering the impact and not yet clean. Showing that the situation is still not clarified for the future, two biggest bond insurers, Ambac and MBIA were downgraded to AA (negative) by Standard & Poor's, being understood that Moody's will follow soon. Like says the *Financial Times*, in very hard words: "Without a triple A credit rating, there is no prospect of these bond insurers doing new business again".

4 It is understandable that there will be a less negative side to its consequences, if the media, (the greatest power of this century, for better or for worse) paints in softer colours what is already fixed in (hard) primary ones.

5 The FSF is a committee of central bankers and supervisors.

6 *Financial Times*, (2008), May, 14, 2008, p. 29.

7 *Financial Times*, (2008), May, 14, 2008, p. 29.

a key rating committee breached internal codes of conduct, incorrectly rating about “\$ 1 bn of complex debt securities” probably due to a computer error...

Globalization on its open and hard reality, the inter-penetration of markets and the complexity of the financial operations combined with ambitious objectives to attain, and huge bonus to gain, conducted the world, (our 21st Century), to a series of bubbles: the *dot.com*'s⁸ in 2001, the subprime crisis in 2007...and now another shock, which can be seen as the Commodities⁹ related bubble, since we saw the oil barrel reaching more than \$ 140, the gold \$ 1000 ounce, and the prices of other metals and grains increasing. Ups and downs will occur but the scenario is no longer a paradise. And the weaker and weaker USD, making imports more expensive, combined with interest rates cut to sustain the dimension of the disaster, is making investments in the USA less attractive.

The financial paradigm seems to have changed when we saw¹⁰ the U.S. Federal Reserve acting as a “lender as last resort”, providing liquidity to the fragile giant Bear Sterns, (with the JP Morgan’s “generous” offer¹¹ to buy it). The debate is open and will be for quite some time, (more regulation, who cares about what, who will control what, and so on).

Later on¹², after Northern Rock and bear sterns, came the next nightmare: the major set back was the announcement of the hard problems showed by the two government-sponsored enterprises, GSE's, Fannie Mae and Freddie Mac. Two mortgage companies forcing the U.S. government to provide support, a rescue plan to avoid major disasters, and forcing the Federal Reserve chairman to come to the markets, on July 15, delivering a tough warning, highlighting the “numerous difficulties” facing the U.S. Economy. Later on, July, 22nd, Secretary of State Henry Paulsen presented to the U.S. Senate a study prepared by the Statistics Department of the Congress, assuming the cost to the “help plan” could go up to € 15,7 thousand million, (over \$ 23 thousand million).

Since regulation already exists in a wide perspective, it seems reasonable that the next move, besides curative/healing measures, will be to qualify (to intensify is different) the supervision, being tough, but with the need to clarify and control

8 Blomberg quoting the Securities Industry and Financial Markets Association, referred 40 000 employments lost during the *dot.com* crisis, plus 90 000 during the following years.

9 Absence of confidence, specially coming from the *subprime* crisis, and the USD getting weaker and weaker, made investors jump out of the Stock Exchanges to the Commodities markets, understood as a good investment. At least for a while!

10 On March, 14, 2008.

11 Offer, later on, increased to be accepted as real.

12 *Financial Times and International Herald Tribune*, (2008), July, 15 and 16, different articles. Just a quick update, since there is a major issue, with future developments to follow. I couldn't avoid to refer it.

the products and sophisticated packages, avoiding “creative” but uncontrollable methods and ways, combining these actions using IT in a proper way.

The impact on the Chinese economy will be dealt with later in this essay.

The American Economy: concerns and world impact

In terms of the United States economy, there is a debate about the possibility of a recession or a slowdown, especially due to the financial side of *the subprime crisis* which is affecting not only the USA market and its population, but is spreading around Europe and Asia. We are now starting to see its impact on the world and local markets, which may affect not only local economies but also the living of millions of people¹³.

World Banking is showing deep problems and the figures for some big banks for the fourth quarter of 2007 is clearly an image of deep concern. UBS with \$ 11 400 million, Merrill Lynch with \$ 9 830 million and Citicorp with \$ 9 800 million were some of the major financial institutions affected by the *subprime* crisis. But the image can be really worse, under media figures:

Merril Lynch	\$ 24 400 million
Citicorp	\$ 22 200 million
UBS	\$ 18 400 million
Carlyle Group	\$ 16 600 million
Morgan Stanley	\$ 9 400 million
Bank of America	\$ 5 300 million
Société Générale	\$ 2 900 million

13 Updating: the USA under *medium-long term financial storm*, showed, (On June, the 6th, 2008) the biggest unemployment rate in 20 years, increasing in one month half a point to 5.5%. To show how important is this negative figure, the Stock Exchanges came down, so as the weak Dollar.

Financial crisis and Energy Needs; Energy Security Issue - Consequences and Contagious Effects

A word about the world's energy security¹⁴, more relevant issue in countries like China¹⁵ and India, which are affected by the increasing demand on energy. The fact that the needed additional energy, speaking about oil, comes from the Middle East, represents another vulnerability. Other issues will increase the associated risks: one from the rising demand which will put pressure on the oil prices¹⁶, (and pressure on other sources of energy¹⁷) and, the other, the concentration of the oil reserves in a few countries, mainly Russia and in the Middle East.

14 For a wider and deeper information please read the "*World Energy Outlook 2007*", International Energy Agency, (2007), Paris.

15 China imported around 50% of its total oil consumption, 80% from the Middle East and Africa, major suppliers Saudi Arabia and Angola, 16% share each, and Russia with 11% share, accordingly to the same source, "*World Energy Outlook 2007*", note 11, p.325. We will speak later of the main Chinese state-owned oil companies.

16 The speculative moves can (at least partially) explain the spiral of prices for markets as the commodities and in particular the crude oil. Latest moves: Days after an apparent smooth way down, we could see on June, the 6th, the biggest one-day increase in 25 years, \$ 11.33 to \$139, 12, explained as a contribute by "Wall Street banks (...) as they bought crude contracts to cover agreements they have sold to big energy consumers such as airlines and utilities, in the expectation of rising prices". (Quoting the *Financial Times*, (2008), 7-8, June, p.1). Morgan Stanley (Warning oil prices can grow to \$ 150 barrel by the 4th of July) and other analysts came out with projections throwing the target to \$ 150 or even \$ 200 level, (Goldman Sachs). The last word of warning came from the International Energy Agency, IEA, saying that "an investment totaling \$ 45 trillion might be needed over the next half-century to prevent energy shortages and greenhouse gas emissions from undermining global economic growth", (*The International Herald Tribune*, (2008), 7-8, June, p.1. The title: "\$45 trillion blueprint for energy revolution")! We will see that lately, in middle July when got the record over \$ 147 mark, suddenly came down to the 130's level, explained by wider American crude oil inventories.

17 Tim Bond from FT gave two ranges of figures for the future needs for what he called the "Twin shock of finance and resources facing global economy".

a) Regarding the financial markets "require a recapitalization of the banking system, with estimates ranging from \$ 300 bn to \$ 1.000 bn".

b) On energy, and "according to the International Energy Agency, the global energy sector alone needs a real \$ 22.000 bn over the next two decades to meet the anticipated rise in primary energy demand". The explanation for the energy shock is: "The energy sector is just one example of the more generalized supply problems afflicting the natural resources markets. Scarcity is endemic across most commodities markets, as existing capacity has struggled to meet a demand shock from the rapidly developing middle income countries".

Global Warming and the Environment¹⁸

It will be very important that the USA, and the main emerging countries, (when the pressure is becoming a hotter issue), implement *de facto* measures to reduce the greenhouse gas emissions and the World as a whole must be prepared to change the present patterns of economic growth. Global Protocols¹⁹ on the issue are to be respected and fulfilled. Europe and the developed countries must be in the front row.

China is having a very negative impact on the global warming scene, becoming a relevant contributor to global environmental problems, particularly green gas emissions. Researchers, (Maximilian Auffhamer – University of California and Richard Carson – University of UC San Diego), concluded that “Between 2000 and 2010, the increase in China’s emissions will be more than five times greater than all the reductions expected under the Kyoto Protocol”²⁰. They considered that the results of their study surpassed “the worst expectations”, since experts were considering a 2.5 to 5.5.% growth for those emissions but the real rate may be 11%, a different conclusion explained by the fact that before researchers were looking to the country as a whole, and these two researchers “gathered emissions data from each province of China”.

The search for alternative sources of energy is inevitable, and the radical change of our way of life is a global priority. Saving energy and living in different energy atmospheres, are both individual and global agendas we must adopt.

Although being a threat to global security, there are other topics to summarize:

Security in a Changing World

There was a change of paradigm since the *proxy wars* of the Cold War era, with the development of military technologies and the proliferation of different kinds of arms all over the world.

18 This is just a brief reference to the issue, since I will elaborate more on China at a later point in this essay.

19 Like the *Kyoto Protocol*. But there is a big (environmental) concern on the way the accountability of carbon credits is being made, and the case of Japan eventual purchase of credits – called assigned amount units - from Hungary and Russia is, for instance.

20 *Business Week*, (2008), March 24, p.62.

After the “9/11 incidents”, the USA, supported by allies, initiated the so called “war-on -terrorism” policy taking to the Iraq war and the Afghanistan campaign, two military actions producing some concerns and divergences²¹ among the countries participating in both events.

Some contention was negotiated between the main powers but it didn’t end the nuclear arms race, only eventually limited it. And other tension focuses are still active in different parts of the world: for example, Iran, India - Pakistan file, Middle East, and the African recent conflicts.

With the sophistication of military technology, let’s mention the latest intensive dialog²² between the USA and Russia on the Defense Missile System, with the intention from the USA to defend a shield to be implemented in two countries: the Czech Republic and Poland. The justification to make it “softer” for Russia is the threat coming from Iran, (or from an eventual Middle East uncertainty).

Another field where we can see some tension is in the competition for space control, since China and later the USA launched missiles with satellites as targets, showing an active race and close surveillance.

Finally, globalization is leading to other sources of violence and risks in the “world map” due to people mobility, (increasing globalized crime, human trafficking, drugs, and arms), and goods exchange, which threaten global security.

3. China’s Trends and Vulnerabilities

Now is the right time to have a traveling²³ approach, detailed and well documented analysis, to show a deep and dynamic view of China’s economy. Some figures will offer the means to understand the pace of Chinese evolution, helping to dissociate what is structural from the seasonable effects.

21 Specially on the dimension of participants and the timing of ending actions. But another delicate, sensitive concern was the veracity of military information provided by the USA to its allies.

22 A minor but positive perspective for NATO, and for the USA, is figured out by the presence of Putin in a 26 -member NATO Summit, in April, 2008, in Bucharest, followed by the Black Sea Sochi meeting between the Russian leader and the president of the US, the agenda including discussion matters as relevant as the U.S. Missile Defence System. The result, not so effective, will be written in a “strategic framework document”, a delicate legacy to the new leaders of both superpowers. The meeting in Bucharest, with the approval of the “Missile Defence”, hit a hot spot with NATO’s invitation to Croatia and Albania to become full members, while the accession of Georgia and Ukraine was postponed.

23 I mean *traveling* as a concept used in movie making. Although the first text was done during the final quarter of 2007, as there were updates possible for revisional periods for the final text. What explains the dynamic form of expressing the evolution of the Chinese economy, and all the data analysed.

First of all the most impressive indicator is that of Chinese growth evolution. We know that higher rates are easier to get if the stage of the economy is not so developed. But the speed of Chinese economic development is remarkable and paradoxically becoming a source of concern, since the main problem now is how to control it.

Looking at the latest figure and the forecasts (% change on year ago)²⁴,

Gross Domestic Product		
2007	2008	2008(Year)
11.2 (Q4) ²⁵	10.6 (Q1) ²⁶	9.6 ²⁷ (10.8/11.3) ²⁸
Industrial Production		
2007	2008	
17.4 (Dec)	15.4 (Jan and Feb) ²⁹	15.7 (April) ³⁰

And if we look at the trend in the past, seeing the following three periods, it was quite impressive:

- (2002-2007)³¹: 10.6% (Average annual increase)
- (1995-2005): 9% (Average annual increase in real GDP) - 5th place
- (1985-1995): 10.0% (Average annual increase in real GDP) - 1st place

24 *The Economist*, (2008), March 8th, p.101. An exception for the January and February Industrial Production (n. 12).

25 The Asian Development Bank explains: Brisk exports, strong investment and buoyant consumption will lift economic growth in the People’s Republic of China (PRC) to 11.2% this year, up from an earlier estimate of 10%(...). In ADB Site: “ADB Raises PRC Growth Forecast for 2007 and 2008.mht” (accessed on March, 22, 2008).

26 *The Economist*, (2008), 24, May, p.109.

27 *The Economist*, (2008), 24, May, p.109.

28 In December, 2007, growth forecasts for that year end and for 2008 were: “The State Information Centre forecast China’s GDP growth at 11.4 percent for the whole of this year and at 10.8 to 11.3 percent for 2008”. In http://news.xinhuanet.com/english/2007-12/05/content_7204886_1.htm.

29 From the Chinese Statistics Bureau. In Blomberg_com Asia_INDUSTRIAL_MARCH.mht (accessed on March 21, 2008).

30 *The Economist*, (2008), 24, May, p.109.

31 Taken from the speech of the Chinese Premier Wen Jiabao during the 11th National People’s Congress, pointing out that the Chinese economy has increased in five years by 65.5%, an average annual increase of 10.6%, becoming the world’s fourth largest economy, and reaching its gross domestic product of \$ 3 425 billion.

Finally the latest GDP Quarterly Figures³², (2008):

1 st Quarter	2 nd Quarter
10.6 %	10.1%

a) With its memorable growth rate, (and combining with other figures bellow), the economy is closer, if not yet, to overheating: Growth over 10% and industrial production over 15%;

b) China was expected to soon become 3rd in World economy³³, after the USA and Japan, taking Germany's present position.

c) Even if in some quarters we can see a slight decrease in industrial production, quoting Bloomberg, "Weaker output growth is unlikely to ease government concern that the world's fourth-largest economy risks overheating after inflation surged to the fastest pace in 11 years in February(2008)"³⁴.

d) The main Olympic Games Effect³⁵ on Chinese development, (site construction and employment) has already been mostly absorbed³⁶. The previously estimated USD 1 600 million budget was increased in October, 2007 to USD 2 000 million³⁷, a figure presented on the sidelines of the 17th National Congress of the Communist Party. As far as Beijing itself is concerned, regarding the global ambient, the practices followed will perhaps only be felt for a short period and there is the risk that the next wave of economic activity (construction work) or normal life (traffic for example) following the Games will bring to the surface the same big threats we saw before. And if we think about the dimension of Chinese economy, it is easy to understand that the amount involved is not significant. Above all, this event is important for China to reshape the national image to the outside world.

32 Chinese Natuinal Bureau of Statistics, NBS. In order to introduce some more relevant data, relevant to understand the present pace, I just updated some figures for the second quarter 2008, manly for two variables: for the Chinese growth rate and for its inflation.

33 We shall see these rankings counter valued by the present debate on the World Bank new figures. Remember that the World Bank calculating it under the price purchase parity, undervalue it for about 40%.

34 Bloomberg_com Asia_INDUSTRIAL_MARCH.mht (accessed on March 21, 2008).

35 I investigated this topic on other occasion, for a Sinology Conference in Lisbon, regarding the "Economic and Financial Impact of the 2008 Beijing Olympic Games" in January, in a session presided by Prof. Pierre Gentelle. There are other consequences: a financial expert, Roger Nightingale, told *Bloomberg* that the Beijing Olympics will "promote the interest in Chinese funds". Please see note 88.

36 "The economic and financial impact of the 2008 Beijing Games", Rui Paiva, conference presented in January in the III Sinology Conference, Lisbon.

37 Considered by the Chinese officials as still below the USD 2 400 million for the 2004 Olympic Games, in Athens.

e) The debate on the perspectives for 2008: In February, 2008, while the Chinese government was forecasting 10.8% for 2008, the International Monetary Fund presented 10% and the World Bank 9.6%. For *The Economist* will be 9.6%. The snowstorm that affected the daily life of tens of millions of people, the collective effort from the government (sending military men to the worst storm sites) and population, could soften the effects. More than this, the strong storm, which was pressing the prices, should have the effects of a real American recession, with its global interrelationships all over the world. The latest natural disasters, like the snowstorm, which coincided in time with the Chinese New year, the Sichuan's earthquake on May, 12, and the former floods, aggravated the situation. Specialists were generally considering not much impact on growth levels;

f) A field where it is relevant to follow the growth is the commodities one. It's interesting to refer the record China got by becoming the top gold producer³⁸.

g) Finally, speaking about the latest data, let's refer that although there is a global slowdown, the Chinese growth rate shows that the economy is expanding well, at over 10% a year, and we can see that the growth rate is coming down a bit, what is explained by weaker exports (weaker export markets) and in the financial side by restrictions on (banking) lending.

Note: A final remark, following my professional experience in Asia in my first stay in Macao, between 1979 and 1982, when I have been for about one year head of the Economic Services, I stress that in Asia there was a real interest in improving practices, and, although there were no accurate statistics³⁹ at all, there was an impressive *will* to develop new concepts and new legal frameworks. All over the Asian countries there was the fight for productivity, through the Asian Productivity Organization, APO, and although the very bad means of communication means at the time, we used to participate in conferences, to exchange experiences, and I remember another issue: a Conference in Hong Kong about the simplification of the documentation, a real war on bureaucracy.

Finally, in Macao besides restructuring the Economic Services, I prepared with the Secretary for Economics and Finance, a brand new Trade Law, effec-

38 *Financial Times*, (2007), January 4, p.5.

39 Trade with China was really not controlled by the Macao official services; we used to receive a statement prepared by the gigantic Nam Kwong, (Chinese official enterprise centralizing the external trade), with the description of goods imported. I remind that the Portuguese – Chinese relations came just a few years before.

tive Jan., 1st, 1981, which has been active up to the hand over, not very far in concept, (considered the proper dimensions), from the Chinese one effective July, 1st, 1994).

In order to understand growth, let us refer its two most important contributors:

- The Trading Engine (Export growth)
- The Investment side

China became in August 2007 the world biggest exporter, up to € 78 540 million, against € 50 754 (2006). Germany the previous front runner got this time a smaller figure: € 74 582, and its trade balance has been jumping: August, 2007, has shown a remarkable growth, \$ 244 800 million (from \$238 700 in July), and 259 800 million in November, and \$265 200 in December 2007. The latest known is the February (2008) one, slightly lower, \$ 250 000 million.

Although this surplus would usually be assessed using the exports side, a UBS study analyzing imports said: “China’s trade surplus is only loosely related to unstoppable structural phenomena like productivity and a cheap currency. The key driver of China’s surpluses has been the relative weakness of imports since 2004, due to the displacement effect of the strong rise in domestic industrial capacity”⁴⁰. Right, but the engine of export growth is not neglectful either.

Besides the trade balance, in 2006 the current account balance represented over 10% of the GDP, (\$249 900 million)⁴¹.

Being a tough partner, with its greater surpluses, China simultaneously becomes a global problem to its trade partners, as the concern expressed by the World Bank⁴² when it declares “(...) the main macroeconomic task remains containing the rising trade surplus” which “is causing trade tensions internationally” and “domestically it is the key driver of the large balance of payments surpluses that buoy liquid, keep monetary conditions loose, and contribute to asset price pressures”. Again the inflation⁴³ effect.

Investment is the second main factor generating growth. First of all, let us analyze the different components of total capital formation: fixed capital

40 UBS Investment Research, (2007), Economic Insights, November, 12, 2007, p.10. This was an argument related to the RMB discussion, regarding its eventual revaluation.

41 *The Economist*, (2008), March 15th, p.118.

42 Quarterly Update, World Bank Office, Beijing, September 2007, p. 10.

43 Inflation is affecting much more the emergent countries since the the foodstuff part is the major contributor to their price indexes.

formation and the inventory accumulation. The first one, the most important for economic growth, (infrastructures, factories, real estate), was over 40% of GDP in 2005. In the early 90’s inventory accumulation was about 10%, it has been stable since 2000, and is almost irrelevant.

Another component of investment is foreign investment. It is a very relevant fuel for the economy, considering that in 30 years, “foreign-funded enterprises have invested a total of 2.11 trillion US dollars in China as of the end of the year, up 23.5 percent year-on-year”, according to the State Administration For Industry and Commerce, (SAFIC). The cumulative total dates back to 1978, when China began its reform and opening-up policies”⁴⁴.

So, 286,200 foreign-funded companies were approved to invest in China during that period, 37,888 in 2007, (down 8.68 percent from 2006), looking for a more competitive market since there were tax reforms (a “new corporate income tax law that took effect on January 1 unified the income tax rate for domestic and foreign companies at 25%, when before the effective rate was 25 % for the Chinese companies and 15% for foreign ones”).

It is relevant to point out that the “strong investment demand (capital)” was a significant drive of China’s economic growth, increasing in 2004 up to the high level (investment rate) of 44%⁴⁵ and that China’s Economy has two other important contributors to the growth:

China finances its domestic investment through the Chinese domestic savings, and it’s not dependent on the Foreign Direct Investment, FDI⁴⁶, although its impact is positive for its (quality of) growth.

A study by Jonathan Anderson⁴⁷, working for UBS, calculated savings up to 50% of the GDP, explaining the increase of savings through the reduced social system, comparing with Japan (30%), Hong Kong (39%) and USA (less than 14%).

44 www.chinadaily.com.cn/china/2008-03/12/content_6542967.htm (accessed on March 17, 2008).

45 Li Yang, Robert Lawrence Kuhn, (2007), *China’s Banking and Financial Markets*, Singapore, John Wiley & Sons, p.5.

46 One note about the sign given by the E, when we update the FDI from the EU to the BRIC countries in 2007. A few comments about these figures obtained from the *Eurostats*:

- a) A significant drop of FDI from UE into China (excluding Hong Kong SAR) from € 6 000 million in 2006 to € 1 800 million, when the EU out flows increased 53% up to € 430 000 million;
- b) Other (BRIC) emerging economies got much more FDI from the EU:
Brazil: € 7 100 million / Russia: € 17 100 million / India: € 10 900 million / **China: € 1 800 million.**

The leading receivers (in thousand million Euro) were the USA and Canada with € 113 and € 79, respectively.

47 *Diário de Negócios*, (2007), January 4, p.9.

As mentioned before, exports and savings are giving huge financial resources to the Chinese Government.

One parenthesis to show a different approach, to add the Country Risk, another accurate way to evaluate, through independent bodies, the consistency of the overall status. Just see how Moody's is rating China and the main assertions:

Moody's Investors Service:	
Category	Moody's Rating
• Outlook	Stable
• Country Ceiling: Fgn Currency Debt	A1/P-1
• Country Ceiling: Fgn Bank Deposits	A1/P-1
Gov. of China	
• Outlook	Stable
• Government Bonds	A1

Quoting its *Global Credit Research, October, 25, 2007*: "The government's foreign currency bond rating was raised from A2 to A1, in late July 2007, at which time Moody's assigned a government long-term local currency bond rating of A1. The upgrade was prompted by the exceptional strength of China's external payment position, continued success in reform and favorable fiscal trends. Financial sector reform has improved the intrinsic strength and supervision of the banking system – which reduces contingent liabilities to the government. China's external success has been accompanied by rising trade friction with the US and the EU. The US-China Strategic Economic Dialog is however, attempting to resolve trade disputes and forestall protectionist measures from the US Congress".

A good overall evaluation, denoting a clear improvement, but with some issues to correct.

Thinking about development and intensive growth, we can ask how employment is created, how environment is preserved (or affected), and (related to this point) China's needs and real management of its Energy file.

With an active population of 740 million⁴⁸, (2000 census), the unemployment rate in 2007⁴⁹ was 9.5%. But if we analyze Chinese Statistics, they indicate just around 4% urban unemployment.

Looking at its employment structure⁵⁰, Agriculture stands for 49% of employees, Industry

22%, and Services 29%. It is interesting how it has evolved since 1978, when the situation was very different, namely, the primary sector represented 70% of employees, the secondary, 18% and the tertiary sector 12%.

Now look at the origins of GDP⁵¹: Agriculture 13%, Industry 48% (manufacturing 34%) and Services 40%.

Energy: in 2005⁵² China was the second biggest producer (1,536.8) of energy and second largest consumer 81,609.3 million tons oil equivalent.

In the same year, it was the 6th top producer of oil (3,627,000 barrels a day) but the 2nd top consumer (6,988,000 b/d), holding the same position in terms of coal production, 1107.7, and consumption, 1081,9 million tons.

As far as China's environmental issues are concerned, they are really disappointing. Air pollution, land contamination, infected water are three major issues, which require different attitudes from the population and quick and tough measures from the government.

Environmental problems derive from the almost chaotic use of energy, such the repeated use of coal⁵³ (80% of electric energy comes from coal)⁵⁴. The huge consumption of coal is due to its inefficient use, producing very high levels of pollution. The media shows that almost everyday coal centrals⁵⁵ are being opened. On other hand, the international media reported that during the January 2008 snowstorm, and the severe constraints due to the weather conditions, some coal centrals, which had been closed because of their lack of conditions

48 For a total Chinese population of 1 313 000 in 2005, (and 1 388 600 in 2015), represents around 6 514 800/ 7 295 100. Human Development Report 2007 – 2008, p.p.246. Chinese population represents 20% of the world population (in 2015 will be around 19%). The urban population is 40.4% and will be in 2015 bigger: 49.2%.

49 *The Economist*, (2008), March 8th; p.101.

50 *The Economist*, World in Figures 2008, (2007), London, p.130.

51 *The Economist*, World in Figures 2008, (2007), London, p.130.

52 *The Economist*, World in Figures 2008, (2007), London.

53 Coal is getting more competitive because of the rising prices for oil and gas. It is impressive to see that China and India use 45% of all coal used all over the world.

54 70% for Elizabeth C. Economy. See next note.

55 90% of the Chinese coal resources are in inland provinces. In "World Energy Outlook 2007", International Energy Agency, (2007), Paris.

or environmental reasons, became active again, polluting the atmosphere and aggravating diseases.

To understand the problem's dimension, confirmed by recent pictures from Beijing, Elizabeth Economy stresses that China is "home to 16 of the world's 20 most polluted cities"⁵⁶.

The Asian Development Bank expressed some concerns on the big problems coming from the inefficient use of energy:

"Further steps to cool the rapid investment expansion are likely and the Government will put more emphasis on improving energy efficiency and on cutting pollution. But top priorities remain the creation of jobs for nearly 8 million rural surplus workers migrating to cities each year and on lifting income growth in lagging regions and areas," says the report"⁵⁷. Energy alternatives are relevant, like those using the natural means, like wind, water and sun.

"Measuring the global carbon footprint" HDR, (2007/2008), one can see that the *Mt Co2 emissions* have increased from 2,399 to 5,007 between 1990 and 2004, and in the USA from 4,818 to 6,046, with the respective growth rates of 109% and 25%. This is the reason why China is considered relevant in this (negative) competition.

Another concern is the "water stress and water insecurity" due to the low quality of the water in China, which is contaminated by industrial products. The water from Northern China poses another risk due to the "immense vulnerabilities associated with the retreat of glaciers – at a rate of 10-15 meters a year in the Himalayas"⁵⁸.

However, it is relevant to refer the impact of the environmental price – costs – paid by China:

1. The World Bank considered the "price tag for China's air and water pollution at \$ 100 bn a year, or about 5.8% of GDP"⁵⁹.
2. The OECD stated that: "(...) air pollution alone reduces the country's output by between 3% and 7% a year, mainly because of respiratory ailments that keep workers at home"⁶⁰.

56 Elizabeth C. Economy, "The Great Leap Backward", *Foreign Affairs*, (2007) September-October 2007, p.40.

57 ADB's Site: "ADB Raises PRC Growth Forecast for 2007 and 2008.mht" (accessed on March, 22, 2008).

58 Human Development Report, (2007), Summary, 2007/2008, p.18.

59 *The Economist*, (2008), 15, March, p.14.

60 Quoting *The Economist*, (2008), 15, March, p.14.

3. The State Environmental Protection Administration, SEPA, estimates⁶¹ the annual cost of environmental damage at 8-13% of DGP.

One final remark on its impact on social unrest: in the same issue of *The Economist*, one could read that “(...) the environment is the second most frequent subject of public protests after disputes over land”⁶².

Before analyzing the major asymmetries underlying Chinese potential economic success, we should refer to another concern: Chinese pressure on prices. The inflation rate is increasing fast, and it is a major concern.

Inflation Rate					
2008 ⁶³			2008		
January	February	March	April	Year (1)	Year(2) ⁶⁴
7.1% (2.2% year ago)	9.2%	8.3	8.5 ⁶⁵	4.0	4.8% (5.9%) ⁶⁶

a) First there is the quite negative social impact, since high inflation is influencing the Chinese population quality of life, and it is a major potential cause of social unrest, considering the low GDP pc;

b) Its an important factor affecting competition⁶⁷. Before, China was “exporting low inflation”, and this trend can alter the results, forcing China to increase export prices, (the same for the *re-exports* – goods imported to be industrially transformation).

61 *The Economist*, (2008), 15, March, p.14.

62 *The Economist*, (2008), 15, March, p.14.

63 All information from: *The Economist*, (2008), March 8th; p.101 for March data, and for April from *The Economist*, (2008), 24, May, p.109.

64 Being the agricultural products prices the main influence to this inflationary process, Wen Jiabao showed his determination to keep “inflation “around 4.8 per cent” and to constrain the implication for “low-income urban groups”.

65 “(...) Food costs rose 22.1% in April from a year earlier, driven by demand for pork. However fresh food prices dipped. High inflation increases worries that China’s economy may be overheating. “Greater prominence needs to be given to curbing inflation and controlling price rises,” said the country’s National Bureau of Statistics”. And, However, despite the government declaring it wants to tighten monetary policy in the battle against inflation, the authorities have not yet increased interest rates in 2008. There were six interest rises in 2007. Instead, banks have been told to increase the amount of money they hold in reserve and curb lending to limit credit growth”, in <http://www.iht.com/articles/ap/2008/04/11/business/AS-FIN-China-Foreign-Reserves.php>

66 *The Economist*, (2008), 24, May, p.109.

67 In global competitiveness China was the 15th overall, 8th government and 28th infrastructure. In *The Economist*, World in Figures 2008, (2007), London.

c) Besides the above points, although it is known that there is government control over some essential products (the government freezes prices⁶⁸), these rates can be explained by the increasing prices of food products, such as pork meat. Inflation is more and more concerning the government (s)⁶⁹. See other measures next d).

d) The Chinese Government came with “mixed news on inflation”:

- *consumer price inflation*, between May and June, declining from 7.7% to 7.1% a month;
- *factory gate inflation* rising from 8.2% to 8.8%.

The ways the authorities are using to tackle the inflation were⁷⁰:

- accelerating the rate of currency appreciation;
- placing stricter quotas on new bank lending, (but not increasing the interest rates).

e) Finally, although explained in other part of this essay, the expressive level the price of the crude was attaining during the second quarter 2008, rising above the \$ 147 in middle July, a barrel figure, (seeming to run to the \$150 level, but during June coming down), was pressing the prices in different sectors of activity. In one way, China as a giant consumer is enlarging the global demand and pressing the oil prices. On the other hand China is feeling the pressure. An interesting debate is getting more visibility and being more accurate in Asia: about the eventual end of subsidies for oil prices. Countries like Malaysia, Indonesia, Taiwan and Sri Lanka are studying⁷¹ how to cut this subsidies. In a worst forecast, the \$ 200 a barrel price is not impossible to occur up to the end of the year. Speculation⁷², weak American currency, increasing pressure on the

68 Some are politically more sensitive, such as foodstuffs and fuel. Consumer goods can have a big impact on domestic expenditure.

69 When looking at the government policies, in a different level of analysis, another debate is “warming up”: Joseph E. Stiglitz explains the sensitive effects of the inflationary phenomenon, making social unrest to be closer, but considering that the inflation targets as monetary measures were getting wild results. For him these targets must be abandoned. Please read “El Fracasso de las metas de inflación”, in *El País*, (2008), 25, May, 2008.

70 *Financial Times*, (2008), 18, July, p.3. The same newspaper, (same date), was saying that the IMF “singled out inflation as key threat”, considering that the emerging economies should fight inflation as their “top priority”, and advancing for 2008 for those countries, an inflation rate of 9.1% and 7.4% for 2009.

71 Sensitive intention, since the question will be how can the governments manage the issue accordingly to the opular pressure in order to to maintain it.

72 Paul Krugman, considered, (in synthesis), that there is no speculation, since there is no oil crude “fiscal accumulation” (See *El País*, June, 8, 2008, p.24 “Negocios”).

general demand and some constraints on the supply⁷³ side are just some of the explanations for this global red alert.

A quick parenthesis to say that the crude oil pressure on prices, or the so-called “speculation”, can assume several shapes or explanations, being some:

1. Geopolitical features: Iran, Middle East, pressure coming from “Emerging Countries”;
2. Demand and Supply effects: For instance, the increasing Demand from the emergent countries, (like from China and India), and from the USA⁷⁴, or controlled Supply by production countries, (as OPEC members, or other countries);
3. Market operations with derivatives: like the crude oil futures’ deals;
4. Bio - fuel, (considered by the World Bank as one of the major pressures on the foodstuffs increasing prices;
5. Mixed effects: an example, when combining with the increase of several commodity prices, speaking about, for example, foodstuffs / cereals, (soyabean increased 50% in 2008), also considering besides bio-fuel effect, (some specialists attributed the prices’ increases to this alternative energy), or the natural disasters or bad weather effects, (floodings, earthquakes, snowstorms).
6. Finally, a simple explanation, the sinking dollar: a study by the Fed “said that about a third of the rise in the price of oil from 200 and 2007 was caused by the falling dollar”⁷⁵.

After looking at some major problems affecting the Chinese population and how growth can be assessed, we can now define real and visible asymmetries.

Some social asymmetries have to be solved because they evidence the lack of quality of life of the Chinese population. If they remain unsolved, they can lead to social unrest in the near future.

The first of these asymmetries is the (contradiction) urban-rural dichotomy.

73 The USA through president Bush in a recent visit to the Middle East strongly pressed Saudi Arabia to increase oil production. Iran is supposed to increase too.

74 National Commission on Energy Policy: 70% of the USA daily consuming, (21 million barrels), is used for transportation!

75 *The International Herald Tribune*, (2008), James Saft from London, July, 18, p. 14.

A. China's Gini Coefficient⁷⁶

a) First let us look at China's Gini coefficient⁷⁷: for the Chinese government, (through China Economic Net, dated 2005, September, 13), it had hit 0.465 in 2004, and should reach 0.47 in 2005.

b) UNDP - Interesting that the quoted text defended that this coefficient couldn't be used⁷⁸ for the Chinese Economy, since it "is a typical country based on dual economy".

- Another Source on December, 17, 2005 the UNPD⁷⁹ stated that:

"(...) "China's Gini Coefficient now exceeds 0.4 and could be as high as 0.45, the threshold considered by many to indicate potential social unrest,"

And, "(...) Chinese income inequality is now markedly higher than that of the avowedly capitalist US, according to UNDP data. While the number of people judged to be living in abject poverty has been cut dramatically, the richest 10 per cent of the population enjoyed 41 per cent of China's wealth, the report quotes a 2002 Chinese household survey as showing."

c) The Asian Development Bank ⁸⁰, on 8 August, 2007 declares - "(...) China's Gini coefficient is estimated to rise from 40.7 (0.407) in 1993 to 47.3 (0.473) in 2004 in China, which means that its wealth divide has been increasing, according to Key Indicators 2007". This means that the gap is increasing between the rich and the poor.

76 *The Encyclopaedia Britannica - BRITANNICA BOOK OF THE YEAR 2006* - Showing a difference in relation to the previous administration, the government began to take active measures to ease rural poverty. The widening wealth gap in Chinese society had prompted social protests and distrust in government. The Gini coefficient (a measure of income distribution in a society by which 0 = perfect equality and 1 = perfect inequality) in China had already exceeded the 0.4 threshold—widely viewed as an indicator of potential serious social disruption and instability. While the country's economy had been on the fast track in recent years, a significant portion of its rural population had not been lifted from poverty. As such, the People's National Congress in March decided to eliminate most of the basic agricultural taxes imposed on rural families and to increase agricultural subsidies for grain production. Agricultural reforms, however, fell short of granting peasants greater control over their land.

77 http://en.ce.cn/Insight/200509/13/t20050913_4669147.shtml# (accessed on March, 22, 2008).

78 "(...) In practical view, applications of Gini coefficient in various countries across the world are not exactly the same. Many countries integrate it with other factors to judge the income gap in a comprehensive manner. Among quite a few countries, Gini coefficient features different criteria and benchmarks. China is a typical country based on dual economy. The special national condition of huge gap between urban and rural areas make it impossible and unreasonable to simply judge China's income gap by common standards of Gini coefficient".

79 <http://ranc2.blogspot.com/2005/12/undp-chinas-gini-coefficient-nears-45.html>, (accessed on March, 22, 2008).

80 http://news.xinhuanet.com/english/2007-08/08/content_6493366.htm, (accessed on March, 22, 2008).

d) Finally the “United Nations Human Development Report for 2007-2008”⁸¹, considers the

Gini Coefficient as being as per 2004 figures, 0.469.

Different figures, although there is one important conclusion: the situation is not improving.

But there is another coefficient presented by the Chinese Social Sciences Academy:

B. The Engel Coefficient⁸²:

	2001	2002	2003	2004	2005	Unit: %
Urban families	38.2	37.7	37.1	37.7	36.7	
Rural families	47.7	46.2	45.6	47.2	45.5	

And the conclusion is: “While income growth rate is lower than the overall economic growth rate, the high growth of the savings rate of Chinese residents still commands our attention. Since reform and opening up, the savings rate of the resident sectors has always been comparatively high. This generates the huge domestic capital sources that constitute China’s capital accumulation, and has also become one of the important factors that have underpinned the rapid development of the economy”.

But from a national point of view, there are different stages of development when we compare the inland and the coastal provinces with the west and inland of China.

In a study by Li Yang and Robert Lawrence Kuhn called “Regional financial-asset quality and economic level in Eastern, Central and Western regions (2004)”⁸³, the following figures are presented (and a major conclusion - “economic development level is not the only factor that determines the quality of financial assets”):

81 UN Human Development Report, 2007-2008, (2007) (table 15).

82 “The proportion of food expenditure to total consumer expenditure”, as per Li Yang, Robert Lawrence Kuhn, (2007), *China’s Banking and Financial Markets*, Singapore, John Wiley & Sons, p.15.

83 Li Yang, Robert Lawrence Kuhn, (2007), *China’s Banking and Financial Markets*, Singapore, John Wiley & Sons, p.343 . An indicator rating “Non-credit Asset Quality”, “Credit Asset Quality” and “Off-balance-sheet business Quality”.

	Asset Quality ⁸⁴	GDPpc
Eastern Region	66 849	22,811.11
Central Region	25 335	10,979.96
Western Region	52 234	7,973.49

And again the Asian Development Bank, in its September report⁸⁵, (2007), shows the government's concern:

“Supported by policies to boost the rural economy, investment in agriculture surged by 37.5% in the first half, faster than that in industry (29.0%) and services (24.6%).” The report also “says domestic agriculture should be boosted by policies to lift rural incomes and improve rural infrastructure. Growth in the services sector will be supported by the summer Olympics next year”.

(If we investigate the “Human Poverty Index” in the Human Development Report 2007 – 2008⁸⁶, China ranks 29th – value 11.27%).

Two actions taken by the Chinese authorities should be stressed: In 2003, “(...) the roll-out of the “Sunshine Policy”, designed to provide prospective with rudimentary job training and information about conditions in destination cities”⁸⁷; and, in 2005, the authorities decided to abolish the agriculture tax, making life easier for the farmers. These two have not yet been fully evaluated.

We can see increased imbalances and more pressure to solve social problems.

What is China doing with its public revenue, how is China planning its public expenditure? The investment in main sectors is really incipient, which is why the latest Human Development Report⁸⁸, classifies China as 81st, slightly below the Medium Human Development limit (between the 70th and 71st), all figures represent % of GDP:

Public Expendi- ture on Health	Public Expendi- ture Education		Military Expenditure		Total Debt Service	
(2004)	1991	2002-05	1990	2005	1990	2005
1.8	2.2	1.9	2.7	2.0	2.0	1.2

84 Measuring units.

85 ADB Site: ADB Raises PRC Growth Forecast for 2007 and 2008.mht (accessed on March, 22, 2008).

86 Human Development Report 2007-2008, (2007), p. 238.

87 Barry Naughton, “The Chinese Economy”, (2007), Massachusetts, MIT, p. 134.

88 Human Development Report 2007-2008, (2007), p. 295.

Finally, another important issue (together with the increasing pressure China will experience the Beijing Olympic Games in August, 2008 and some other political relevant constrains⁸⁹): the governance issue, just to give you an up-date on the latest (March, 2008) government remodeling. An important issue arising from this latest NPC meeting was the super-solution drawn to establish five super-ministries, “which constituted part of the country’s latest government reshuffle plan”⁹⁰ or in other words, “as part of an effort to streamline a bloated bureaucracy and clarify conflicting responsibilities that stymie top level decision making”⁹¹, and affecting the administration of different areas of governance⁹², presented by the China Daily⁹³ in the following order:

- a) Ministry of Industry and Information – Li Yizhong;
- b) Ministry of Human Resources and Social Security – Yn Weimin;
- c) Ministry of Environmental Protection – Zhou Shengxian;
- d) Ministry of Housing and Urban – rural Construction – Jiang Weixing;
- e) Ministry of Transport – Li Shenglin.

First reactions. Difficulties arising⁹⁴:

- Regarding the environment protection and the reduction of inequalities, “the government in Beijing, (...), has had trouble in implementing these sensitive policies in provinces obsessed by growth at all costs”.
- In reference to areas like “transport and agriculture”: “Their increased power, and the proposed separation of regulation and enforcement from policymaking, is designed to make it harder for provincial Communist leaders to flout the will of the centre”. And “Already there are signs of resistance, with state-owned oil and power companies lobbying against the idea of a powerful energy ministry”.

As a conclusion, the main focus is the different kind of lobbies, either CCP, local powers or Energy or Industrial Groups questioning the implemen-

89 China is facing deep pressure from three sources: Taiwan, Tibet and Xinjiang, which will be harder issues as the Beijing Olympic Games get closer; managing of the asymmetries will be relevant but not enough. The opposite, disparities and cultural shock can worsen the socio-political environment. Taiwan – wind is blowing in a different direction since the Nationalists won both recent elections, specially the presidency elections, with a clear sign of no-belligerency between both parties, (doesn’t mean Taiwan will be peacefully integrated in the near future).

90 www.chinadaily.com.cn/china/2008-03/17/content_6542967.htm(accessed on March.17,2008).

91 *Financial Times*, (2008), 12, March, p.4.

92 *Financial Times*, (2008), 10, March, p.8: “(...) construction, transports, IT policy and social security”.

93 www.chinadaily.com.cn/china/2008-03/17/content_6542967.htm(accessed on March.17,2008).

94 *Financial Times*, (2008), 10, March, p.8.

tation of policies and regulations, showing that there still is a visible hot spot between the centralization policies and the regional powers.

4. Financial China

Firstly, we will analyze how China has built its Banking System, and later, which are financial system's main pillars and latest developments. Our objective is in to update information and understand the progressive internationalization of the Chinese financial system.

Noteworthy is the fact that China tightened its monetary policy, increasing its banks reserve requirements for the 9th time in 2007, increasing its interest rate again.

We shall then begin by analyzing the Chinese Banking system.

China has been living with a “monobank system”, the People’s Bank of China, PBC, established in 1948, until the economic reform era came in 1978. In fact, was Deng Xiaoping who has drawn in 1979 the Opening and Reform Policy.

Its main missions were mainly of supervisor, government treasury and commercial bank. In other words, they were at the time prepared:

- to issue currency;
- to extend loans to the government and state enterprises⁹⁵ following the central planning (approved by the planning authority) ;
- to accepted savings deposits from the public, through its branches;

PBC was transformed into a central bank in 1983⁹⁶, when the global strategy under the economic reform book was heading towards a market-oriented economy. Then, a few specialized banks were established:

- the Industrial and Commercial Bank of China, ICBC;
- the Agricultural Bank of China, ABC;
- the People’s Construction Bank of China, PCBC;
- the Bank of China, (foreign transactions) .

As the three first banks were given autonomy in terms of credit concession, there were two relevant consequences:

95 “Besides the state enterprises there are three types of enterprise in China: collective, individual, and overseas-funded, the last having been established under the open-door policy”, (Chow, 2007), p. 55.

96 “This process was finalized with the establishment of the PBOC as a central bank and the Industrial and Commercial Bank of China (ICBC) as an independent entity in 1984”, in Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p.4.

- There was a quick increase of currency supply by 50% in 1984. This was explained (Chow, 2007) by the central bank having to honor the credit extended by those specialized banks.
- In 1985 the inflation rate was 8.8%, (overall retail price index).

In October 1992, the Central Committee of the CCP decided on a socialist market economy, being relevant the reform of the banking system to speed the economic reform pace. However, only in 1993, in the Third Plenum of the 14th Central Committee of the CCP, were issued directives to accelerate the reform of the financial sector. Two main decisions were taken:

- PBC became independent, a “real” central bank;
- The specialized banks became commercial banks.

Only in 1995 did the People’s Congress pass two major laws:

- Law on the People’s Bank of China, (March, 18 and May, 10, and effective same day);
- Commercial Banking Law, (effective July, 1st).

The recapitalization of the banking system started in 1998, with the issuance of RMB 270 000 million⁹⁷ in special bonds in order to improve the Capital Adequacy Ratios (CAR’s) of the Big Four.

In 1999, four state-run Asset Management Companies (AMC’s) were created, to buy nonperforming loans (NPL’s) generated before 1996 from each of the four major banks⁹⁸. This policy was twofold: banking restructuring and the enterprise’s reform⁹⁹.

The WTO agreement, (in December, 2001), and the desire to join this Organization led to the speeding of the system’s reform.

In 2003, in order to fix the regulatory function and to increase the independence of the central bank, the central government established the China Banking Regulatory Commission (CBRC) to supervise financial institutions under the State Council.

Its main laws and regulations are:

- Law of the People’s Banking of China;
- Commercial Banking Law;
- Law on Banking Supervision and Administration.

97 Barry Naughton, “The Chinese Economy”, (2007), Massachusetts, MIT, p. 462.

98 Bank of Communications-Orient Asset Management; Agricultural Bank of China: Great Wall Asset Management; China Construction Bank-Cinda Asset Management and ICBC-Huarong Asset Management

99 The state Enterprise restructuring and gradual downsizing started in the mid-90’s.

But legal independence is not necessarily real. The statutes/structure/practice of both the CBRC and PBOC, and the action of the central, regional or local authorities, show that their independence is still a mere written word, not yet reality.

Violaine Cousin¹⁰⁰ explains the political influence affecting the regulators, PBOC and CBRC:

“(…) Parts of these laws do point to some degree of independence, while other parts refer to the strong position of the State Council other ministerial agencies and their instructions.

“(…) Committees in both PBRC and CBRC also are mostly staffed with personnel from the Communist Party chosen by the State Council. (…) Through the committee for monetary issues, the National People’s Congress also gets an opportunity to oversee the work of the PBOC (Grimm, 2005; Wei W. 2005)”.

“(…) As a result from the strong influence exerted by the State Council, PBOC and CBRC cannot be made fully accountable for their policies and actions. Their subordination to the State Council reduces the degree of achievable functional, institutional, personal and financial independence. Local authorities also influence the regulatory authorities where and when deemed necessary”.

On July 21, 2005, the Bank of China revealed the markets (when there was huge international pressure to revalue the RMB, a pressure led by its greatest trade partner, the USA), that the government was going to reform the exchange rate system, (abandoning the peg between the RMB and the USD), adopting a floating exchange system with reference to a basket of currencies.

In 2005 more than 35000 institutions formed the Chinese banking system under CBRC, mainly:

- 4 state-owned commercial banks, SOCB’s, (representing major share of banking assets, but with 3 weak points: involvement with the state sector, insufficient equity and high level of NPL’s);
- 3 state-owned policy banks, SOPB’s, (Agriculture Development Bank, Export-Import Bank of China and China Development Bank¹⁰¹).
- 13 joint-stock commercial banks, JSCB’s, (established between 1987 and 1995; small market share and *good* loan portfolios, since they are almost free to grant credit to the SOE’s);

100 In Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p.26.

101 See 6. B) about Barclays’ share issue, (June, 2008).

- 115 city commercial banks, CCB’s, (created in the late 90’s in urban areas, with the merger of more than one hundred Urban Credit Cooperatives, and 709 still active UCC’s);
- and 30 438 rural credit cooperatives, RCC’s, (which started to absorb the rural savings and provide funds to agriculture projects and TVE’s, township and village enterprises, with low quality loans and local government influence).

In 2005, more than 73% of the banking assets were controlled by the three groups of institutions¹⁰².

Now we are going to look at the Chinese Banking Ratios (2006 data), working on information I collected from the latest issue of *The Banker*¹⁰³:

The two maps below show the Chinese Banks Performance and Soundness, in comparative terms:

Table 1. Chinese Banks Ratios

Ranking¹⁰⁴

2005	2006	Banks	Tier 1 Capital	Assets Size			Performance Profits on Av Capital		Return on Assets		Cost to Income Ratio	BIS Capital Ratio	NPL ¹⁰⁵ to Total Loans
				\$m	\$m	Rk	%	Rk	%	Rk			
16	7	ICBC	59,166	961,576	20	20.1	453	0.96	599	36.30	14.05	3.79	
17	9	BOC	52,518	682,262	30	20.5	436	1.28	458	46.32	13.59	4.04	
11	14	CCBC	42,286	697,740	28	21.4	406	1.21	485	na	12.11	3.29	
60	65	ABC	11,425	684,349	29	14.4	636	0.23	934	na	-17.56	23.43	
65	68	BC	10,647	220,198	69	22.4	365	1.01	567	47.66	10.83	2.53	

Key: 1. Information worked on *The Banker*, (2007), July, 2007.

2. Banks considered:

ICBC, BOC – Bank of China, CCBC – China Constructions Bank of Corporation, ABC – Agricultural Bank of China, BC – Bank of Communications (Shanghai)

And the following map demonstrates the Soundness of the Chinese Banks:

102 A few books were consulted to confirm the banking history, and also in order to get the present view of the China’s Banking Sector, such as three books published in 2007: Gregory Chow, (2007), “*China’s Economic Transformation*”, Victoria, Blackwell Publishing; Randall Perenboom, (2007), “*China Modernizes*”, and Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan.

103 *The Banker*, (2007), July 2007. A reference to the world of Banking.

104 Map based on information in *The Banker*, (2007), July 2007.

105 Non-performing loans.

Table 2. Chinese Banks Ratios

Ranking - 2006		Soundness – Capital Assets Ratio			
Ranking Tier 1 Capital	Banks	% (latest)	% (previous)	Ranking (latest)	Ranking (previous)
7	ICBC	6.15	3.96	556	864
9	BOC	7.70	5.34	381	663
14	CCBC	6.06	6.20	570	537
65	ABC	1.67	1.67	996	996
68	BC	4.84	5.07	747	700

Legend: Information worked on *The Banker*, (2007), July, 2007.

Some brief conclusions:

a) Only two banks, ICBC and Bank of China improved their Ranking position for *Tier 1 Capital*;

b) Regarding *Soundness*, only one bank is in a worse position, Bank of Communications.

c) We must pay attention to the latest evolution on the Capitalization processes operated in China, ICBC being the biggest IPO ever, with \$22 000 million.

d) In terms of the different ratios:

di) Good *Cost to income ratios*, well below 50%;

dii) *Performance*, through the ratio *Profits on average capital*, completely out of their dimension, between the 365th (Bank of Communications) and the worst, Agricultural Bank of China¹⁰⁶;

diii) The same conclusion can be drawn in terms of *Return on Assets*, although the best of Chinese bank is Bank of China, the Agricultural Bank of China being closer to number 1000;

div) When analyzing *Soundness*, the Bank of China is best, with a very strong recovery;

dv) *BIS Ratio* is in line with the ranking, and only ABC is showing negative status, and a very high *NPL to Total Loans*;

dvi) *NPL to Total Assets* is generally low since their portfolio has been cleaned up, (see point 5 of this essay).

106 Please note that the performance of the SOCB's has improved "dramatically since 1999, perhaps with the exception of ABC, where small progress has been made): NPL's have been transferred, capital has been freshly raised, subordinated debt has been issued, much of this thanks to the largesse of central authorities" Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p125.

It is clear that the reform of the banking system is not yet finished and there are still hard weaknesses to solve.

Violaine Cousin also points out some, when starting to speak about the system, namely, “insufficient capital¹⁰⁷, government interference, poor risk management practices and a large shunks of NPLs”¹⁰⁸:

I will elaborate more on this latter issue, considering it a major weakness, with large impact on future financial and economic activity.

Explaining the “emergence of NPLs”, I quote a statement issued by the People’s Bank of China in 2004 which says: “According to this survey, 30% of the NPLs resulted from state planning and administrative intervention, 30% were due to defaults of state enterprises after state banks provided financing based on state policy, 10% came from structural adjustments as a result of state orchestrated closures, mergers and restructuring of enterprises, 10% stemmed from intervention of local governments including poor credit protection in the judicial and enforcement process, while 20% was due to the inappropriate internal management. In addition, factors, such as poor credit culture, intentional defaults and inadequate application of accounting standards, can be found in all over categories.”¹⁰⁹.

These explanations show clearly how serious the problems were faced by the financial system as a whole, and how much is still to be done for them to be completely solved, since some of these characteristics are visible.

The same author, speaking about the NPLs, states that “As for many banks their NPLs exceeded their equity in the past, the banks were technically insolvent and kept afloat only to avoid bank runs”¹¹⁰. This sentence evidences deep concern.

It was a major global economic problem and the turning point was when the government decided to create four Asset Management Companies, AMC’s, (one for each SOCB), and with injections of cash, to proceed with the transfer of NPLs from the SOCB’s¹¹¹. In 2002 “the government required

107 But as explained the listing process shows a different time frame. Please compare with above mentioned weak points. For SOCB’s.

108 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p.3.

109 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p.83, 84.

110 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p.81.

111 Look at a list of weaknesses of the SOCB’s, by the same author, p.127, where you can find a synthesis of what we are confirming in this chapter: “(...) NPL/NPA levels; Lack of functioning corporate governance structures; Interference of state, bearing scars of socialist planning; Under capitalised; Lack of qualified personnel; Corruption; Large numbers of policy related loans; Rigid management structures; Simple products; Low level of customer service”.

banks to account for their NPL's in a way that was in line with international current practices"¹¹².

But the worst point is that the banking system is still keeping a huge part of those NPL's. In an Ernst & Young report¹¹³ published in May 2006, it was stated that around USD 900 000 million were still in the system.

The China Regulatory Commission has a softer view on China's Banks and the Non Performing Loan, NPL ratio¹¹⁴: Although the NPL for large banks is 8% average, (the China Banking Regulatory Commission, CBRC), the small and mid-size lenders average is only 2.45%, with 20 banks having less than one percent. In 2006 there was a combined NPL for China's 12 joint-stock commercial banks of 2.96%.

The good news came from the "qualified institutional investors, involving more than 100 senior domestic and foreign managers" and CBRC suggests that small banks "should continue to improve corporate governance and beef up asset management and risk control to prevent a resurgence of bad loans as global financial situations soured".

Another issue not much mentioned but quite relevant is the so called "*informal lending*"¹¹⁵, which distorts financial intermediation. The negative aspects: "(...) it adds pressure on sources of funding for formal banks, it represents foregone tax revenues for the authorities, interest rates can be usurious, it breaches with official development policies (runs contrary to any controls that governments tend to set upon financial flows), and finally limits the regulatory role of the authorities (Girardin, 1997)". It is provided in two ways, "one formal, dominated by the steering hand of the state, (...), the other informal, dominated by networks and relationships among individuals, which has provided an alternative to the mainstream system. Both seem, however, to be necessary ingredients of China's economic success (Allen et al., 2005)"¹¹⁶. Informal lending markets "are estimated to amount to around CNY 950 bln to CNY 1 trillion, which is around 7% of GDP and 6% of all lending in China (OECD...)"¹¹⁷.

A few pages ago saw a first approach to the Chinese banking rankings, an analysis based on ratios. Let us speak now about the performance¹¹⁸ of the

112 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p86.

113 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p 252.

114 www.chinadaily.com.cn/china/2008-03/15/content_6542967.htm (March.17,2008).

115 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p 78, 79.

116 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p 78.

117 Violaine Cousin, (2007), *Banking in China*, London, Palgrave Macmillan, p 252.

118 *China Daily*, (2008), January, 21, (Accessed on January, 21, 2008).

banking system in 2007. Eight of the 14 listed commercial banks reported about 50% profit increases, and the Industrial and Commercial Bank of China estimated a surge of 60%, over \$ 10.8 thousand million, (78 thousand million Yuan). China Construction Bank had a 48% increase to 68.6 thousand million Yuan, “(...) strong revenues from loans and expanding wealth management and credit cards services”).

The perspectives for 2008 are not optimistic according to the Finance Research Institute of Chinese Academy of Social Sciences (CASS), which explains that offering similar services and taking their profit from the high interest margins, being the government policy oriented to get a tighten monetary policy, the margins can be narrower and the revenues can decrease. As I have stated before, the integration of Chinese banks in the global markets, the sub-prime crisis and other problems can seriously affect the sector¹¹⁹.

An important event was the agreement¹²⁰ between China and the United States of America, in December, 2007. *China Daily* used the asymptomatic title “China agrees to open up financial service industry”, introducing a few remarks on the developments discussed and eventually agreed between both countries. China promised to “complete a study of foreign equity participation in the banking sector by the end of 2008 and make relevant policy recommendations”. This means that China wants to get some more time for changes and wider opening up.

Another (little) step was taken regarding foreign banks - China Banking Regulatory Commission, “has finished its feasibility study of allowing foreign banks to list domestically”¹²¹, a process to be completed during the year.

The irregularities and banking problems are still quite big and sensitive. To understand the dimension of the banking problems, the Chinese regulator (when the major commercial banks got a profit of about € 21.6 thousand million, for total 2007) informed the market that there were banking irregularities of over € 81 thousand million.

But the law and the reality are different. And one of the major characteristics of the present status of the world financial markets is the stock exchange dynamic activity, which offers a different perspective on China’s financing companies, state owned companies and the growing private sector, and the government.

119 Asian Development Bank through its senior analyst, Zhuang Jian, defends the opposite trend, saying Chinese banks are getting stronger.

120 *China Daily*, (2007), December, 13.

121 *China Daily*, (2008), January, 21.

Initial Public Offers¹²², IPO's, are forcing the improvement of corporate governance, (board of directors, supervisory boards, senior managers) and also forcing the bank's efficiency.

Looking at the corporate governance and management systems in the Western banks, there are two major streams: independent director system, and supervisory board system.

- The first one is applied in the United States and Britain, where an external body supervises bank management.
- The second one comes from Germany and Japan, where they oversee day-to-day operations.

If outside China both systems do not coexist, in China we see both systems, plus the role of the Communist Party Committee (system).

• March, 2008: The *Subprime* crisis exposure and the Chinese banks and securities cos.

Chinese authorities, in this case, Chinese Premier Wen Jiabao, expressed the difficulties dealing with what he called “potential global economic fallout from the US subprime crisis and expanding financial woes which could make China's job of balancing growth and fighting inflation more difficult”¹²³. And the *China Daily* expressed some concern since investors were getting scared, and gave some examples of Chinese banks whose shares were coming down:

“In only three months share prices of Industrial and Commerce Bank of China, ICBC, China Construction Bank (CCB), and Bank of China (BOC), have stumbled 29 percent, 27 percent and 2 percent respectively last Friday from the first day of 2008”¹²⁴.

Some research reports¹²⁵ state that Securities firms still consider that there was a limited and not significant impact on ICBC, CCB and BOC.

Finally, the same sources declare that “of the three banks, BOC and ICBC were the top two investing in the US *subprime* mortgage market. The analysts claim the losses of the banks from the subprime debt will be very limited, since the three only own \$ 10.237 billion¹²⁶ of subprime assets, accounting for less than 1 per cent of their total assets, which is not significant enough to impair performance”.

122 Please see again n. 7 where this issue will be further discussed.

123 “Wen: China worried about US financial woes”, in *Chinadaily.com.cn*, 2008, March, 18, (March, 18, 2008).

124 www.chinadaily.com.cn/china/2008-03/17/content_6542389.htm (March.17,2008).

125 See same article.

126 In this chapter billions= thousand millions. This figure, for example, should be read as \$ 10 237 million.

In another article from the *China Daily*, CCB informed that its *subprime* bonds accounted only for 2.75 % of its total investment in foreign exchange bonds. Then the different announcements:

“CCB, which owns US 1.062 billion subprime-related bonds and assets, says its revenue won’t be affected by the crisis since the assets are a very small amount accounting for only 0.12 percent of the bank’s total assets and 1.96 percent of its net assets”¹²⁷.

“ICBC said its subprime mortgage- backed and related securities were valued at \$ 1.228 billion, accounting for 0.1 percent of its total assets and 1,68 percent of its net assets. The bank had allocated 30 percent risk reserve - \$ 61 million – to cover the losses from the subprime debts”.

“BOC the largest holder of the US subprime-related assets, owns \$ 7.947 billion of subprime debts, accounting for 0.95 percent of the bank’s total assets, and 12.70 percent of its net assets. However because the bank has actively improved its subprime-related portfolio and sold the comparatively risky part of the debts, its subprime assets have been greatly reduced. The bank has disposed of all its subprime-related collateralized debt obligations (CDO), a high risk subprime bond, and set aside risk reserves of 1.15 billion Yuan to cover losses from the subprime crisis”.

Again the amount can be not so small, but really the magnitude of the figures generated in China’s economy give a distinct relative value to the potential negative impacts.

Finally, and regarding the latest trouble issue, the Fannie Mae and Freddie Mac case, it is something important to look at it in the future:

- How will China be affected? Immediate impact: Asian and European markets suffered sharply falls on their stock markets. Quoting the *Financial Times*, “mainland Chinese investors owned \$ 376 bn¹²⁸ of agency long-term debt at the end of June, last year”.

We will go now to the Chinese International Economic Activity.

127 www.chinadaily.com.cn/china/2008-03/17/content_6542967.htm (March.17,2008).

128 USD 376 000 million, European norm.

5. The Internationalization of Chinese Economic Agents

- **Overview and latest developments**
- **The role of the Sovereign Wealth Funds**

Following the *logic* of the dynamic SWF's, during the last couple of years China has developed a major issue, the internationalization of its economy and finance. Highly capitalized institutions/corporations, with plenty of excess liquidity, (but which have still not yet performed all the restructuring and technical recycling, so as its modernization "homework"¹²⁹) view the presently ailing international institutions as easy targets to invest. A dual intention should be in mind: a strategic one, getting an important presence in American or European institutions, getting technical skills and expertise from these deals, and also internationally projecting its image¹³⁰. The second is purely financial, as soon as it is (at least theoretically) a profitable operation behind it.

What seemed to be an easy way to be part of the global competitive markets is, on the other hand, a more complicated action, since it has experienced some setbacks:

- Blackstone investment by China Investment Corporation, (the neophyte¹³¹ but powerful Chinese Sovereign Fund);
- Bear Sterns vs. CITIC Securities (the huge American Investment Bank under a recovery solution);
- Morgan Stanley vs. CICC (in March, 26, 2008, Morgan put on hold the provisional sale of its stake to China International Capital Corp, CICC).

But considering the present and future potential impact of this activity, and looking at the China's investment praxis, it is interesting to further analyze the nature of investment activity, because it is a confirmed trend - China will invest Overseas in a more dynamic and consistent path.

129 In another direction, it is relevant to understand the role of the World Bank and China: last year, the new president of the World Bank defended that China must receive aid despite its rapid growth and huge FX reserves, just because China was considered as having reached its turning point from receiver of funds to the active role of donor. To confirm this assertion, China gave financial support to the Democratic Rep. of Congo and Costa Rica, in 2008.

130 A negative characteristic of the Chinese industrial effort is **the absence of well known trade-marks**. This is presently obvious when China doesn't have much to show on that subject for the Olympics Mega-Show. I have written on this topic in other occasion, for a *Simology Conference* in Lisbon, regarding the "Economic and Financial Impact of the Beijing Olympic Games" in January, in a session with Prof. Pierre Gentelle.

131 China Investment Corporation was founded last year, during 2007.

China is expanding its appetite for natural resources and looking for attractive investment deals. In 2007 China was quite active in expanding its targets for investments, and we can stress the following:

- The BHP-RioTinto¹³² case: China appeared involved just to support one side, as it had done with Barclays’ pre-offer of purchase of ABN. [See point 6. A) b) and c)];
- Stakes in International banks, (See point 6.).
- Participation deals by Chinese companies in overseas enterprises or groups.

A quick look to the third issue:

Chinese Groups targeting Oil-Companies abroad:

I will speak about the other two points. But considering the strategic moves operated by Chinese companies abroad I can give the example of the investments in oil-targets.

In 2005 the state-owned CNOOC, China National Offshore Oil, was forced to withdraw from the bid - \$ 18 500 million- for the California’s Unocal, considering the political opposition to this Chinese move.

Table 3. Chinese Acquisitions of Energy-related Companies Abroad¹³³

Date	Acquirer	Target	Deal Value (\$1000) / Stake
2005	China National Petrol Corp	PetroKazakstan / Kazakhstan	4 200 / 100%
2006	CNOOC	Oil&Gas Assets / Nigeria	2 700 / 45%
2006	Sinopec	Udmurtneft / Russia	3 500 / 99.5%
2008	SAFE ¹³⁴	British Petroleum / UK	2 000 / 1%
2008	SAFE	Total / France	2 900 / 1.6%
2008	CNOOC ¹³⁵	Awilco Offshore ASA / Norway	> 2 000

Note: A few pages further I will explain SAFE’s statute and activity.

132 On June, 24, 2008, a surprising move shock the steel market. **Baosteel, China’s biggest steel group agreed to pay Rio Tinto 96,5 % more**, for the iron ore, (the previous increase was about 9,5 %). The main Australian competitor, BHP Billiton came to say that the rises was not enough, planning to “reshape the market”.

133 The Wall Street Journal, (2008), June, 23, 2008, p. 5.

134 See 5. B).

135 Under talks in June, 2008. A consortium led by the oil-services arm of CNOOC. The Wall Street Journal, (2008), June, 23, 2008, p. 5.

Although the USA (as the EU and other players) criticize the undervalued Yuan, as China is investing huge values in U.S. Bonds, and although they are loosing value because the dollar is weaker, it's not easy for China to change to other financial products or currencies. A quick move would lead to the devaluation of those bonds; this is a clear sign of how these two countries are "in the same boat".

How is China doing in 2008? And how are other countries investing in U.S. Securities? Is China avoiding the inter-dependence?

Table 4. Top Foreign Buyers of US Securities (Jan.-April, 2008)¹³⁶

Countries	Investment in US Securities (\$ Million)
China	76 700
Japan	56 300
Hong Kong	39 200
Brazil	22 700
Norway	16 600
Mexico	14 800
Canada	13 900
Singapore	12 300
South Korea	6 300

Some conclusions, (also using quotations from the same source):

- a) The growing import bill is financed by emergent-market nations, ("from poor to rich");
- b) Amounts invested by foreigners in US stocks, bonds and securities: "China alone accounted for 21 percentage points of the total¹³⁷, , Brazil with 8.4% and Russia 2.8 points, (...)";
- c) "The US has to import, on net, almost \$ 2 000 million a day to cover its enormous trade gap".
- d) We can see four countries from Asia, and if we put together Hong Kong and China, the investment is \$ 115 900, roughly the double of Japan, the 2nd biggest investor.
- e) We can see that there are not mentioned oil-rich countries from the Persian Gulf. It's a fact. And it is partially explained by investments through London, and then considered British.

136 The Wall Street Journal, (2008), June 23, 2008, p. 11.

137 The % of the total foreign investment in US stocks, bonds and securities, according to Bank of America calculations using U.S. Treasury data.

Now let us briefly look at China’s investment policy abroad¹³⁸

First of all we should mention that in 2007 China was ranked top “attractive” country for investment, reaching € 51 thousand million out of the financial sector, against € 47.5 thousand million in 2006.

Investment in banks, insurers and shares reached € 5.4 thousand million. On the other hand, China invested substantially less abroad: €13.6 thousand million, through 120 thousand companies operating out of the country.

These figures are really impressive, since China adopted policies to restrain the capital inflow, trying to protect the real estate sector and its heavy industries, like the auto industry.

China’s two main national vehicles of investment are:

A) China Investment Corporation and the Sovereign Wealth Funds

The most relevant issue is the fact that last year China opened a new door to investment: China started its own Investment Fund in 2007¹³⁹. Let us now analyze the main Asian and Middle East Funds as per FT/ Standard Chartered¹⁴⁰.

138 *Oje*, (2008), January 21, p. 4. and *Lusa Agency*.

139 Its head is Lou Jiwei.

140 *Público*, (2008), Janeiro 11, pp.8-9.

Table 5. Asian and Middle East Funds (in thousand million USD)

China	China Investment Corporation, CIC	2007	70/80 ¹⁴¹
Singapore	Temasek	1974	108
	Government Investment Corp.	1981	215
Brunei	Brunei Investment Authority	1983	30
Korea	Korea Investment Corporation	2005	20
Malaysia	Khazanah Nasional BHD	1993	17.9
Taiwan	National Stabilizing Fund	2001	15.2
Abu Dhabi	ADIA	1976	625
Kuwait	Kuwait Investment Authority	1973	213
Russia	Oil Stabilizing Fund	2004	127,5
Norway	National Pension Fund	1990	322
Qatar ¹⁴²	Qatar Investment Authority ¹⁴³	2000	60 ¹⁴⁴

These funds were created to manage huge reserves, investing¹⁴⁵ mainly in US dollars and choosing American treasury debt as investment target. With the US dollar weakening, and managing increasing amounts of cash, these funds are opting for other currencies and other types of investments.

The gigantic losses presented by major financial institutions, like Citigroup, Merrill Lynch, Morgan Stanley, UBS and Barclay's, are new targets where these funds hope to produce high profitable investments. The *Financial Times* declared that:

141 *Financial Times*, (2008), April, 5-6, p.2. It should read USD 70/80 thousand million. But some other sources speak about USD 200 000 million for CIC. Smaller other SWF's (USD 1000 million): AUSTRALIA, *Australian Future Fund*, USD 42, CANADA, *Alberta Heritage Savings Trust Fund*, USD15, CHILE, *Economic and Social Stabilizing Fund and Pension Reserve Fund*: ~USD 11 and BOTSWANA, *Pula Fund*: USD 5.

142 Qatar asked help from the NYSE Euronext, to transform its Doha Securities Market into a "cash equities, derivatives and commodities platform". FT, (2008), June 25, 2008, p. 18.

143 Please see 6. A) c) about Barclays' share issue (June, 2008). About its objectives: "QIA is a sovereign fund whose prime objective is to achieve revenue diversification for the state of Qatar over the next 10 to 15 years from its establishment date. **As a result of its stated strategy to minimize risk** from Qatar's reliance **on energy prices**, the fund predominantly invests in international markets (USA, Europe and Asia) and within Qatar **outside the energy sector**. **The fund focuses on three asset classes; real estate, private equity and investment funds**". **Interesting to understand how clear vis the strategy!** In http://www.zawya.com/cm/profile.cfm/cid1003480.

144 In http://www.zawya.com/cm/profile.cfm/cid1003480

145 Please see one example of strategy for QIA, footnote 137.

“Sovereign wealth funds are suddenly the capital provider of first and last resort for ailing US financial institutions, investing at least € 20.5 thousand million)...”¹⁴⁶

This is a brand new face of this SWF’s activity. Just after the *subprime crisis* breaks down!

Another issue is that while the investment was considered as “cross-border investment” it was seen as some kind of passive investment in bank deposits and US treasury debt, but as soon as they became a “cross-border nationalization”, “channeling investments into the private sectors of other countries, to get a higher return”, they are seen as posing a different sort of risk or concern. The fact that there is no disclosure¹⁴⁷ may allow for their activity to be politically oriented. That is reason why the USA is pressuring the International Monetary Fund to produce a “code of best practices”¹⁴⁸.

Gao Xiqing the head of the Chinese SWF, CIC, on June, 3rd, in a OECD conference in Paris, trying to calm down the fears manifested by the western entities, informed the CIC was investing for financial return not for political motive, making passive investments in companies and walking away from countries in any way publicly hostile to SWF’s.

Just opening a space to speak about the new SWF coming from South America. Brazil, is nowadays the *star*, since got the *investment grade* status¹⁴⁹, and accordingly to a statement by the Minister of Finance, is preparing the launch of a Sovereign Fund, (€ 7 600 million). But the budget deficit of € 16 600 million, (fiscal year – end of March) is referred by analysts to consider it not a good idea. Some positive signs, like the significant surplus coming from the exports of commodities and USD reserves, so as the recent discovers of natural

146 *Financial Times*, (2008), January, 18, p.7.

147 In August 2007, an article was published in the New York Times which was called “**A Fear of Foreign Investments**” which stated: “(...) Mr. Truman of the Peterson Institute is one of many experts urging the United States, the International Monetary Fund and the World Bank to draw up codes of conduct that would keep politics out of investment decisions and require the funds to share information about the composition of their investment strategies”. The fear can be read in the sentence: “(...) As Asians countries and petro-states get rich, they certainly have the money to try to exert influence”. And regarding China, although in literal terms mixed with the Middle East, comes the real fear...“(...) But China and the Middle East have a long way to go before they are as transparent as Norway is. Some experts’ wonder what would happen if China took over an American pharmaceutical company and pressed for changes in prescription drug programs. Likewise, what would the reaction be if an Arab government demanded a bailout or tax break for its company in return for supporting peace talks in Iraq or Israel?”

148 *New York Times*, (2007) December, 3.

149 The latest BRIC to deserve it. This status was granted by the Rating Agency Standard & Poor’s in May, 2008.

gas and oil, (Tupi, Jupiter and Carioca sites/reserves: “The Economist” says that these fields can last one decade to start the oil production, and that Lula da Silva Brazil’s president informed that his country should join the powerful OPEC¹⁵⁰). China is the second trade partner of Brazil, which has recently chosen Macao to start a trade basis to work with the Chinese huge market.

Coming back to China, there is an intense activity, and its clear the use of power of seduction, even by countries. As we can confirm: a small column was published in the *International Herald Tribune*¹⁵¹, in January 2008, with the title “Seeking stronger ties”:

“Prime Minister Gordon Brown told China that he wanted Britain to be the top choice for Chinese trade and investment, as he sought to take the relationship to a ‘higher level’. Speaking in Beijing at a news conference alongside Prime Minister Wen Jiabao, Brown also said he welcomed investment from China’s huge sovereign wealth fund”.

But the issue is even more sensitive: during the first quarter of 2008, another huge financial institution is becoming more and more relevant, which now analyzed in a different perspective, as a “ferocious competitor” to CIC:

B) The State Administration of Foreign Administration, SAFE¹⁵², was founded by the Central Bank¹⁵³ to manage the Foreign Exchange Reserves¹⁵⁴. In February, 2008, its amount was €1.050.000 billion. Investing hugely in USD Treasury bonds, (about 70% investment in USD denominated bonds), the latest financial application was taking a 1.65 stake in Total, the French oil company, about € 1 800 million.

What are the main points of friction?

a) As they are two agencies, one may argue on the correctness of maintaining both¹⁵⁵, or if China should integrate them creating one huge and powerful Agency;

150 Indonesia decided to quit OPEC, moving from the posture as *oil exporter* to the *consumer* one, with the impact of the growing up of the crude oil prices and the end of subsidies (countries in Asia were subsidizing the prices to avoid worst conditions, and social unrest). Indonesia defended the oil prices to come down, (so as, Saudi Arabia decided to increase its production to press the prices down), but other members preferred to keep it high.

151 *International Herald Tribune*, (2008), January, 19-20, p.17.

152 The site: <http://www.safe.gov.cn>.

153 The People’s Bank of China, as we told.

154 I will return to the topic, showing the rapid evolution of the FX Reserves. See point n. 7.

155 Two different positions: Kuwait has only one body. Dubai and Singapore are defending two investment institutions, in order to improve investment performances, run better checks and balances.

b) The two have different means of management: SAFE has a much bigger amount to manage, so its investment strategy can be more aggressive.

c) There can be promiscuous management: The top official of SAFE has a seat in CIC board, which gives SAFE complete knowledge of CIC’s portfolio;

d) There is the so called “institutionally rivalry”: SAFE is controlled by the Central Bank and CIC reports to the Ministry of Finance.

e) Finally SAFE works based on secrecy, while CIC has to be more transparent in order to avoid current criticism endured by the different Sovereign Wealth Funds.

6. The Globalization Process of the Chinese Financial Institutions

Some conclusions can be drawn: we can point out some common features regarding China’s financial management, all evidencing the growing activity of Mergers & Acquisitions, (M&A) with China as an active partner/dealer:

1. *There is a deep interest in buying abroad, establishing partnerships around the world, with as main targets, the USA and Africa, in the near future this will be a dynamic and frequent trend. But also active in S. America, Central Asia, Middle East, Russia;*
2. *Chinese banks are taking advantage of the pressure on American bank stocks, affected by the so called sub-prime crisis, and eventual recession.*
3. *China, (besides securing commodities/energy needs), with its huge financial reserves and enormous liquidity is starting a new phase: “helping” big financial institutions in global deals, thus obtaining expertise and, above all, power, for better and for worse.*

In order to make the reading of this chapter easier, there will be a synthetic approach, more interested in trends and relevant features, and in typifying¹⁵⁶ some cases, rather than in a more descriptive analysis:

A. Chinese banks buying (or financing) abroad

- a) ICBC (2006) bought Indonesian **Bank Halim**¹⁵⁷ (a small bank);

¹⁵⁶ Pretends to be more a range of interesting examples, rather than an exhaustive analysis. Couldn’t be a complete one.

¹⁵⁷ A small bank.

(2007, Oct.): the acquisition of 80% of Macao Seng Heng Bank¹⁵⁸, for € 427 mios.

b) China Development Bank, (CDB), (2007) offered to pay € 2.200 million for 3.1% in

Barclays in order to help buying the Dutch bank ABN¹⁵⁹.

The consortium formed by Fortis and Santander won the deal.

But CDB and Temasek invested considerable amounts, although up to middle 2008, they saw a sharp draw of their stakes.

And again the CDB:

c) Barclays (2008) called on investors (groups) from Asia and the Middle East to provide the financial needed for its € 5 600 million share issue. Qatar Investment Authority¹⁶⁰ and the chairman of Qatar Holdings can go up to 10%. **China Development Bank** with 3% of the bank is going to invest £ 136 million. **Temasek** from Singapore will invest £ up to 200 million. Another investor will be Sumitomo Mitsui Banking Corporation¹⁶¹, through Sumitomo Mitsui Financial Group, its main commercial-banking-unit, acquiring a \$ 930 million stake.

B. Foreign Banks “purchasing” in China exhaustive

a) La Caixa, (2007, Sept.) bought 4.15% of **Bank of East Asia (BEA)** - Chinese bank established in Hong Kong - for € 265 millions, an agreement was signed between both banks.

b) Minsheng Bank and **UCBH**¹⁶², (2007, October, 8) An agreement was signed between Minsheng Bank¹⁶³ and **UCBH**¹⁶⁴, establishing that the former would buy 9.9% of **UCBH**, since American banks were considered cheap¹⁶⁵.

c) Bank of America, (BOA), it was said on May, 28, had plans to raise its stake in **China Construction Bank, (CCB)**, up to close to 11%, an investment of nearly USD 1 900 million, “by exercising an option it has to buy more

158 Belonging to the Macao gambling magnate Stanley Ho.

159 Barclay’s Bank did not get it, the *troika* formed by Fortis, Santander and Royal Bank of Scotland did.

160 See point Table 5. point 5. A).

161 Japanese banks are active: Mizuho Financial Group invested \$ 1 200 million in January, 2008, in Merrill Lynch. Mitsubishi UFJ is expected to follow the trend.

162 *Business Week*, (2007), November, p. 5.

163 It is the eighth largest bank.

164 **UCBH** Holdings, based in San Francisco.

165 This will probably be more dynamic in near future, explained by the enormous liquidity (“cash from going public”) obtained from recent IPO’s and its strong growth.

common shares”¹⁶⁶. The first deal was in June 2005, when BOA bought a 9% stake in a USD 3 000 million deal.”Since 2005, the two banks have started nearly two dozen partnership projects”.

d) BBVA which has a strategic cooperation agreement with **Citic Group**, is going to double its participation in twp of its unities, **Citic International Finance Holding (CIFH)** to 30%, and in **Citic Bank** up to 10,7%.

C. Exchange of Participations and Joint Trusts

a) CITIC¹⁶⁷ **Securities** and **Bear Sterns** (2007, October) announced the markets they were exchanging participations¹⁶⁸ and establishing a strategic alliance, the amount considered was € 715 million (USD 1 000 million)¹⁶⁹.

b) (2008, March): Problems with Bear Sterns led CITIC Securities Co. to inform the market that it couldn’t guarantee reaching a “final agreement to buy into US investment bank Bear Sterns when there was the intention by CITIC to buy”.

(2008, March, 5): *The New York Times*, quoting Kong Dan, chairman of Securities CITIC Group, revealed its company renewed interest together with an increase in the stake¹⁷⁰.

As Bear Sterns’ equities were under very intense pressure, two actions were taken:

- JPMorgan Chase first injected¹⁷¹ a huge amount to help to rescue the US investment bank.

166 The Associated Press, May, 28, 2008.

167 The biggest Securities House in China, whose major shareholder was Citic Group. *Diário Económico*, (2007), October, 23.

168 Please note that in October 2007 both companies informed that Citic was going to take a 6% stake in Bear Sterns, representing an investment of USD 1 000 million, while Bear Sterns should invest in CITIC the same amount, taking 2%.

169 Through the joint-venture they were opening (with head office) in Hong Kong. Bear Sterns was already receiving investment from Chinese institutions. *Business Week* clarifies the deal: “Citic will buy 40-year convertible trust preferred securities equal to 6% of Bear’s shares, with the option to boost the stake to 9.9%. In return, Bear will pay \$ 1 billion for six-year convertible debt representing a 2% stake in Citic, with an option to go to 5%. M&A business in China and Asia, will be the main focus for their future activity”.

170 The NYT article started as follows: “CITIC Securities, China’s top brokerage by assets, is negotiating a bigger stake in Bear Sterns Cos to reflect the U.S. Investment bank’s tumbling stock price since the two parties agreed to swap stakes last October, a CITIC executive said (...)” and “Citic is expected to seek a 9.9% stake in B.S., the maximum allowed to foreign parties without triggering a process of intense U.S. Government scrutiny, for \$ 1 billion”. And “It (B.S.), joins New York rivals such as Merrill Lynch, Morgan Stanley and Citigroup Inc. that have tapped foreign investors for billions dollars of new capital to help work through their losses”.

171 Agreeing to provide B.S. with emergency financing for four weeks, guaranteed by the Federal Reserve.

- **On** March, 16, 2008, JPMorgan Chase informed that it was going to acquire Bear Sterns “in a deal value at \$ 236.2 million (€ 151.79 million), representing \$2 a share, (two days before the announcement they were at \$ 30 a share and had been traded at \$ 159.36 at their peak).”

Then the Federal Reserve announced it was going to provide special financing to JP Morgan Chase, (to cover Bears’ less liquid assets), funding up to \$ 30 000 million, (€ 19 280 million).

b) While **Morgan Stanley** and **Royal Bank of Scotland** are negotiating, some other entities were approved by Chinese authorities to establish joint trusts with Chinese firms: **Barclay’s**, **National Australia Bank**, and **Ashmore Investment Management**.

The media¹⁷² informed that the financial regulators are preparing to raising the cap on foreign participation in joint ventures, from 20/25% to up to 49%.

D. Securities¹⁷³ Joint-ventures

The first approvals to establish mainland securities joint ventures were given to **Goldman Sachs** and **UBS**, but the regulators stopped that activity, fearing their control.

A sign that this market is going to move forward is the agreements signed between Credit Suisse and Founder Group (a conglomerate with a securities branch) to set up a joint venture to underwrite IPOs, advisory and research services.

172 *Caijing Magazine/ Business Week*.

173 *Financial Times*, (2007), December, 8-9, p.10.: The relaxation of the securities operation by foreign banks. Other cases: Morgan Stanley and China Fortune (one of the oldest brokers). The market is expecting to take months to be approved by the Chinese Securities Regulatory Commission, CSSR, and these two foreign operators will acquire no more than 33%, the maximum allowed for a stake in a joint venture. Other players, which were said to be interested were JPMorgan, Citigroup, Deutsche Bank and Lehman Brothers.

E. Investment Abroad, Africa¹⁷⁴

About the Chinese investment in Africa¹⁷⁵, the theme could deserve a whole new chapter, so, I just give an example: Macao magnate Stanley Ho¹⁷⁶ invested in a Mozambican Bank – Banco Moza.¹⁷⁷

F. Insurers Buying in China and Abroad (stakes in Foreign banks)

i) The two largest insurance companies, **China Life Insurance** and **Ping An Insurance**¹⁷⁸, received the regulatory approval to buy a stake in China Minsheng Banking for USD 1 420 million, (RMB 10 900 million). Each one will get 4.93 %.

And there are “(...) plans to buy into emerging-market financial institutions after the Chinese government broadens the scope for overseas investment by insurers(...)”¹⁷⁹.

ii) **Ping An Insurance**, announced it was going to pay around € 1800 million for a 4.18% stake in Belgian-Dutch Fortis Bank¹⁸⁰. On November 29th this information was released to the markets, which increased Fortis shares by about 7.3%. It was the first time a Chinese insurance company had taken a stake in an overseas insurer.

Besides the global conclusions mentioned before, we can see:

- i) **Strategic Alliances being established (in M&A it’s crucial for defense/offensive actions);**
- ii) **Exchange of expertise and technical skills;**

174 China is working with several Portuguese ex-colonies and Brazil, the so -called “Portuguese Speaking Countries”, through the Macao Platform, a business Forum to promote the business relationship among those countries.

175 The main forum of cooperation is the **Forum on China-Africa Cooperation, FOCAC**, founded in 2000. In a few words, the investment is managed through the **Exim Bank** or the **China-Africa Development Fund, CADF**, (FOCAC commitment 2006).

Note: A so different era, comparing to 1980, when I leaded a trade mission to South Africa, with traders from Macao and Hong Kong, and the Chinese members were considered “white” and stay in the same hotel, just because, some time ago, there was a close security agreement with Taiwan, (evolving also Israel).

176 The famous and prosperous business man from Macao Special Region, has 49% participation in a new bank, through its company Geocapital. Another partner will be Moçambique Capitais, taking 51% of the new bank and congregating about 150 business men from Mozambique. Geocapital is interested in investing in other areas of business. Branches will start working during the fist quarter of 2008. Following some previous partnerships in Mozambique, vice-chairman will be Prakash Ratilal, an ex-governor of Mozambican central bank. The new bank will operate in investment banking, and will provide corporate and private banking services.

177 *Oje*, (2007), November, 23.

178 China’s second largest life insurer.

179 *Financial Times*, (2007), June 12.

180 *Financial Times*, (2007), December, 1-2, p.11.

- iii) In Commercial business, the exchange and reciprocity of clients basis and products, nurturing client portfolios;
- iv) Diversification of risks and also of revenue sources;
- v) Exchange of accountability and supervision concepts;
- vi) Increasing global integration.

7. The Fund Raising Process and Some other relevant financial Issues

The Initial Public Offer, IPO's¹⁸¹ fund - raising and the Top Companies all over the world

Considering the industrial, financial restructuring and modernization legal actions, and the strong corporate and banking activity in 2007, the next years will be relevant for China, as it's gathering business experience, showing a more mature financial system and having to open the market to foreign banks, insurers or corporations faster.

In September, Bloomberg¹⁸² clearly showed this big change, as China had three players in the top ten, surpassing the paramount American financial Citigroup, and the big Oil Groups. ICBC got the third position less than a year after its appearance in the Stock Exchange, and after being the biggest co in the world.

So we can conclude that Chinese “conglomerates” are gaining momentum as the biggest market capitalization companies. I think it is quite interesting to look at the differences between in September and November, 2007.

Table 6. The Top Ten International Companies (in billion USD)

Companies	Capitalization	One-Year Variation (%)
1 Exxon Mobil	345 000	+24,78
2 General Electric	289 000	+12,95
3 ICBC	204 000	+109,00
4 Microsoft	196 000	+10,81
5 China Mobile	190 000	+ 95,22
6 Petrochina	190 000	+ 29,53
7 AT&T	179 000	+ 28,88
8 Royal Dutch Shell	178 000	+ 0,81
9 Citigroup	170 000	- 5,19
10 Gazprom	168 000	-24,59

181 Initial Public Offer.

182 *El País*, (2007), September, 2.

Looking at these figures we could comment that:

- Another relevant fact is the need to be listed in other financial markets, (and the Chinese companies consider “other markets” all those excluding Hong Kong, where they already are), so Petrochina is preparing to be listed in the Shanghai Stock Exchange. Petrochina and Chinamobile are also listed in New York.
- In May, Petrochina reported the discovery of the biggest Asian oil deposit in 30 years, in the Boan Bay, representing 7 500 million crude barrels.
- Just remind that Petrochina bought in December, 2006, 67% of PetroKazakhstan, then starting its internationalization process.

Volatile markets and conditions changed completely in November¹⁸³. The three Chinese companies included in the Top Ten Capitalization Ranking were Petrochina, which became 1st with the 878 000 mark), China Mobile is 4th and ICBC has lost a few places and is now 7th.

Regarding this information, I would like to quote an article by Floyd Norris published in the New York Times, (October, 20, 2007¹⁸⁴):

“China has passed the United States this year, with eight companies, among the 20 most valued ones, in world stock markets. The United States has seven, Western Europe has four and Russia has one.”

But if we look at the latest *FT Ranking* the situation is different, since among the top 20 China just have 4! Consequences of the changes operated in 2008 in the equity markets:

Well, let us see how is now, middle 2008 the situation. The *subprime* crisis came, (and still persists with all its epidemic consequences), China suffered natural disasters, (snowstorm, earthquake, floods), but the global markets show us interesting points. Look at the 2008’s *FT Global 500*¹⁸⁵:

183 In November, 2007: Market capitalization in billion USD: **1. Petrochina** / 878 000/Energy /China, 2. Exxon Mobile/ 472 000/ Energy / USA; 3.General Electric / 387 000/ Industry / USA; **4 China Mobile** 342 000/ Telecom’s/ China; 5 Microsoft / 315 000 / Software/ USA; 6 Gazprom/312 000/Energy/ RUSSI; **7. ICBC** 280 000/Finance/CHINA; 8 AT&T/237 000/Telecoms/ USA; 9. BP/237 000/Energy/UK; 10 Petrobrás/ 227 000/ Energy/BRASIL.

184 <http://www.nytimes.com/2007/10/20/business/20charts.html?pagewanted=print>. British way of presenting figures.

185 *Financial Times*, (2008), FT WEEKEND, June, 28/29, 2008, p. 35.

Table 7. FT Global 500 – 2008 – Marketing Capitalization Ranking \$m
(June, 28th, 2008)

Global Rank					
2008	2007	Companies	Countries	Market Value \$m	Sector
1	1	ExxonMobil	USA	452,505	Oil & Gas
2		PetroChina	China	423,996	Oil & Gas
3	2	General Electric	USA	369,596	General Industries
4	6	Gazprom	Russia	299,764	Oil & Gas
5	16	China Mobile	Hong Kong	298,093	Mobile Telecoms
6	9	ICBC	China	277,235	Banks
7	3	Microsoft	USA	264,131	Software&Computer
8	5	AT&T	USA	231,168	Fixed Line Telecom
9	10	Royal Dutch Shell	UK	220,110	Oil & Gas
10	13	Procter & Gamble	USA	215,640	Household goods & Home construction
(...)	(...)	(...)	(...)	(...)	(...)

And looking for more Chinese companies down to the 50th:

20	35	China Construction Bank		Banks
26	23	Bank of China		Banks
37	53	Sinopec		Oil & Gas
50	41	China Life Insurance		Life Insurance

A few comments:

- i) China has three companies in the major world companies in Marketing Capitalization Ranking, although the positions changed if we compare with Table 4. But for the *FT Global*, Petrochina maintained the 2nd row.
- ii) China Mobile jumped from the 16th to the 5th, but it is a HK player;
- iii) In the banking sector, only ICBC is represented, as number 5, up 3 positions;
- iv) Other Chinese companies are: two banks in 20th and 26th, one Insurance Company and Sinopec (Oil Sector).
- v) The USA have five companies in the Top 10; Citigroup¹⁸⁶, the biggest drop, is now the 53rd, when was last year the 4th.

Now we go to a specif sector, the financial sector:

186 In Table 4 was the 9th.

When preparing the latest revision I decided to show up, for March, May and June the **Financial Institutions Capitalization Rankings, to get a dynamic view**. The situation was impressive: China was represented with 3 companies in the top 5 places, being always ICBC the top one, and seeing just during the period, two of the Chinese institutions, China CB and Bank of China going up one position each, to 2nd and 4th positions. It is visible the consequences of June equity downtrend, with Market Capitalization decreasing.

Table 8. International Market Capitalization Ranking (€1000 Million)

Rkg/Companies	Countries	Market Capitalization				
		March, 31 st 187	Rkg	May, 21 st 188	Rkg	June, 18 th
1. ICBC	China	175 341 000	1	179 700	1	162 600
2. HSBC	U.K	123 769 000	3	127 900	3	123 500
3. CCB	China	111 632 000	2	134 600	2	125 500
4. Bank of America	USA	106 524 000	5	97 900	6	81 400
5. Bank of China	China	100 885 000	4	103 600	4	95 700
6. JP Morgan	USA	92 277 000	6	92 300	5	86 900
7. B. Santander	Spain	78 929 000	7	86 200	7	75 900
8. Citigroup	USA	70 541 000	8	72 600	8	71 400

Chinese Foreign Exchange Reserves¹⁸⁹ – Jumping Accumulation Process

The Foreign Exchange Reserves were, in June, 2007, over USD 1 300 000 million, mostly in USD. But afterwards, there was a changing in the policy and actions were taken under this new strategy. Wu Xiaoling, the Deputy Governor of the People’s Bank of China, informed the Chinese press, the China Securities Journal, that the Authorities would increase the reserves in Euro, considering the currency’s stability and growth in Europe (the figure presented was about € 892 000 millions).¹⁹⁰ The intention was to make it without decreasing the USD percentage¹⁹¹, roughly about 70% of the global amount. The growing devaluation of the USD is conducting China to financial losses. At the end of 2007 the foreign exchange reserves were: USD 1 528 200 million¹⁹², and in March 2008, already over USD 1 680 000 million.

187 Bloomberg: *Financial Times*, (2008), May, 13, P.15. Financial Institutions.

188 Bloomberg: *Financial Times*, (2008), June, 7-8, P.3. Financial Institutions.

189 See point 5.

190 Oje, (2007), June, 4th, 2007 and Xinhua.

191 We already saw in Table 4. the Chines investments in US securities.

192 <http://www.chinability.com/Reserves.htm>, (March, 8, 2007). Source referred by the site: State Administration of Foreign Exchange, People’s Republic of China.

Look at the impressive evolution:

Table 9. Foreign Exchange Reserves (USD Million)

	Evolution January.2004 – March.2008					
	2004	2005	2006	2007	2008 (Feb.)	2008 (Mar.) ¹⁹³
Jan.	415 700	623 600	845 200	1 104 700	1 650 000 ¹⁹⁴	1 680 000 ¹⁹⁵
Jun.	470 600	711 000	941 100	1 332 600		
Dec.	609 900	818 900	1 066 300	1 528 400 ¹⁹⁶		

Some more remarks:

In November, 2007, there was a significant pressure on realignment, especially by the G-20, who met at Cape Town. As a result, several statements were issued mentioning that:

- G-20 expected to offer resistance;
- The USA-China trade gap reached USD 23 800 million in October alone.
- *Eurostat* reported a 13-nation Euro area's trade gap with China reaching USD 70 000 million.
- China was firmly resisting any move upward;
- Asian neighbors could suffer from a stronger Yuan, (for example a stronger Yuan would mean weaker rupee, leading to the rise of imports from China, and then inflation pressure);
- A weak dollar is a "real problem" for Europeans, explained by the loss of confidence in the currency since there was concern about the US possible economic slowdown;
- A strong Euro was considered a problem affecting European exports.
- Prices and economic growth were viewed as China's main goals;

193 Foreign Reserves and Oil Reserves - It is interesting to follow the internal debate in China about eventual use of the Chinese foreign reserves. Xinhua, on June, 1st, was opening the file: "(...) China had foreign exchange reserves of \$659 billion as of the end of March. Some economists have recommended that China diversify its reserves, which are still heavily weighted in U.S. dollars. In March, Guo Shuqing, director of the State Administration of Foreign Exchange, **suggested China could use some of its foreign exchange reserves to purchase (imported) oil**, (...). China already plans to build a strategic oil reserve, though this plan is believed to be making slow progress.(...) in http://news.xinhuanet.com/english/2005-06/01/content_3029036.htm.

194 February figures, from Financial Times: *Financial Times*, (2008), April, 5-6, p.2.

195 Figures from: <http://www.iht.com/articles/ap/2008/04/11/business/AS-FIN-China-Foreign-Reserves.php>

196 The site of SAFE shows USD 1 528 249 million for December, 2008. Source: http://www.safe.gov.cn/model_safe_en/tjsj_en/tjsj_detail_en.jsp?ID=303030000000000000,16&cid=4

- “Keeping its exports machine humming provides jobs, and underpins the legitimacy of the Communist regime in Beijing but this instinct also competes with China’s desire to maintain its prestige in the world. It worked hard to get into the major multilateral organizations, notably the World Trade Organization, and fights efforts to isolate it in other institutions like the United Nations”.¹⁹⁷

Some relevant actions:

- The President of the European Central Bank visited Beijing, on November, 27, 2007, to pressure a more flexible exchange rate;
- The U.S. Treasury Secretary Henry Paulson Jr. and Bush cabinet members visited Beijing for another round of the “strategic economic dialog” which started last September, 2007.
- The President of the European Union, Prime Minister José Sócrates, informed the media that this theme would be focused in Beijing in the next meeting China – EU.

Besides all these political messages we can see that during 2007 the People’s Bank of China was not going to accelerate the revaluation of the yuan (about 5% since 2005). And another (ironic) sign:

The American Chamber of Commerce in China, (AmCham) was against the pressure on yuan, and in a White Paper presented at the 2007 China Trends Conference in Shanghai, urged the US government to stop putting pressure on China to revalue the RMB, explaining:

“(…) China’s steady reform of its banking and overall financial infrastructure is considered key to the full integration of China’s currency globally”. The full global integration of China’s financial sector and the enforcement of protection of intellectual property rights are also believed to be crucial factors contributing to the long-term and sustainable growth of the two countries’ economies, the chamber noted¹⁹⁸.

Other ideas presented in that document were:

- The important progress China has made in reforming its capital market.

197 *International Herald Tribune*, (2007), November, 17-18, pp 1,16.

198 [Http://cs.xinhuanet.com/english/ei/200706/t20070611_1121203.htm](http://cs.xinhuanet.com/english/ei/200706/t20070611_1121203.htm), (accessed on June 11, 2007).

- The deepening of the reforms to further open the capital market in China would allow for the removal of capital controls and enable China to adopt a market-driven, flexible rate regime.
- China's rapidly expanding economy and liberalizing markets have revolutionized international business.

Another topic is the Exchange Rates and Asia. In an interesting book¹⁹⁹ Günther Schnabl defends China's role as a regional stabilizer, saying that "Despite these fluctuations in the yen/dollar exchange rate, China has assumed the role of a natural stabilizer in the increasingly integrated East Asian region, with the "highest growth in the region, for the last two decades, but it has been also more stable than in any other East Asian country. (...) The People's Bank of China also eased the austerity policy, which has been adopted in 1993, by pressuring the state banks to extend credit for the construction industry, exporters, home purchases and infrastructure projects as well, as to the struggling state owned enterprises".

So he foresees that China and PRC will play the role of region stabilizer, pressing state owned businesses to ease the credit flows to different levels of clients.

We can not forget the Stock Exchange game as one of the most dynamic financial mechanisms, another recycling process, with its refinancing capabilities as well as growing potential risks:

China and Its Bubble Stories²⁰⁰ – Risky Future²⁰¹?

Let us see, first of all, what happened during the first half of 2007. The first crash was in February, 2007, but in May the CSI 300 (composite 300 hundred biggest companies in Shenzhen and Shanghai markets) fell 7%. Again the stock markets have recovered after those two main slumps, caused by the stamp tax hike on May, 29. The speculation and the signs of crash were so clear that the government decided to take measures, and the stamp tax hike was the major.

199 Ronald I. Mckinnon, "Exchange Rates Under The East Asian Dollar Standard", London, The MIT Press, London.

200 It's quite easy to understand that the Stock Exchange market is very dangerous. Let's see some other important remarks by Peter Kwong: The number of stock accounts is more than 100 million, with 27 million accounts opened since the end of 2006. "(...) Teachers, pensioners, taxi drivers, and accountants have dipped into retirement funds and mortgaged their homes to finance the frenzy known as *chao gu*, or "stir-frying stocks". "In neo-liberal Communist China, almost social welfare safety nets have been stripped away, and the middle-class is putting away its savings in the stock market, hoping to enlarge the nest egg to be able to pay for emergency medical bills, retirement, the inflated costs of a college education and the purchase of exorbitantly priced living quarters".

201 The first version was written in October, 2007, and I decided to maintain the previous analysis, adding some updates, in order to be understood the Equities Markets' dynamic view.

In June, 2007, *China Daily* published the following on the market capitalization correction:

“(...) China’s combined market capitalization slipped 1.35 percent last week to 17 trillion Yuan (US\$2.2 trillion) by the close of the last trading day, following the government’s trading tax hike²⁰² to cool the overheated economy”.

One of the dramatic signs of this threat was the number of accounts being opened to invest in the stock markets, which resorted to different kinds of mortgages, people from all conditions asking loans to pay bets.

An updated image: The first version of this analysis was written in September, 2007. Some months later we see how were confirmed the negative perspectives. Although I will not elaborate more on this issue²⁰³, (the stock exchange fluctuations), I must stress that the Shanghai Composite suffered a correction from 5 500 in January, 2008, to less than 3 500, end of March. We saw the so-called corrections, but if the trend is being confirmed as it is, a specific social unrest can be not far and difficult to solve. And with the commodities and crude oil prices “shocks”, the financial markets are very much volatile. And off course the present downturn is the result of the world problems, being the American GSE’s issue, the Fannie Mae and Freddie Mac huge problematic, and inducing wrong waves to the Chinese stock exchanges, in a global move.

State-owned enterprises, *Princelings* and Other Agents: One important point is that 80% of the Chinese stock exchange listings are state-owned enterprises restructured in the 1990’s into stock holding companies, managed by top party officials and their family members. The restructuring process allowed children of top party officials, known as the *princelings*, to take over China’s most strategic and profitable industries: banking, insurance, transportation, power generation, natural resources, media and weapons.

“*Princeling*²⁰⁴ can get loans from government-controlled banks, acquire foreign partners and list their companies on stock exchanges. Before going public, they often divvy up large blocks of shares for themselves, mid-range managers, and their families”.

202 “China raises the stamp tax on stock trading to 0.3 percent from 0.1 percent”, in *China Daily*, (2007), June, 12.

203 What should be a different approach and a need to recenter and update some topics I decided to maintain in order to stress the main fragilities and potentialities of the Chinese equity market.

204 In <http://www.iht.com/articles/2007/11/16/opinion/edkwong.php>. Also, read: http://www.businessweek.com/magazine/content/02_08/b3771021.htm.

Floyd Norris in “The bubble risk in China”²⁰⁵, after comparing the lists of the top “20 most valuable companies in the world” in 1989, 1999 and 2007, showed that in 1989, Japan dominated with 14 companies, (four banks in the top five!), with a strong participation of banks, whose profits were enhanced by their stakes in many other Japanese companies, whose shares in turn were also soaring. Japan’s bubble burst brought them down by bad loans, leading to mergers and bailouts. In the USA there was a protectionist move by the Congress “to shield American companies from unfair Japanese competition”.

In 1999 most of the top companies were dedicated to technology, software (Microsoft), industry, energy, telecoms, and only one bank, the 14th Citigroup.

Norris says: “Only a small portion of shares in many technology companies had been sold to the public, limiting supply as investors crowded in”.

In 2007 there were 11 from the energy sector (8, and 3 from China), industry (1 - USA), finance (7, with 4 from China, 3 banks – ICBC, 5th; China Construction, 17th; Bank of China, 20th, and one insurer - China Life, 12th). The other banks are HSBC, 13th; Citigroup 14th, and Bank of America, 15th).

There were only three U.S. companies: General Electric, Exxon (merged with Mobil), and AT&T.

But the most important is to look at China’s present status:

- The parallel with the concern showed by the American politicians (and European, we add), on China’s trade surplus, “and Chinese companies profiting from owning stakes in other companies whose stocks are soaring”.
- The limited number of shares available for investors to buy, and “with most shares controlled by the Chinese government”, the stock prices were pressed up.

The economy is combining inflation with speculative performances by equity markets and a strong growth rate, which forces the Chinese government to control its pace to avoid losing its own strategy. Two such measures were:

- To cool the economy, a tightened monetary policy, and a step-by-step control based on gradual increases of the so called “key-one-year” interest rate, which happened for six times up to a nine-year high of 7.47 %;

205 *International Herald Tribune*, (2007), 20-21, October, p.18.

- To absorb the abnormal liquidity generated by its huge growth, in 2007, China already increased ten (10) times the reserve requirements, up to 14.5 %.

And finally,

How China is Globalizing, and becoming a more assertive Regional Power

Before the final conclusions, it’s important to summarize the latest developments occurred in 2008 in the China’s external front. We can’t forget that getting closer to its neighbor countries, as a “peace-minded nation”, it is also a quicker way to obtain, besides political stability and better economic engagement, significant economic and financial gains. The Chinese Foreign Policy (and the economic diplomacy), combining the political agenda and the economic interests, is evolving smoothly, accelerating the progressive integration in the region as a major regional power, mainly Taiwan, (since Hong Kong and Macao smoothly joined the *Empire*), and (the *rapprochement* with) Russia, (through **The Shanghai Cooperation Organization**²⁰⁶), *re-routing* the Silk Road in a moving Central Asia, the *slow motion dialog* with the “long term enemy” Japan, (and also the race into Africa and South America²⁰⁷). So look at the latest developments:

China and its Effort in the Foreign Policy Area

Early 2008 came with significant political and economic (bilateral) events with diverse significant developments in different fronts:

Russia: 1. On May, 23rd, the new Russian president Dmitry Medvedev visited China, taking the occasion to join Chinese president condemning USA plans for a missile defense shield, and “warning that it could upset the world’s

206 A long term agreement, since China and Russia formed in 1996 the “Shanghai Five”, (including besides both countries, Kazakhstan, Tajikistan and Kyrgyzstan), admitted in 2001 Uzbekistan. Up to July 2005, the main concern was the regional security. The support by “western countries” of Georgia and Ukraine and action of the Uzbek government took the organization to a different level of cooperation. A joint statement in July 2005 and the military exercises carried out in August, sealed the agreement. As observers, came to join in July 2005, Mongolia, Iran, Pakistan and India. Main areas of cooperation: Energy Policy, (to settle down Russian energy companies in China, the promotion of bilateral projects with supplying energy to third parties, and the no less important delivery of Russian oil and gas to China; but China worked also with Kazakhstan to settle a new pipeline out of Russia frontier/control), Arms sales, (Russia was exporting over 80% to India and China, being Iran another good client); Demographic File (mainly to control the illegal immigration from China into Russia), and a General Economic Interaction. (See reports on this matter). These areas explored are not developed, since that’s not my main topic of analysis. What its clearly shown is the relevancy and complexity of this theme, and how important it is how China will deal with it. **And to show up that Central Asia will be more and more a geo-strategic hot topic.**

207 This theme naturally deserved a more specific analysis, (I am writing another text, but not included in this book). Speaking about South America, where some country’s regimes, being out of the US’s area of influence, are presently more open to the Chinese approach.

strategic balance”²⁰⁸. 2. The International Economic Forum of San Petersburg in June, 7, where Medvedev attributed the responsibility for a “world crisis” to the USA. and expressed his will to transform Moscow in powerful financial center. 3. The Russian Duma²⁰⁹ menaces to abandon the Friendship and Cooperation Treaty signed with Ukrain if it is going further in its road to join NATO. The other source of uncertainty is the hot present relationship with Georgia, about the separatist region of Abkasia. Besides this, the Russian PM, Medvedev visited²¹⁰ Berlin in its first visit to Europe. Finally the statement putting Russia as the 6th world largest economy by the end of 2008, as per words of the Russia’s First Deputy Prime Minister Igor Shuvalov at the 12th St. Petersburg International Economic Forum²¹¹. There will be an Economic Forum Finland-China-Russia in October, 2008.

4. When on July, 8th, the U.S. secretary of state Condolezza Rice signed in Prague a missile-shield agreement, the Kremlin response was a sudden reduction of about 15% in oil deliveries to the Czech Republic, explaining with “technical reasons”²¹².
5. Signaling the “end of demarcation work of the 4,300-km Sino-Russian boundary”, China and Russia signed July, 21st, an agreement solving a problem coming from 1929 when Russia occupied, during border fights, two islands: the return to Chins, of the Yinlong Island (Tarabarov Island) and half of the Heixiazi Island (Bolshoi Ussuriysky Island). Act signed by the Chinese Foreign Minister Yang Jiechi and the Russian counterpart, Sergei Lkavrov.
6. The same day Russia announced that Premier Vladimir Putin will be present in Beijing Olympic Games.

Total Trade China-Russia (2007): USD 48 000 million - China is Russia’s second largest trade, after the EU, being Russia the China’s eight partner.

Japan: 1. The Chinese President Hu Jintao visited Japan in May, being received by PM Yasuo Fukuda, the first visit of a Chinese leader to that country in a decade, both agreeing to hold regular summit meetings, so as to maintain

208 *Financial Times*, (2008), May, 24-25, 2008, p.5.

209 Resolution approved by 408 against 5 votes on June, 4th, 2008. Iulia Timochenko, Ukrain PM criticized the radical decision.

210 On June, the 5th, 2008.

211 http://news.xinhuanet.com/english/2008-06/08/content_8327846.htm(accessed on June, 9, 2008).

212 *International Herald Tribune*, (2008), July, 15, p.3. The eventual retaliation was not a real trouble, since the Czech Republic had diversify during the 90’s its energy sources, purchasing from the TALIKL pipeline, a Mediterranean way.

“civil and military exchanges”, and “talks on furthering strategic mutually beneficial relations”²¹³, but not solving²¹⁴ at that time, the dispute over gas resources they have in the East China Sea. 2. When Japan was going to provide help sent by air force cargo’s, China didn’t accept it. Later gave a green light. 3. Japan/Africa: Japan hosted in May a get-together with 40 African leaders, showing its efforts to get a better access to the African natural resources. A true competitor?

Total Trade China- Japan (2007): USD 236 000 million; Japan has been for 11 years China’s biggest trade partner, and became China’s biggest exporter and its fourth main market. In 2007, China was Japan’s biggest trade partner.

Taiwan: as soon as the Kuomintang won the legislative and the Presidential elections, and since the pro-independence moves were put aside, we can point out some signs of opening will:

1. On May, 28, 2008, the official visit to Beijing of Wu Po-hsiung²¹⁵, the chairman of the Taiwan’s ruling party, the Kuomintang, meeting the Chinese president Hu Jintao, agreeing to resume bilateral talks, with no evolution for a decade. Hu Jintao words: “Communication and dialog between the mainland-based **Association for Relations Across the Taiwan Straits (ARATS)** and the Taiwan -based **Strait Exchange Foundation (SEF)** on the basis of ‘1992 Consensus’ should be resumed as early as possible”²¹⁶. 2. Following that visit, the first official meeting since 1999, took place on June, 12, 2008, in Beijing, with the agreement for regular non-stop charter flights²¹⁷, an increase in bilateral tourism and more talks. 3. Some measures were taken to reinforce the “will”: The Taiwan’s parliament approved legislation legalizing the renminbi on the island, the same day, and the Taiwanese authorities announced, in order to “facilitate Chinese travel to Taiwan”, they were preparing to allow banks, eventually in July, to exchange renminbi for local currency.

Now we can see that besides the either “direct” or indirect²¹⁸ trade and investment business, finally there’s a mood for a wider and closer relationship. George Tsai, (the same FT): “In Taiwan the majority hopes to keep the status-quo, while China hopes, through closer exchanges, to create a trend that would

213 http://news.xinhuanet.com/english/2008-05/07/content_8121991.htm, (accessed on June, 9, 2008).

214 What apparently happened weeks later.

215 Since 1949 not such high-ranking visit from Taiwan to Beijing.

216 China Daily/Xinhua, May, 29, 2008, updated at 07:34. Accessed on the same day.

217 Previous flights were through Macao or Hong Kong.

218 So: “The agreement ends a decades-old ban on direct flights across the Strait that had imposed additional costs on millions of Taiwanese, the biggest foreign investors in China”. FT, (2008), June, 13, 2008, p.4.

eventually result in unification”²¹⁹. But, it will take time to be a total free and open interaction, at political level, in a chess table where the USA will have a word to say with their regional influence.

Finally, if we pursue focusing more in the eco-financial side, mainly about trade and investment, these facts can represent a good step to the improvement of bilateral business, strengthening their links and supporting future moves.

Total Trade China-Taiwan (2007): USD 102 300 million, (Surplus for Taiwan of USD 46 260 million, 20% more). China is the main Taiwan’s trade partner, making economically more dependent on China.

Regarding **Taiwanese FDI**²²⁰ **in China**: \$ 9 970 million in 2007.

Latest but not the least, the Korea’s. One day before receiving the KMT chairman, Hu Jintao hosted the visit of the South Korea’s president, Lee Myung-bak, agreeing to upgrade their “comprehensive and cooperative partnership” to “strategic cooperative partnership”, in what seemed to be, for China not only a words’ game, (and giving some room to explore the North Korea issue, where China participates in the “six-party talks”).

It’s impressive the trend of the above mentioned bilateral trade. The future will show if these steps are (consistently) forging a new era, and if those trade partners are going to get closer, becoming members of a real “community” or if there will be reasons to foresee the eventual creation of new barriers among them.

8. Conclusion

The financial world is, presently, a quite complex and sophisticated puzzle where the political, financial, economic winds and gestures evolve in a more and more quickly *metamorphosis*.

The international financial environment will show consecutive corrections, cyclical downgrades, periodic fears, losses of confidence, affecting the equity markets, and wider “universes” of world population. Then, the speculative moves will take place, since the crisis era’s always have their episodic predators. From the financial crisis we step into a wider economic crisis, corresponding to a stagflation status, (the market regulators will be defining policies, and decid-

219 Financial Times, (2008), June, 13, 2008, p.4.

220 In <http://www.taipetimes.com/News/biz/archives/2008/06/02/2003413558>. Quoting from the Taipei Times: “(...)Since 1991, approved Taiwan investment in China has increased by a factor of nearly 60, standing at US\$9.97 billion last year — tensions notwithstanding”.

ing the rates, having a hard choice to fix the medicines, between inflation and growth), there are doubts if the emergent economies will be strong and sound enough to compensate the negative effects.

China is nowadays in a different position facing the global scene, if we remind how has found its own way during the 1997's *Asian crisis*. Acting against the market forces and growing pressures China has resolved the difficulties, avoiding the major impact, and has developed a positive role in helping other countries stepping out of crisis. At that time, China was much more isolated, much more in its own way, using its own forces, its own energies.

In 2001, China's accession to WTO led to a much more open China, (more in its external relations, considering its financial placements and investments in the international financial markets). If China has won a different political and economic posture, simultaneously became much more integrated in global finance and exposed to the present high volatile global framework. With plenty of liquidity, it is going out to buy a great variety of assets. On a different layer, due to its huge need of natural resources, it has focused its attention (and appetite) mainly towards Africa and Latin America. And as explained, the recent (foreign policy) moves in the International Arena, will take sooner or later positive consequences.

There will be a very important mega-test for China, as a matured, pacific, responsible and (politically) integrated country. The Beijing Olympic Games, (to take place in August, 2008), will be a worldwide media event under intense scrutiny. I foresee three phases: the 1st with a gradual increase of pressure from the "public-opinion", an escalate of atomized political manifestations, the "western governments" divided in their reactions, much more in a symbolic sense than in an effective way, (for instance - channeling their discontentment to concrete attitudes - regarding their presence in the Opening Ceremony). The cause of Tibet was the first case, to make it happen. In my opinion, though, in general countries will not be hostile towards China, avoiding sending it out of the global (consensual) game. In the 2nd phase, (not so strong, because of the disasters, like the earthquake), ONG's and other Institutions will be more active, resorting to different sorts of actions to pressure the Country under the Human Rights' flag. In the 3rd phase, closer to the date of the event, the pressure will be strong and the atmosphere can be more dramatic, because China feeling the pressure will direct its critics against "anti-China" hostile groups. So, China has to deal with this issue with great flexibility, with open-mind decisions, (assuring its internal security as other matured democratic players), but showing real interest in opening the country, respecting the HR file. Otherwise, it will

be difficult to manage the complex situation. And this will be a great event, followed second-by-second by all kinds of means of communication, mobiles (i)phones, media, television stations, and so on. Like in a giant *you tube*, millions of viewers will be on-line watching China!

But above all, we (can) understand the majority of countries are not interested in opposing China, since that behavior should result in forcing (or pressuring) China out of the global scene, which should be dangerous for the “western political and economic wishes/interests”. Some “competitors” will use its own weapon: prosecuting the engagement strategy, making business above all and avoiding reading the facts through the real colors of reality

As we could see (point 2.), China’s economy, although becoming stronger, has deep problems to solve. First of all, (an irony for so many countries all over the world intensively fighting to get 2 or 3% as growth rate), it has clearly been unable to control its own path of growth. The recent smaller growth can be just a reflection (the result) of the global slowdown. And that evolution is made with a visible waste of resources, an accumulation of closed production units, (abandoned in erratic processes of changing production targets), and a disorganized industrial texture. Because there is plenty of means: capital, work force, foreign interest, and volatile markets. That is creating higher and higher inflation pressures, feeding a significant unemployment rate, painting in gray colors the marvelous Chinese landscape and atmosphere, and eroding huge financial needs.

Lately, the Chinese political framework established two main streams of ideas:

- the target as an Harmonious Society, Confucius-type society;
- the Scientific Development Concept, meaning, in a few words, development with social concern.

Then, at this stage of our analysis, I foresee how the financial system is the core sector for China’s future, since will always simultaneously be, the engine of economic growth and the recycling machine (investment and exports variables are filtered through its systematized structure), and finally, if well managed, the crucial mechanism to resolve the social and regional disparities [we saw the worst Gini Coefficient and analyzed the different kinds of asymmetries: east-west regions, rural-urban population, (elderly) active population, social network and so on].

The banking system must recycle the country’s heavy domestic savings, correctly re-direct them to the economy, but making them available and useful to the population’s most important needs (education, health, and a sensitive

social and retirement scheme) and to the modernization of the infrastructure, as well as other major public works, and finally to the pressing needs of China’s increasing climate change and its consequences.

This is a country where the financial system is much more oriented by the government (and the party), than by the market forces.

Globalization offers opportunities, but at the same time generates multiple risks, as we could see around the world with the *subprime crisis*, and the present energy-commodities shock! Noteworthy also is the close relationship between China and the USA, not only under the WTO surveillance, but especially in terms of the inter-penetration of markets and objectives, (v.g. China invested huge amounts in Treasury bonds and the USA is a very important partner for external trading, so as are quite relevant both markets). Two major power engines in our world in financial turbulence.

When the world is sinking troubled waters, suffering finance and economic shocks, (eventual longer term financial crisis combined with commodities and crude oil pressure on prices resulting in higher inflation; minor growth; increasing unemployment, accelerated by globalization’s direct sequels), China is calmly going further:

- a) Distending the regional tensions, assuming its role as a regional superpower, a “peace-mind” country offering its warmful hand;
- b) Trying to build a better image to the world as a “responsible player”, through:
 - bi) The Olympic games’ operation, (dispite the HR and Tibet issues);
 - bii) The global “prompt” and “responsible reaction” to the natural disasters;
- c) Securing the economica and financial needs (and wills), mainly through two ways:
 - ci) Natural resources: in Africa, Latin America, Central Asia, and spreadind out it arms around the world.
 - cii) Investments: financial takes in American, European, (and other targets) groups or companies, assuring the consistency of a rich, an inteligent and a powerful global player.

So, one of the most important issues in the future is the financial China. The Chinese Sovereign Fund, the China Investment Corporation, has been founded and may experience the hardships of market going down, considering its investment in Blackstone and others American targets. China will be under pressure to show its intents, under the global debate on the need for a code of

conduct for SWF's activity. But even here what seemed to be a winning career for this huge investment vehicle, is becoming a national competition: CIC, or China Investment Corporation has to prove to be better managed than SAFE, the powerful State Administration of Foreign Exchange, which will make it more difficult (for a Sovereign Fund) to be independent and clearly diverted from the national political power.

China's financial system is only partly open to foreign institutions, since participation is only allowed on a very restrictive basis. This restriction is visible not only in the way operations are approved or the cap on foreign participation in eventual joint ventures, (although its raising is expected to occur sooner or later), but also in its very demanding standards, (minimum amounts, investments by branch, and so on).

The banking system is financing under government decision-making, (even political direction) giving support to fragile SOE's or securing political projects that don't fulfill all the strict credit criteria. Although we can easily understand that the government has to resolve social problems, it must manage a more matured financial framework.

Another concern is the fuel the system is providing to securities' markets, financing the highly volatile stock exchange (bubble). China's stock exchange had recovery capacity, but in a global negative financial environment it could break down, (and already came heavily down), which may (soon) lead to dangerous levels of (poverty and) social unrest.

Besides that, the environmental problems are so many and of an enormous dimension, with such a negative impact, that China has to take action to improve its practice and to implement a new corrective and more efficient energy-policy. This means to recycle more and more financial means to invest in important funds to correct the situation. Major financial institutions should sponsor environmental projects, in order to improve the population's quality of life (and preserving important resources of something as simple as the water). As mentioned before, China has to deal with the issue of energy, shifting to the alternative sources, and developing cleaner options.

A major issue: credit quality is still bad in this banking system, the old NPL's, sold to the AMC's are still unresolved. The system is not yet clean. It is important to strictly follow the international standards on Capital Adequacy Ratio (prudential regulations), taking due care of the solvency, and soundness ratios.

The financial system has still to deal with some areas:

A. The financial system must be more accurate in its supervision, (Ministry of Finance, Central Bank, Regulatory bodies like the China Banking Regulatory Commission, or the China Securities Regulatory Commission). There should be a real regulator for the booming opportunities being generated (from stock exchanges to financial projects, passing through the industry texture).

B. There should be a more transparent and better managed banking system, (good governance, good practices, technical expertise and highly professional personnel):

- the asset portfolio must be cleaned up, solving the problematic issue of the NPL’s;
- the banks must be well capitalized;
- banks must be treated as other agents of the market ruled by market forces (and the financing machine for (mainly) the state owned companies.

C. Economic and financial agents, banks, companies, and others must be prepared for the competitive market(s) which soon will become the rule in terms of business, instead of present government protectionism or exaggerated orientation.

Plenty of challenges are coming and it is crucial that the financial system becomes modern, that the markets become really open, in a more reciprocal way (and posture), though regulated, with high professional technical skills and under straight supervision. Risks are evolving and other Grey areas are appearing (like a mutant mechanism-alive).

China is a different dimension (in terms of space, time, culture, history, complexity) and it will regain its Dragon-Size-dimension. However, it is also pressured by all the fragilities that being a giant implies. The world will accommodate the China’s growing power, depending on the country’s the correct use of its virtues.

Finally, the future will show us how smoothly these two factors will be integrated: the China factor and the World factor (mainly within the global financial framework). China’s success will be the result *of the mismatch* of social-political and economic-financial spheres and the way China will deal with them.

Energy and China's Geo-Economic Dilemmas

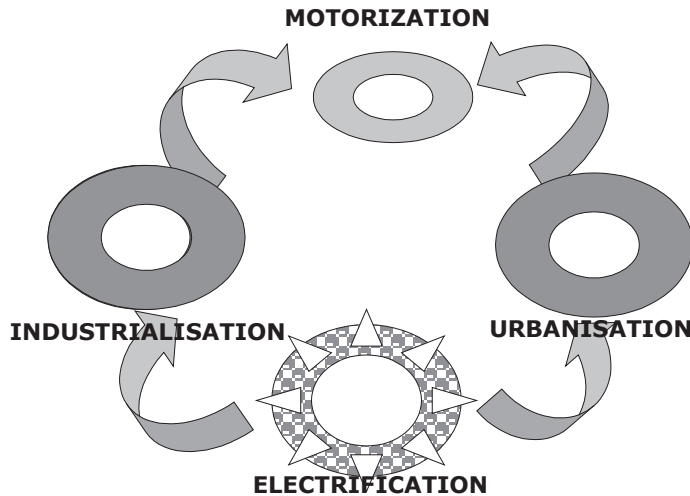
José Félix Ribeiro, Fátima Azevedo e Rui Trindade

When analyzing the development of the role of energy in Chinese economic growth in the past twenty years, three conclusions may be drawn:

- In 1994 China became a net importer of oil and since then, its consumption has maintained a sustainable growth turning it into the world's second biggest oil consumer, after the United States
- Over a long period of time, China accelerated its growth and at the same time reduced its energy intensity by redirecting its industry to sectors that are less energy-consuming and more orientated towards exports; this phase of Chinese growth coincided with a period in which oil prices were even lower than before 1985
- Since 2001 the rapid growth in China has been due to very strong investment and exports of heavy industries which are more intense in energy; this process is still ongoing and coincided with the worldwide rise in oil prices.

The rapid growth of energy consumption in China is based on three key processes – **industrialization, urbanization and electrification** and more recently, **motorization**, which is stimulated by industrialization and urbanization as illustrated in Figure 1.

Figure 1. Processes That Explain the Growth of Energy Consumption in China



This paper will not look at issues related to energy from a macroeconomic point of view but rather from a two-fold geo-economic perspective:

- energy as a sector that will cause a series of problems to the “geo-economic unity” of China;
- energy as a sector that will put China in difficult decision-making positions regarding its preferred external relations

To conclude, we will present **four different scenarios** that demonstrate the **different ways China can try to solve the problems that it faces at these two levels.**

We will start by the internal component, analyzing the geographical distribution of agricultural, industry and energy activities.

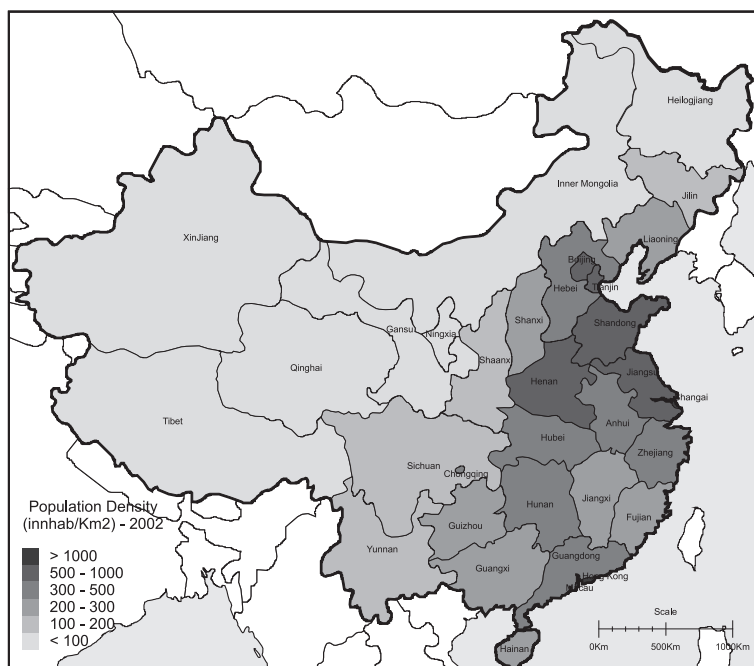
1. Industry & Agriculture – The Four Chinas

Maps I and II allow us to divide China according to the weight of agricultural and industrial activities in four main macro regions:

- An essentially agricultural China covering the majority of the territory (corresponding to the two shades of green) with significant importance in the most populated areas of the center and south of

- the country namely Sichuan, Guizhou, Hunan, Jiangxi and Anhui which are rich in water;
- A highly industrialized China, located along the coast (corresponding to the two shades of red) which may be divided into three distinct sections – Guangdong in the south; Zhejiang, Shanghai and Jansu in the center and Shandong, Tianjin and Liaoning in the North and Heilongjiang (this province is located on the northern frontier of China)
 - There is also an intermediate China that combines agricultural intensity with the presence of industry although with a much lower percentage than the coastal regions (corresponding to light brown and yellow shades) which includes the northern provinces like Hebei and Henan, and in the center in the surrounding area of Yangtzé as for example, Hubei;
 - a China of the Capital – Beijing – essentially present as a service metropolis

Map I. China: Population Density (By region)



Map II. Agricultural & Industrial China

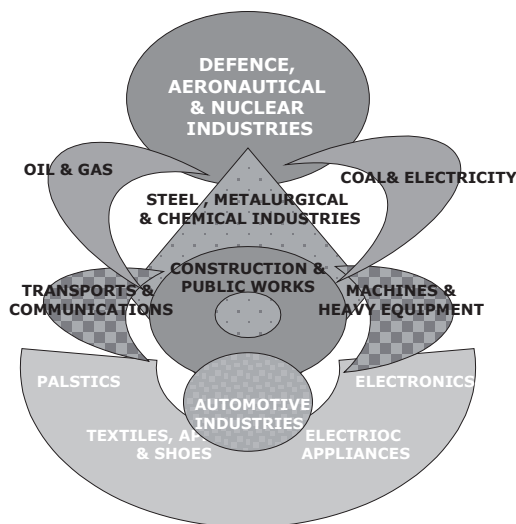


Insofar as the industrial sector is concerned, we can say that there is a Northeastern China (including the Yellow River basin) with heavy industry focused on its internal market; the China of defense and energy industries, and a coastal China that exports consumer and intermediate goods.

In terms of exported goods, three main economic areas may be found:

- A central area that includes Shanghai and the provinces of Jiangsu in the north, and Zhejiang in the south, which make up the most diversified industrial area of China – including heavy industries, current consumer goods, durable consumer goods and electronic industries;
- A Southern area in Guangdong organized around electrical appliances, electronic devices and textile/clothing industries;
- A Northern area around the Bohai Sea where there is a huge concentration of heavy industry, but in which Peking stands out for its electronic industry and Shandong specializes in the electric appliances and textiles industry

Figure 2. China: Heavy and Light Industries –From State to Private Firms,
From Domestic Market to Exports



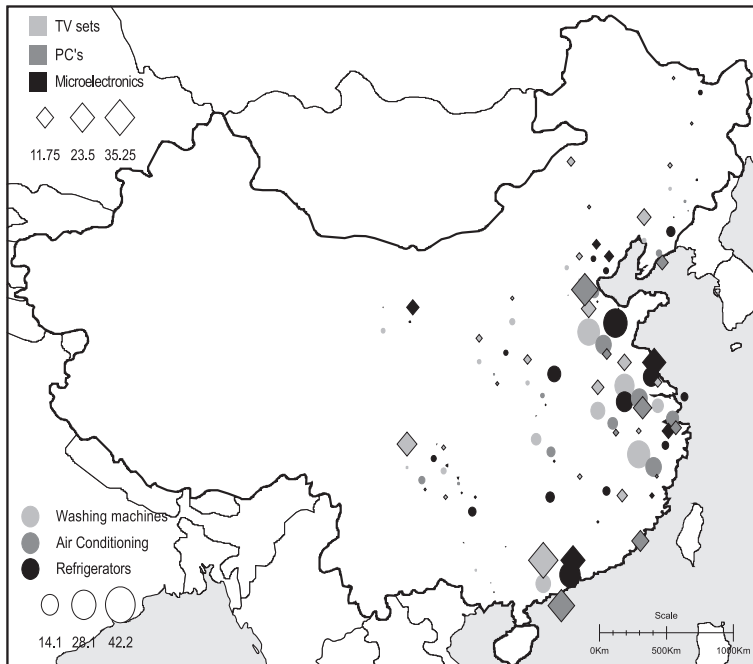
A closer look at four main groups of the **core of the industry sector** - Defence Industries, Aeronautics, Space and Nuclear; Heavy Industries (steel, machine and automobile production), Consumer goods production Industry (textiles, synthetic fibers and plastics), durable consumer goods production industry (washing-machines, refrigerators, air-conditioning) and electronic industries (microelectronics, micro-computers and television equipment)- lead to the identification of four distinct situations:

- Defence, space and nuclear industries are distributed from the Peking area to the inland regions
- Heavy industries are distributed throughout all of the territory, although they are mostly concentrated in the North and Northeastern coast, (Map III)
- The consumer goods production industries are essentially located in the Northeast and Eastern coast, even though there is greater textile production in the inland provinces which share border with coastal provinces;
- The domestic electric appliance and electronic industries are strongly concentrated on the Eastern coast rim. (Map IV)

Map III. China: Heavy Industries



Map IV. China: Electric Appliances and Electronic Industries



One of the main factors for China’s macro economic growth after 2001 was the change in growth factors in favour of internal investment, especially in the heavy industries and public construction works (which later determined the orientation of heavy industry to external markets as a way of managing overcapacities that were a result of that investment boom).

One of the main factors which triggered this investment boom was the expansionist monetary policy prevailing after 2001 (with the Chinese almost unchanged rate of exchange against the US dollar) which inverted China’s tendency to reduce energy consumption and made the Chinese economy more vulnerable to the increase of oil and gas prices. On the other hand, the productive structure of the more developed regions became more complex as each tried to adjust or readjust itself (if their facilities were obsolete or insufficient to correspond to demand) investing in heavy industries and so trying to make their growth less dependent on other regions.

2. Energy – The Other Four Chinas

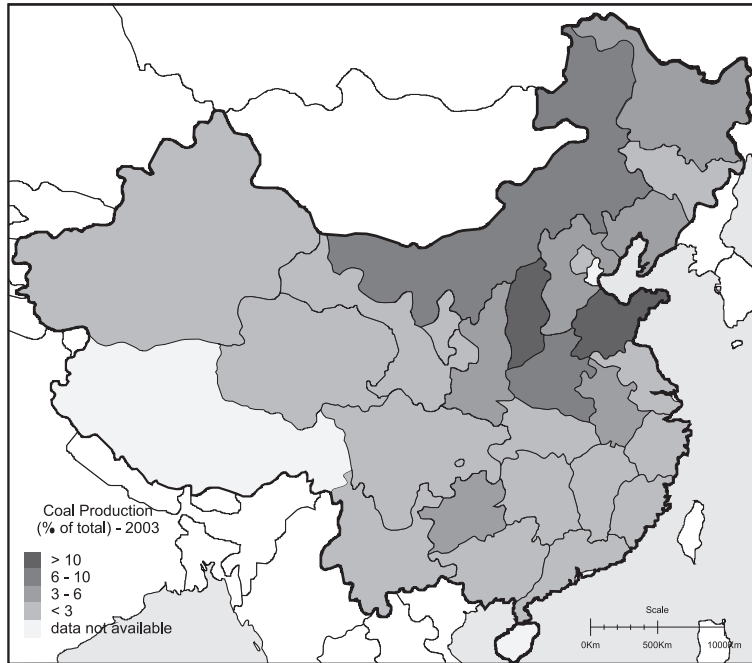
In China today, despite the varied resources of coal, oil and natural gas and the use of hydric resources, domestic offer is manifestly insufficient to answer the high growth rate of energy demand.

Insofar as oil is considered, the main reserve regions are located in desert areas and offshore (currently in front of the province of Guangdong and in the Bohai Sea).

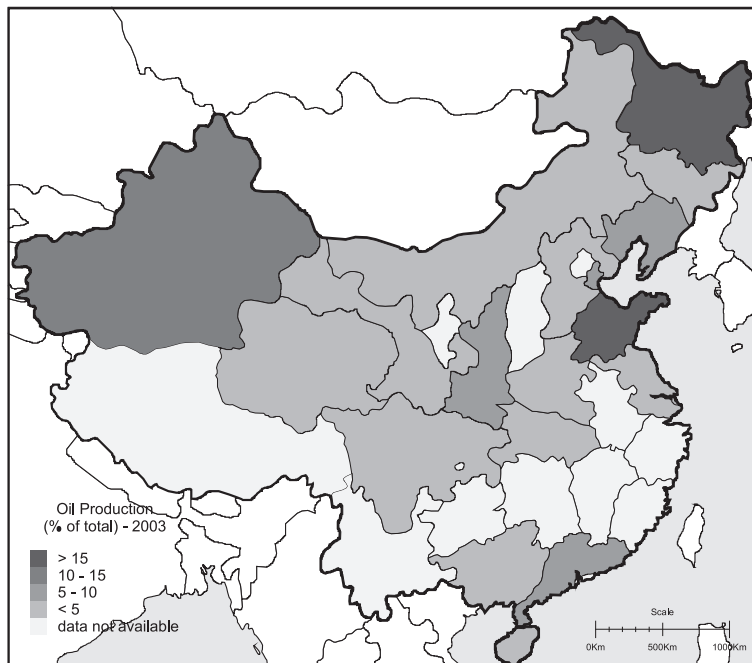
If we associate this geographical distribution to the production of oil, coal and hydro electricity, **four main regions** may be identified: (See Maps V and VI)

- a Desert China, with plenty fossil energy;
- a China of the Yellow River, more prosperous and with fossil energy;
- a Central and South China, with plenty hydroelectricity;
- a Coastal China which is the driving force of China’s development and which lacks primary energy reserves and production

Map V. China: Coal Production



Map VI. China: Oil Production



The province of Sichuan is unique for its production capacity of different types of primary energy.

The energy deficit has made the authorities try to change the structure of the energy sector not only by means of making consumption more efficient, and intensifying the exploration of internal resources, but also by means of the constitution of strategic reserves and the internationalization of state energy firms

3. Internal Dilemmas: The difficult geo-economic unity of China

Based on what has been previously analyzed, the following conclusions may be drawn:

- China's growth and prosperity have been based on the shift to the exports of consumer and intermediate goods by provinces that are part of two coastal areas: the Coastal Ring and the Bohai Ring; recently, heavy industries of both these regions have begun to export more intensively;
- In terms of the value chain, a very significant part of the light export industry is dedicated to the final phases of labour-intensive assembly and processing of imported components;
- Foreign companies, especially Asian ones – South Korea and Japan – and businessmen from Hong Kong, Taiwan and Singapore (“Chinese economies”) played a crucial role in the creation and expansion of China's coastal export base;
- Coastal China as a whole is integrated in a pan-Asiatic system of production for the export of final goods to the USA and Europe;
- From a geo-economic perspective, Coastal China is divided into two distinct areas with the following characteristics:
 - an area on the **Bohai Ring and The Yellow River** which face serious lack of hydric resources, abundance of fossil energy resources, the predominance of state-controlled heavy industries and limited export orientation; due to its high levels of pollution, the survival of this area in the future will depend on a massive shift to the hydric resources of the Yangtze river;
 - an area of the **Coastal Ring**, without fossil energy production but with an undefined potential of oil and gas reserves *offshore*; this coastal China easily access external energy resources by

means of its port system and can count upon a great abundance of hydric resources; this region is export oriented and open to foreign investment and investment by Hong Kong and Taiwanese businessmen;

- Next to this Coastal China lies another China that is technologically more developed, focused on the internal market and based on a military industrial complex (aeronautics, space and nuclear industries)– located along what we can call a “new wall of China”
- And a fourth China that is rich in energy resources is located in the north east and in the almost deserted western regions, far from the dynamic areas of the Coastal ring.

It is possible to conclude that, as a great continental economy, the geo-economic unity of China faces great threats resulting from its structural imbalances:.

- The China of the Coastal Ring can choose to become more fully integrated in the world market not only in terms of exports (relations with the rest of Asia and the USA) but also in its energy supply, while at the same it can rely on its hydric resources, the agriculture and work force of South China and Yangtze for its food supply;
- The China of the Bohai Ring which have clear advantages in the geoeconomic unity of China because it can access the vital hydric resources of other regions and develop their own energy potential; while still being able to continue relying on the transfer of resources for the most sophisticated, but also protected industries.

The geo-economic unity of China requires massive investment in energy and transport infrastructure by the central government while the coastal provinces can be more interested in their own industrial and technological upgrading oriented to world markets .

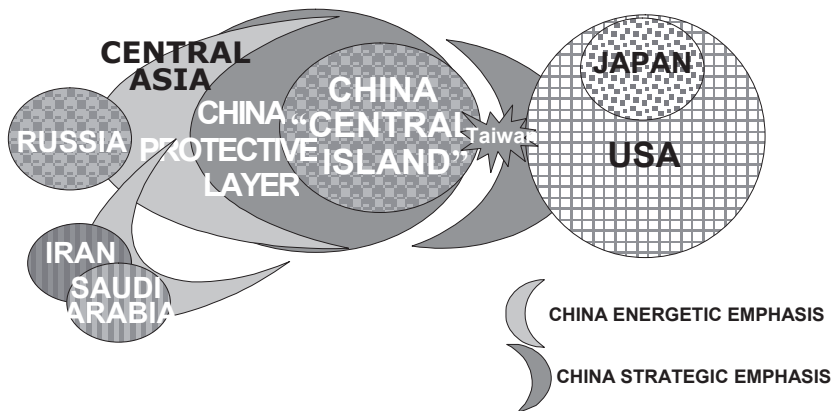
4. External Dilemmas: The dependency on extensive maritime routes

The future of China’s energy supply also poses other types of geo-economic and strategic dilemmas. In fact, to obtain its oil and natural gas China may:

- Depend on distant external sources – from the Persian Gulf to Africa – which implies resorting to extensive maritime supply routes which

- China is not able to protect directly and as such, will depend on the naval power of the USA;
- Invest in the exploration of off-shore energy resources (with the risk of conflicts with other Asian states) and in the Asia Pacific (Australia), and so, reduce its dependency on extensive maritime routes while forging alliances with international oil companies that have the required exploration and development technologies;
 - Concentrate its future supply on the Asian Continent, in the ex-soviet region – Russia, Kazakhstan and other Central Asian States.

Figure 3. Geo-Economic and Strategic Relations of China – A Vision.



5. Crossing the Internal and External Dilemmas

By crossing **the Internal and External Dilemmas** associated to Energy, four contrasting scenarios of development for China may be considered, depending on the options that are chosen to solve the two dilemmas. (see Figures 3 and 4)

Internal dilemmas

- Promoting domestic integration; reinforcing the dependency of the more outward-looking regions on the supply of energy by China's regions with plenty of coal, natural gas and oil, investing massively

in the construction of an internal network of pipelines, gas pipelines, railway lines and electricity.

OR

- Privileging global integration by reinforcing the recourse to the imports of oil and natural gas from outside the country, investing in nuclear energy for the supply of electricity to coastal regions and forming strategic partnerships with western companies with offshore exploration technology so as to develop China's coastal production, thus reducing the need for the internal investment in energy networks, while simultaneously strengthening the energy autonomy of China's more developed regions, which are located precisely in coastal areas.

External Dilemmas

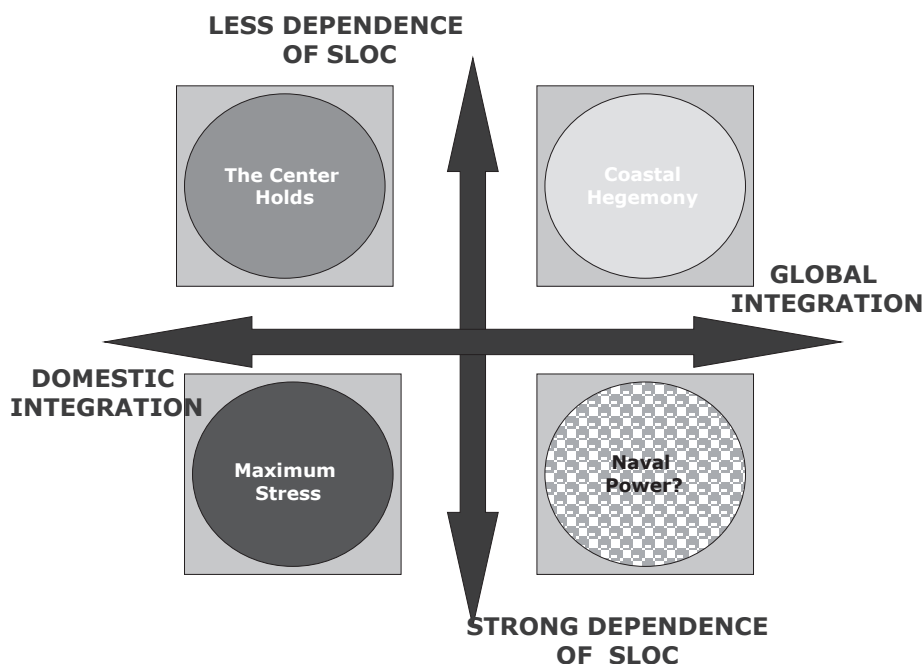
- Resorting to the import of oil and natural gas from far-off regions, but where it will be possible to establish strategic alliances with producer countries (Middle East and Africa), coming up against a strong dependency on extensive Sea Lanes of Communication (SLOC), which are currently controlled by the USA's naval power.

OR

- Concentrating external oil and natural gas supply in origins located in the Asian continent through the construction of oil pipelines and gas pipelines to Russia and to the producer countries in Central Asia, lowering the security impact of the extensive SLOC.

Figure 4 represents the “crossing” of these two dilemmas and the combination of their outline, each Quadrant, representing a different scenario.

Figure 4. China & Energy - Four Scenarios



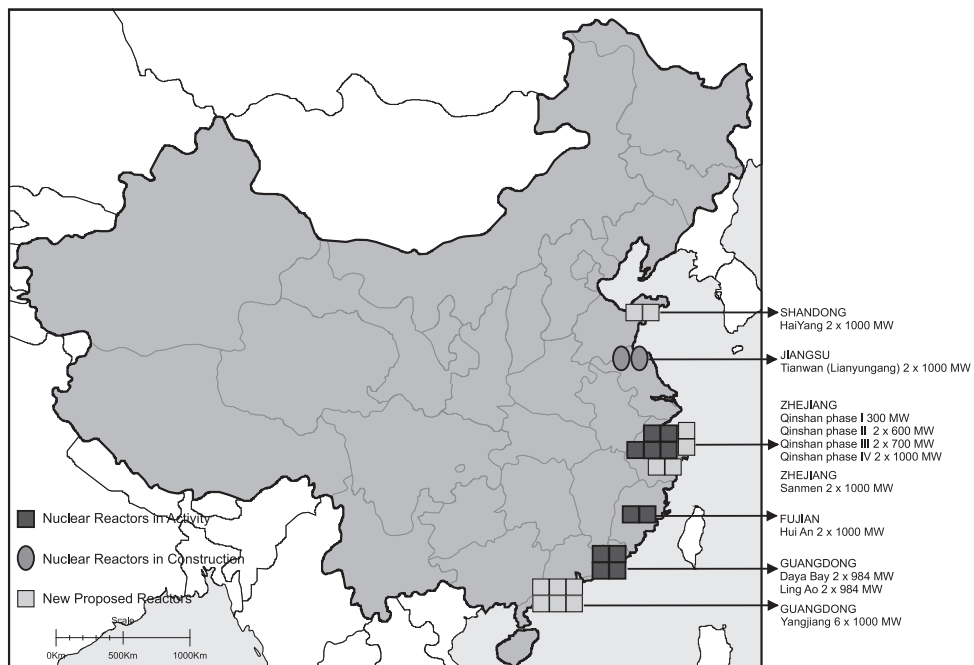
The center holds

In this scenario, the central authorities reinforce the role of coal with a “clean coal” component, and a strong recourse to *coal bed methane* as a non-conventional source of natural gas; however a wide-scale recourse to integrated gasification technologies which can enable China to obtain synthetic fuel and to produce electricity has to resolve the water supply problem to the coal regions. In this scenario the transport of coal by train from the producer regions to the coastal regions that use it would be replaced by the setting up of interconnected electricity networks on a country-wide level, which would enable the circulation of coal. The oil supply from Central Asia and Iran would be articulated with the wide-scale exploration of the oil fields in inland China (Xingiang and Inland Mongolia) through an extensive network of pipelines and gas pipelines that would link Central Asia to Inland China and Inland China to the coastal regions of China. The supply from Russia would, in turn, meet the needs of the north-east region, particularly that of the Bohai Ring.

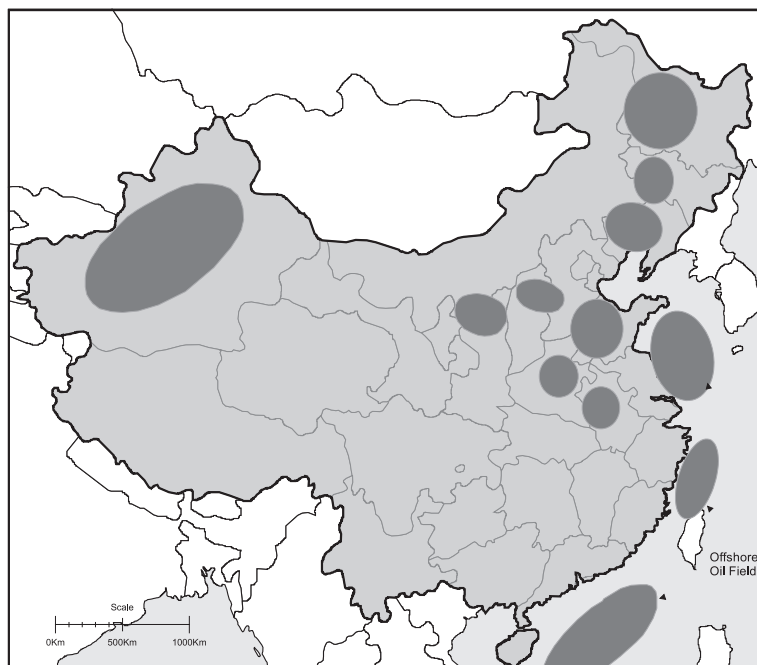
Coastal Hegemony

In this scenario, the coastal regions, which are more integrated in the world economy, will receive their energy supply from the offshore fields and from Asia Pacific namely Australia, and would rely on nuclear energy to supply their main cities with electricity. Relations with western oil companies for the wide-scale exploration of offshore resources would be tightened. The Bohai Ring would rely on relations with Russia for its oil and natural gas supply. The geo-economic unity of China would weaken, while simultaneously the central authorities would not have to deal with the problem of the extensive supply routes in such a pre-eminent manner. In this scenario, China would improve its relations with Japan for the joint exploration of the energy resources of the East China Sea and with the ASEAN countries for the exploration of the resources of the South China Sea. In other words, it would strengthen its relations with several countries which have strong relations with the US.

Map VII. China: Nuclear Reactors



Map VIII. China: Oil ON & OFF Shore



Source: IEA, “China’s worldwide quest for energy security”

Naval Power?

In this scenario, the coastal regions – oriented towards exports – would be supplied not so much by China’s internal resources but rather by oil and natural gas from far-off regions – the Persian Gulf and Africa – albeit from countries with which the central authorities would set up alliances, becoming involved in joint ventures with the respective national companies. However, the extensive shipping routes force the central power to find a way in which to reduce the onus of the dependency on the US naval power. For this it would have to invest strongly in building up an air and naval power not only capable of sea denial (necessary in any of these scenarios for reasons that have to do with Taiwan) but also of intervening over longer distances. In this scenario, it would be all the more crucial to avoid at all costs an approximation between the US and India

Maximum Stress

At the same time, the central power would strive to step up the supply from inland China and from far-off regions, investing in an ambitious program

of internal infrastructures (pipelines and gas pipelines), in the forging of relations with Asian States with energy potential (Myanmar) and in the setting up of a naval power in order to bring down the onus of the strategic dependency on extensive shipping routes.

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The maps have been prepared by the authors based on the CHINA STATISTICAL YEARBOOK 2003

Present and Future Trends of China's Military Modernization¹

Alexandre Carriço

Preamble

This paper takes the middle ground between the bipartisan community of security analysts, between what is popularly designated the “panda huggers” (those who see the rise of China as essentially peaceful and beneficial to the international system) and the “panda sluggers” (those who see this rise as threat, specially to the United States and its Asian allies). I find this “panda hug-slug” label too simplistic. Instead, I would simply say that Stephen Colbert’s “frenemy” construct more helpful in this regard and it will be used throughout these pages, albeit from a People Liberation Army perspective², which in its essence,

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- 1 A previous version of this paper was present by the author at the Asia-Pacific International Symposium Course sponsored by the College of Defence Studies, National Defence University of the People's Liberation Army, in November 2007. The ideas here formulated do not represent the position of the Portuguese Army or of the Ministry of Defence in this matter.
 - 2 Through the reading of PLA publications like *Guoji Zhanlue Yanjiu* (International Strategic Studies), *Guofang Daxue Xuebao: Zhanlue Yanjiu* (National Defence University Journal: Strategic Research), *Guofang* (National Security), *Junshi Kexue* (Military Science) and *Jiefangjun Bao* (Liberation Army Daily) and the interviews and comments obtained by author from PLA superior officers and Chinese scholars during the Asia-Pacific International Symposium Course sponsored by the College of Defence Studies, National Defence University of the People's Liberation Army, in October-November 2007.

it is not so different in its threat perception analysis from the one elaborated annually by the Pentagon officials.³

1. China's Security and Defence Concept and Threat Perception

China's security strategy is made up of three interrelated and mutually reinforcing components. The first is the maintenance of internal stability, a paramount security goal which is also a prerequisite for the advancement of other security objectives, such as economic development and international influence.

The second component is building China's "comprehensive national strength" (*zhong guoli*) which holds that the optimal approach to national security is to strengthen all the dimensions of national power – economic, technological, political, social, military, and cultural.

The third aspect consists of diplomatic manoeuvres through skilful engagement with other countries, international institutions, and regimes which can provide a more favourable external environment for China's economic growth and the enhancement of her international status and influence.

Deriving directly from this strategy we find a "new security concept". This concept was first enunciated by then Foreign Minister Qian Qichen and Minister of Defence Chi Haotian in 1997. It melds several elements of Beijing's global strategic outlook. These include the Five Principles of Mutual Coexistence, the prediction of the emergence of a multipolar world, an embrace of multilateral security mechanisms and "strategic partnerships" with other countries, and the strengthening of trade and economic cooperation.⁴

3 We can see this indefinability on public statements from American military officers. For example on August 19th, 2007, U.S. Marine General Peter Pace said that "Despite recent buildups, the Chinese military does not pose a threat to the United States. Military capabilities and intentions are based on facts. The Chinese military capacity has been growing for the past decade. Despite the military ramp up, the General doesn't see any indications that the Chinese intend to use any of the capacity against the United States. If you look at Chinese military power and you look at ours, you get pretty comfortable, pretty quickly. Chinese capacity is increasing, our capacity is increasing, and the overall delta between their capacity and ours remains huge in our favor." "Gen. Pace says China Not Military Threat". Available on <http://www.1913intel.com/2007/08/21/gen-pace-says-china-not-military-threat/> (accessed on September 3, 2007). Four days earlier (August 15th), Lieutenant General Kevin Campbell, head of the U.S. Army's Space and Missile Defence Command, said that "The Pentagon believes China could be as little as three years away from the capability to disrupt U.S. military satellites during a conflict." "U.S. Military Sees China Threat to Satellites". Available on <http://www.newsroomamerica.com/usa/story.php?id=387687>. (accessed on September 3, 2007).

4 See Yang Wanming; (2007); "On the Concept of Comprehensive Security" in Wang Zhongchun e Chen Senlin (Eds); *World Security Environment*; Beijing, College of Defense Studies, National Defense

For Beijing, the Five Principles of Mutual Coexistence are the political basis and premise of global and regional security in an international system (still) characterized by the United States’ (U.S.) quest for hegemony (*baquanzhuyi*) against a rise of multipolarity (*duoyanghua*). Perhaps the best way to sum up the situation is with the current cliché that the U.S. wants a unipolar world and a multipolar Asia, China desires a unipolar Asia and a multipolar world, while India aspires for a multipolar Asia and a multipolar world.

This global strategic outlook as well as authoritative statements of Beijing’s perception of its security environment, the defence policy and the general strategy it requires, are found in China’s defence white papers. Whereas the most recent white paper, published in December 2006, sees the international system as stable, “factors of uncertainty, instability, and insecurity” are viewed as increasing. In this paper, there is a thinly veiled reference to the United States when it states that “tendencies of hegemonism and unilateralism have gained new ground, as struggles for strategic points, strategic resources, and strategic dominance.” This statement demonstrates Beijing’s apprehension over power and influence of the United States and explains the white paper’s conclusion that “the military factor plays a greater role in international configuration and national security.”⁵ Concomitantly, the United States are at the centre of Beijing’s military security concerns, and this justifies the Chinese logic which sees military power assuming greater importance in protecting People’s Republic of China (PRC) national security, specially in the case of potential confrontation on the Taiwan Strait.

In late July 2006, the Politburo standing committee of the China’s Communist Party (CCP) met for a study session to consider ways of building a “prosperous nation and powerful military” (*fuguo qiangbing*). The result was a “new” strategy with decidedly ancient roots: “to be able to talk peace, one must be able to make war”. This proverb (*nengzhanfang, nengyanhe*) and its implications imply that a strong military helps keep the peace.

University, PLA; pg. 35.

5 China’s National Defence White Paper 2006. Available on <http://www.china.org/cn/e-white/index.htm>. (accessed on September 5, 2007). At its core, Beijing’s suspicion is that American policy seeks not to engage (*jie chu*) but to contain (*e zhi*) China. The 2006 Quadrennial Defence Review states that “U.S. will seek to ensure that no foreign power can dictate the terms of regional or global security. It will attempt to dissuade any military competitor from developing disruptive or other capabilities that could enable regional hegemony or hostile action against the U.S. or other friendly countries, and it will seek to deter aggression or coercion”. Office of the Secretary of Defense, U.S. Department of Defense; (2006); “Quadrennial Defense Review Report”. Available on <http://www.comw.org/qdr/qdr2006.pdf>. (accessed on September 5, 2007).

This “new” strategy connotes ambition and a willingness to be increasingly proactive in protecting China’s interests. A decade ago, China’s leaders would not have considered adopting such a proactive foreign policy for fear of putting domestic reforms at risk. However, this new strategy reflects recent diplomatic successes on the Chinese periphery including demilitarizing several borders, resolving a long-standing territorial dispute with Russia, entering border negotiations with India, and advancing a multilateral security forum for Central Asian states. Other successes include China’s handling of the Asian financial crisis and the delicate brokering of the six-party talks. At the same time, China has built increasingly strong trade relations with neighbours in East, Southeast and Central Asia, bringing traditionally distrustful countries into their economic sphere. Without these positive developments to their credit, any hint of China’s military modernization could have caused more alarm or even sparked regional arms races. By shifting focus at this stage in China’s national development, the leaders apparently feel that a more powerful military will help protect China’s interests, but need not necessarily create an arms race that could undermine economic development or carefully built international trust.

Apparently, People’s Liberation Army (PLA) “strategic transformation” (*zhanlue zhuanbian*) and steady military build-up has been largely focused on Taiwan and its closest ally - the United States - rather than focusing on the ability to project power which would undoubtedly intimidate neighbours and undermine claims that China’s rise will be a peaceful one.⁶ It is clear that China sees itself in a better position to negotiate a peaceful settlement of the Taiwan issue if its military is prepared to back up its threats.

If we have the possibility of reading the studies and speeches published by the majority of the Chinese military analysts and strategists, we can extract the following common and major lines of strategic assessment and analysis (*zhanlue pingjia yu fenxi*) from the last ten years:

- Northeast and Southeast Asia are now two relatively peaceful regions;
- there is strong criticism of the U.S./Japan Security Treaty;
- there is no flexibility on the Taiwan issue and now there is more flexibility on the South China Sea issue;

6 The problem for neighbour countries is that China adopted an algorithm to compute every country’s *zongbe guoli* (comprehensive national power), and for Chinese strategists the end of this algorithm equals *qiang zhi li* (the power or strength to compel other countries). See Wu Chunqiu; (1998); *Da Zhanlue Lun* (Grand Strategy: A Chinese View); Beijing, Military Science Press; pp. 55-70.

- a strong criticism of alliances which are defined as outmoded, emphasizing Beijing’s ties with Moscow and the Central Asia Republics as a model for a different and cooperative form of regional security architecture;
- there is now a more concrete desire for a more multilateral approach to regional security issues; and,
- there is a conditional interest in coordinating policies on North Korea and possibly on South Asia.⁷

From this line of thought, we may conclude that there is a strong appeal in trying to construct a new regional security architecture that is more appealing to China, by means of some kinds of partnerships (preferably strategic ones) or through the balanced management of several triangular relationships: the big triangle with China-U.S.-Japan and the five small triangles of China-Japan-ASEAN, China-Japan-Russia, China-India-Pakistan, China-Japan-South Korea, and China-North Korea-South Korea.

In the security dimension, such “multi-triangular management” should have as a leading beacon three overlapping principles, pointed out by Ronald Montaperto and Hans Binnendijk in 1997⁸ which is still valid today:

- (1) **Common Security.** The structure should promise security for all of the nations of the region and not one nation or group of nations at the expense of another nation or group of nations, under the so-called “win-win strategy”. Within this perspective, military alliances lack utility and are not suitable because they breed mistrust and exacerbate the security dilemma. For example, the redefinition of the U.S./Japan Alliance away from the defence of Japan and towards maintaining regional stability is a disturbing development for them especially because of the Taiwan issue. They make two major criticisms.

7 These assumptions were confirmed by the author during the international symposium at the PLA’s National Defence University (November-December 2007) and were mentioned by Ronald Montaperto and Hans Binnendijk; (1997); “PLA Views on Asia Pacific Security in the 21st Century”. Available at <http://www.ndu.edu/inss/strforum/SF114/forum114.html>. (accessed on September 5, 2007). See also Xu Sheng; (2007); “The Current Asia-Pacific Security Situation” Wang Zhongchun e Chen Senlin (Eds); *World Security Environment*; Beijing, College of Defense Studies, National Defense University, PLA; pp. 38-46.

8 Ronald Montaperto and Hans Binnendijk; (1997); “PLA Views on Asia Pacific Security in the 21st Century”. Available at <http://www.ndu.edu/inss/strforum/SF114/forum114.html>. (accessed on September 5, 2007).

Firstly, they argue that the alliance is being redefined and expanded in order to better contain China.⁹ PLA analysts defend the position that even if the redefined alliance is not aimed entirely at China at this time, it could serve as a tool of containment in the future.

Secondly, PLA analysts are sceptical that the redefined alliance will continue to discourage Japan from developing new military capabilities. Indeed, they express concern that Japan will assume an (unspecified) larger share of its defence burden, that Japan will have a new and expanded role in policing the region with obvious implications for a Japanese role in any Taiwan Strait contingency and that Japanese participation in sophisticated joint defence research programs such as Theatre Missile Defence (TMD) will actually lead to an overall and destabilizing increase in Japanese military capabilities.¹⁰

- (2) **Cooperative Security.** Negotiation and compromise are key elements of regional security. PLA analysts believe it is necessary to respect the diversity of the region, to refrain from trying to impose any particular set of values and to build consensus through a step-by-step approach that recognizes the equality of all of the regional powers.¹¹ Although the regional great powers (China, Japan, the United States, and Russia) have special responsibilities, no nation or group of nations should play the role of a regional hegemon.

9 After the presentation of the 2007 defence white paper in July, Yuriko Koike, the first Japanese female Defence Minister said that “China is believed to be aiming to build capacity to perform operations in waters further and further from its shores.” Beijing was aiming at “air superiority further forward and anti-surface and anti-ship assault capability,” it added. As a result of this, as well as Beijing’s deployment of 700 short-range ballistic missiles capable of hitting Taiwan, the military balance was shifting towards China. The document is the clearest signal yet of Tokyo’s concern about Beijing’s growing military capability. Last year, the white paper said only that Japan needed to watch China’s military modernization carefully and defence officials have consistently denied that they regard Beijing as a threat. David Pilling; (2007); “Japan Feels Threat of China’s Military”. Available on <http://www.ft.com/cms/s/e1ea19d6-2bb7-11dc-b498-000b5df10621.html> (accessed on September 6, 2007).

10 Recently there have been some encouraging signs of a limited *entente* between Beijing and Tokyo. In late August 2007, after the first visit of a Chinese military chief (General Cao Gangchuan) to Japan in a decade, both countries agreed work to ease military tensions through a crisis hotline and ship exchanges, despite lingering uneasiness over Taiwan and Beijing’s growing defence spending. China invited Japan to observe a PLA military exercise in October 2007. “Japan, China Eye Hotline to Boost Military Ties”. Available on <http://taiwansecurity.org/AFP/2007/AFP-300807.htm>. (accessed on September 7, 2007). In late December 2007 Japan made a successful test of a missile defense sea based system, which generated much criticism from China.

11 See Ma Zhengang; (2007); “The Increasingly Eminent ‘China Factor’ in the International Framework” in Wang Zhongchun e Chen Senlin (Eds); *World Security Environment*; Beijing, College of Defense Studies, National Defense University, PLA; pp. 25-30.

(3) **Comprehensive Security.** Security includes both economic and military components. It is necessary to account for interdependence.¹² PLA analysts promote Beijing’s relations with Moscow and the Central Asian Republics (established in Shanghai in 1996) as the model for the future. They claim that China and Russia have built and wish to maintain a coordinated strategic partnership that enables each one to feel secure. Although Sino/Russian ties amount to a strategic partnership, the nations are not allied against any other party: the region needs a network of similar relationships.¹³ Also, in a new departure, PLA analysts advocate initiating a series of supplementary dialogues on relevant strategic issues and the slow building of multilateral structures and regimes.¹⁴

This vision basically implies that Beijing does not intend to sacrifice its domestic economic goals by engaging in militarization or an arms race, but it is also clear that China is determined to safeguard its national sovereignty and security no matter how the international situation may evolve. Beijing’s “posture of active defence” means that the regime is willing to be patient, peaceful and cooperative as long as events fall in with its general expectations of enhanced power but will change course if its progress towards its goals is disrupted by other powers, specifically the U.S. position concerning the Taiwan issue.

Basically, the U.S. “strategic ambiguity” poses difficulties for Washington and Beijing. Washington offers security to Taipei because Taiwan is one of the most important political foothold in East Asia. Were China to unify, Washington’s presence in the region would be significantly diminished. Yet Washington needs to maintain its economic relations with Beijing to protect American investments and it understands that Beijing has limits in relation to Taiwan which means that Washington must support the “one China” policy and try to check moves towards independence in Taipei.

12 See Yang Wanming; (2007); “On the Concept of Comprehensive Security” in Wang Zhongchun e Chen Senlin (Eds); *World Security Environment*; Beijing, College of Defense Studies, National Defense University, PLA; pp. 31-37.

13 Although there is a lack of a formal, concrete Chinese definition of what is a partnership, in broad terms the two sides are both seen as partners and competitors (a concept quite palatable to the Chinese win-win approach).

14 See the Montaperto and Binnendijk report at <http://www.ndu.edu/inss/strforum/SF114/forum114.html>. (accessed on September 5, 2007). But Beijing is critical of the new US-Japan-Australia trilateral dialogue system which can be eventually converted into a quadrilateral one, including India also. China sees this American initiative like the military build-up of Guam as a move towards forming an ‘Asian version of NATO and a security mechanism against China’. This assertion generated a vivid debate between the participants during one of the seminars at the NDU.

At present, the incipient Beijing-Washington conflict is stalemated, but the situation is inherently unstable.¹⁵ The best indicator of whether Beijing or Washington is winning the geostrategic contest in East Asia is the status of the unification issue, which is China's "chosen field of battle". In sum, how Beijing manages this tripartite power relation will in great part determine the success of its regional geostrategy and its continuous power ascension (or peaceful development) in the region.¹⁶

It's understandable that China's grand ambition is to be the premier Asian power in Asia by 2015 and to wield considerable worldwide authority by 2050. It has partially achieved these aims through a combination of skilful diplomacy and a relatively successful program of domestic economic reform. But it still lacks the third leg of the tripod that supports any great state: a respected and competent military capable of credibly projecting power outside national borders and reinforcing policy initiatives in the international arena. Notwithstanding, in the last decade Beijing has taken great strides to reduce its military technological gap *vis a vis* Japan and the United States and has already supplanted Taiwan.

As President Hu Jintao declared at the Great Hall of the People during the celebration of the 80th anniversary of the PLA foundation in August 2007, "We must study ways of running the armed forces under the new situation, enhance defence forces in all aspects and get prepared for military operation at any time... The historical mission of the armed forces in the new century and the new era is to provide an important guarantee of strength for consolidating the status of the Communist Party of China as the ruling party and security guarantee for national development in a period of important strategic opportunities, serve as a strategic underpinning for upholding national interests and

15 See Richard Bush; (2005); *Untying the Knot: Making Peace in the Taiwan Strait*; Washington, Brookings Institution Press. Richard Bush and Michael O'Hanlon; (2007); *A War Like No Other: The Truth About China's Challenge to America*; New Jersey, Wiley and Sons. During the seminar there was a serious and general Chinese concern regarding Taiwan attitudes towards the referendum and their presidential elections in March 2008. A quite delicate matter especially when Beijing is organizing the Olympic Games in August and in November there will be presidential elections in the U.S.A.

16 See Christopher Howe (Ed); (1996); *China and Japan: History, Trends, and Prospects*; Oxford, Clarendon Press. Yoshihide Soeya; (1998); "Japan: Normative Constraints versus Structural Imperatives" in Muthiah Alagappa (Ed); *Asian Security Practice: Material and Ideational Influences*; Stanford, Stanford University Press. Peter Katzenstein and Nobuo Okawara; (2004); "Japan and Asia-Pacific Security" in J.J. Suh, Peter Katzenstein and Allen Carlson (Eds); *Rethinking Security in East Asia: Identity, Power, and Efficiency*; Stanford, Stanford University Press.

play an important role in maintaining world peace and promoting common development.”¹⁷

2. China’s Defence Doctrine and People’s Liberation Army as a Tool of Security

When we read the official press and hear or see Chinese government officials referring the importance of the “all-round” development of the PLA, it is clear that Beijing intends to build a state-of-the-art armed force based on embracing “the revolution in military affairs” (*xin junshi geming*), that is remaking combat by infusing “mechanization” with “informationization”.¹⁸

The foundation of Beijing’s security policy is an armed force capable of winning “local wars under high-tech conditions” (*gaojishu tiaojian xia de jubu zhanzheng*) – under a strategy (*zhanlue*) called “active defence” (*jiji fangyu*)¹⁹ which in its essence is much similar to a pre-emption concept because victory is to be achieved by gaining the initiative by striking first (*xianfa zhiren*), adhering to one traditional “operational principle” (*zuozhan tiaoli*) of “pitting the inferior against the superior” (*yilie shengyou*), a recognition of technological inferiority for an indefinite period of time.²⁰

This concept of active defence with its strategic principles (*zhanlue tiaoli*) and operational principles, highlights among others, the necessity of integrated operations (*xietong dongzuo* or *lianhe zuozhan*), preemptive strikes (*xianji zhidi*), asymmetrical warfare (*buduideng zhangzheng*), transregional operations (*kuaqu zuozhan*), and other general concepts through rapid deployment, information

17 Available on http://english.chinamil.com.cn/site2/special-reports/2007-08/02/content_906100.htm. (accessed on September 7, 2007).

18 The Chinese are now increasingly using the term informationization in their writings. This term has been explained in general terms, but it refers to capacity of adapting itself to the changes both in the international strategic situation and the national security environment and rise to the challenges presented by the revolution in military affairs worldwide, albeit with “Chinese characteristics”. To operationalize the dual task of mechanization and “informationization”, PLA strategists have articulated and advanced the new concept of “integrated joint operations” (*yitihua lianhe zuozhan*). See the latest China’s National Defence 2006, available on <http://www.china.org/cn/e-white/index.htm>. (accessed on September 7, 2007).

19 There is no precise equivalent for “doctrine” in Chinese. The closest appears to be “military thought” (*junshi sixiang*). For Chinese strategists, wars are composed of a series of campaigns which are made up of numerous general operations and specific battles. For the PLA, the strategy of active defence guides him at all four levels (wars, campaigns, operations, and battles).

20 See the English language translation of Peng Guangqian and Yao Youzhi; (2005); *The Science of Military Strategy*; Beijing, Military Science Publishing House. This is an updated version of *Zhanlue Xue 2001* (On Strategy 2001).

warfare, electronic warfare, employment of long-range artillery, short-range ballistic missiles and precision guided munitions.²¹ The strategy calls for forward positioning, frontier defence, engagement of the enemy at or over the border and potential engagement in conflict beyond China's immediate periphery.

Beijing defined five likely limited war (*youxian zhangzheng*) scenarios²²: military conflict with neighbouring countries in a limited region; military conflict in territorial waters; undeclared air attack by enemy countries; territorial defence in a limited military operation; and punitive offensive with a minor incursion into a neighbouring country.

As an overall result, China's military policy is designed to give its armed forces the capability for ensuring the successful fulfillment of political and economic tasks and objectives on the regional scale by their specific methods according to a stage by stage reform and modernization of the military and a gradual build-up in the flexibility of its operational capability. Within this scope, special emphasis is placed on creating military "pockets of excellence" such as raising and training mobile forces, comprising a part of land troops, including paratroops, as well as aviation and naval forces, all connected with an adequate C4ISR²³ system and appropriate logistics.²⁴

But the "army-buiding in the new era" (*xin shiqi de jundui jianshe*) and the inherent "all round" development has a double and symbiotic face. As a result of its overriding interest in internal economic growth, Beijing puts military modernization at the service of its goal of creating a "moderately prosperous society." In other words, the modernization of the People's Republic of China Armed Forces correlates with China's economic progressive modernization and it will be implemented in three stages.

21 See Nan Li; (1999); "The PLA's Evolving Campaign Doctrine and Strategies" in James Mulvenon and Richard Yang (Eds); *The People's Liberation Army in the Information Age*; Santa Monica, RAND. In the absence of active operational experience, the PLA may take another decade to fully implement all the ingredients of these ambitious new military operational principles.

22 For Chinese strategists the aim, range, tools of war and time and space of engagements are all limited.

23 Command, control, communications, computers, informations, surveillance, reconnaissance.

24 The PLA mobile forces have two components: rapid reaction (*kuaisu fanying budui*) with some Special Forces units (*tezong zuozhan budui*) and rapid deployment forces or "fist units" (*quantou budui*). Rapid reaction forces are assault forces featuring high operational effectiveness and maneuverability. They are equipped with small arms and light weapons and are airlifted or sea-lifted to the objective area. Eventually, the Chinese rapid reaction forces have the capability to deploy, by airlift, to any point in China (be it desert, swamp, mountainous terrain, etc.) within 10 hours of an order being issued. Deployment by rail takes one to four days. The rapid reaction forces are comprised of an airborne corps, about six infantry divisions, several special purpose battalions under district command, and naval infantry. They have a total of 385,000 servicemen. Rapid deployment forces are designed to build up the efforts of rapid reaction forces. They have heavy weapons and are deployed to the objective area mainly by rail within a space of two to seven days.

At Stage 1 (from 1979 until 2010), the main efforts by the Chinese military command will be focused on streamlining the structure of the Armed Forces, downsizing them²⁵, and increasing the proportion of advanced weapons and military equipment. Basically, this has resulted in changes in the force structure; reform of the structure and missions of the reserves and militia; changes in the personnel system; an influx of new equipment; continuous doctrinal revision to prepare the PLA to fight and win Local Wars Under Modern High-Technology Conditions or Local Wars Under “Informationalization” Conditions; improvements in the frequency, content, and methods of military training, with emphasis on joint operations (*lianhe zuozhan*); transformations of the PLA logistics system; enhancement of all soldiers’ standard of living, pay, and lifestyle; and modification of the professional military education system. As a result of these “security investment” priorities, China should be able to partially reduce the gap towards the world’s major military powers and ensure its capability of containing possible adversaries and successfully fight local wars.

At Stage 2 (from 2010 until 2020), the main efforts will be concentrated on providing the troops and naval forces with more advanced, high-tech weapon systems and parallel military doctrine adjustments. As a result, China will emerge as one of the leading military powers in the region, acquiring the capability to effectively uphold its interests by military methods on the regional scale.

At Stage 3 (from 2020 until the 2050s), modernization of the Armed Forces is to be “completed”. By this time, it is planned to turn China into one of the world’s leading powers with an appropriate military capability.

To sum up, there are four contextual drivers of China’s military modernization: the Taiwan issue; the regional security environment; the U.S. military footprint around China; and Beijing’s growing energy needs.

In spite of this military modernization drive, we can say that in the first decade of the 21st century, the PLA is not a central actor on China’s foreign policy the way it was a few decades ago. Nevertheless, this military reform policy underscores the political significance of the PLA which can not be

25 The Army was the most affected of the services with the personnel reductions in result of the PLA mission emphasis shifting from the continent to the maritime periphery. The Chinese government confirmed this prioritization in China’s National Defence in 2004, available on http://english.chinamil.com.cn/special/cnd2004/contents_04.htm. (accessed on September 2, 2007). In the last decade there were two major personnel reductions: the first between 1997 and 2000 reduced 500,000 men and the second between 2003 and 2005 which demobilized 200,000 men. After these reductions PLA have a force of 2.3 million.

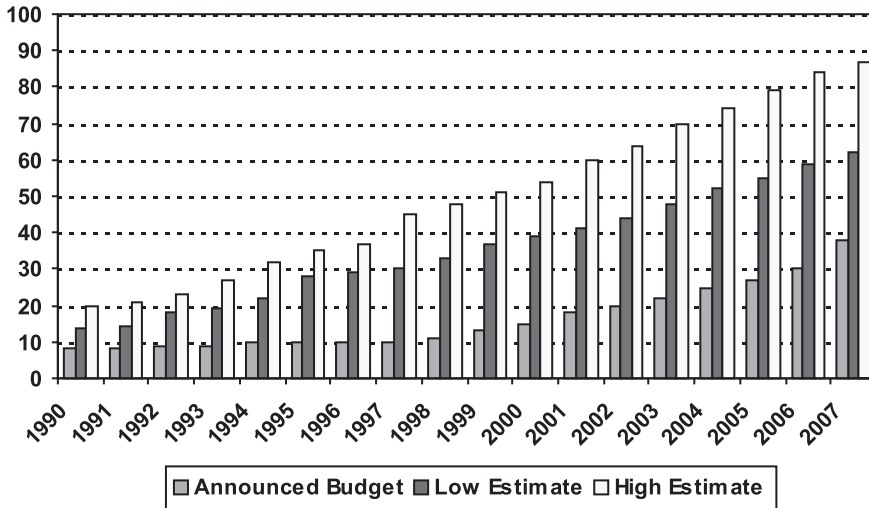
misunderstood. According to China's security concept, the military remains a player that may have a more active role and influence (if judged necessary) in China's policy towards such countries and regions as the United States, Japan, the Koreas, Southeast Asia, South Asia, and, of course, Taiwan. It is important not to overlook that, in times of crisis or conflict, the role and influence of the PLA rise significantly.

This assertion will lead us to direct drivers of China's military modernization: the military budget; military strategy and defence policy; and the military-industrial complex.

In the last twenty years, the Chinese defence budget has had systematic increases (normally above the two digits).²⁶ Those increases have always generated an intense debate and a certain degree of speculation reinforced by Chinese opacity about the real dimension of his defence budget.²⁷

26 In 2007 the increase was of 17.8 percent to about \$45 billion. See http://english.chinamil.com.cn/site2/special-reports/2007-08/02/content_906097.htm. (Accessed on September 2, 2007). This last announcement came on the eve of a reshuffle of the U.S. command. The last U.S. Pacific Command chief, Admiral William J. Fallon, was moved to Central Command in the Middle East. He was a driving force for closer contact with the Chinese military; he increased the frequency of dialogue with his Chinese counterparts; and he was involved in the first joint-training exercises with China in 2006.

27 A recent RAND report estimates total defence expenditure to be 1.4 to 1.8 times the officially announced number. This estimate is much smaller than the one presented by the U.S. Department of Defence, because comprehensibly it does not include the funds to the People's Armed Police. See Keith Crane, Roger Cliff, Evan Medeiros, James Mulvenon, and William Overholt; (2005); *Modernizing China's Military; Opportunities and Constraints*; Santa Monica, RAND. Available on http://www.rand.org/pubs/monographs/2005/RAND_MG260-1.pdf. (accessed on September 1, 2007). This disparity in the estimations depends on the factors applied in terms of comparison (e.g. McDonald's purchasing power parity, Schumer-Graham estimate of 43 percent undervaluation). For a state of the field *tour d'horizon* see Richard Bitzinger; (2003); "Analysing Chinese Military Expenditures" in Stephen Flanagan and Michael Marti (Eds); *The People's Liberation Army and China in Transition*; Washington, National Defense University.

Figure 1 – Estimates of China’s Defence Budget (1990-2007)²⁸

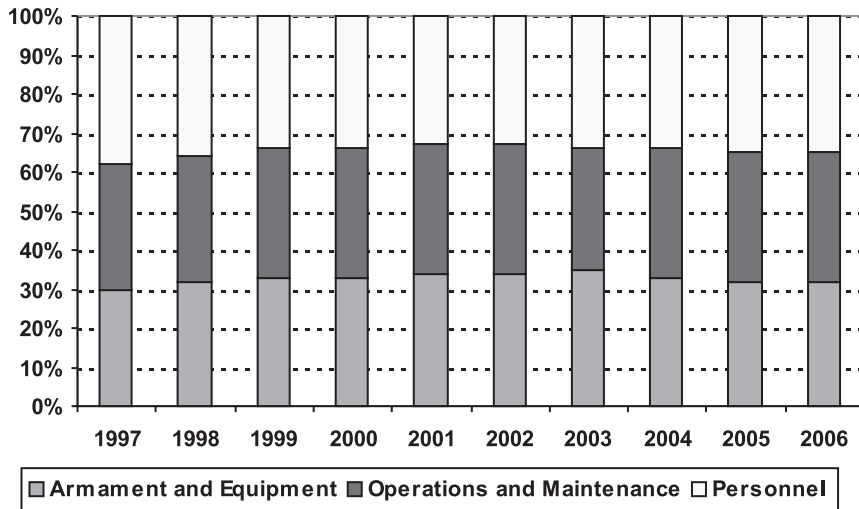
But there are some reasons to believe that Beijing is selectively and progressively lifting this veil of secrecy, although in the mid-term it will remain essentially opaque. In September 2007, China said that it would submit information about its military spending and weapons trading to the United Nations, in what appeared to be an effort to calm fears about its secretive and rapidly expanding armed forces. The Foreign Ministry announced that Beijing would begin providing basic data about its military budget and resume submitting annual accounts of imports and exports of conventional weapons. Beijing authorities declared that they are “Moving from a country that keeps its secrets

28 Compiled from Paul Godwin; (1996); “Estimating China’s Military Expenditure” in Gerald Segal and Richard Yang (Eds); *Chinese Economic Reform: The Impact on Security*; London, Routledge Press; pp. 63-67. SIPRI; (1994); “World Military Expenditure: China” in *SIPRI Yearbook 1994*; Oxford, Oxford University Press; pp. 441-447. Richard Bitzinger and Chong-Pin Lin; (1994); *Analysing and Understanding Chinese Defense Spending*; Washington, Defense Budget Project. Bates Gill; (1999); “Chinese Defense Procurement Spending: Determining Intentions and Capabilities” in James Lilley and David Shambaugh (Eds); *China’s Military Faces the Future*; New York, M.E. Sharpe; pp. 195-227. Amitav Acharya and Paul Evans; (1994); *China’s Defense Expenditures: Trends and Implications*; North York, Ontario, University of Toronto-York University Press. Wang Shaoguang; (1996); “Estimating China’s Defense Expenditure: Some Evidence From Chinese Sources”; *The China Quarterly* n°147. David Shambaugh; (2003); *Modernizing China’s Military: Progress, Problems and Prospects*; Berkeley, University of California Press. Wang Shaogang; (2000); “The Military Expenditure of China, 1989-98” in *SIPRI Yearbook 2000*; Oxford, Oxford University Press. Richard Bitzinger; (2003); “Just the Facts, Ma’am: The Challenges of Analysing and Assessing Chinese Military Expenditures”; *The China Quarterly* n°173; pp. 164-175. Dwight Perkins; (2006); “China’s Economic Growth: Implications for the Defense Budget” in Ashley Tellis and Michael Wills (Eds); *Strategic Asia 2005-2006: Military Modernization in an Era of Uncertainty*; Seattle, National Bureau of Asian Research; pg. 380. China’s National Defence White Papers, available on <http://www.china.org/cn/e-white/index.htm>. (accessed on September 3, 2007).

in the interests of security, to one that shares them in the interests of security. This is a sign of confidence".²⁹

Transparency criteria apart, it is possible that today the defence budget may take about 3 percent of China's gross domestic product (GDP) and most of it has been directed to expenses with personnel and foreign arms acquisitions (mainly from Russia, but also from Israel).³⁰

Figure 2 – Percentage Distribution of PLA Budget by Rubrics³¹



If China's economy continues to grow at this pace until 2025 (which is not very probable) then the defence budget can take about 9 percent of GDP, which is excessive and supplants NATO expenditures. Moreover, with the "greying" of the Chinese population, the central government will be confronted with growing demands for more societal spending (social pensions, health care, educations, public infrastructure, and environment policies which will add more pressure to military spending.

What we are actually seeing is a balanced development of the national defense capability and the national economy, partially justified by the aspira-

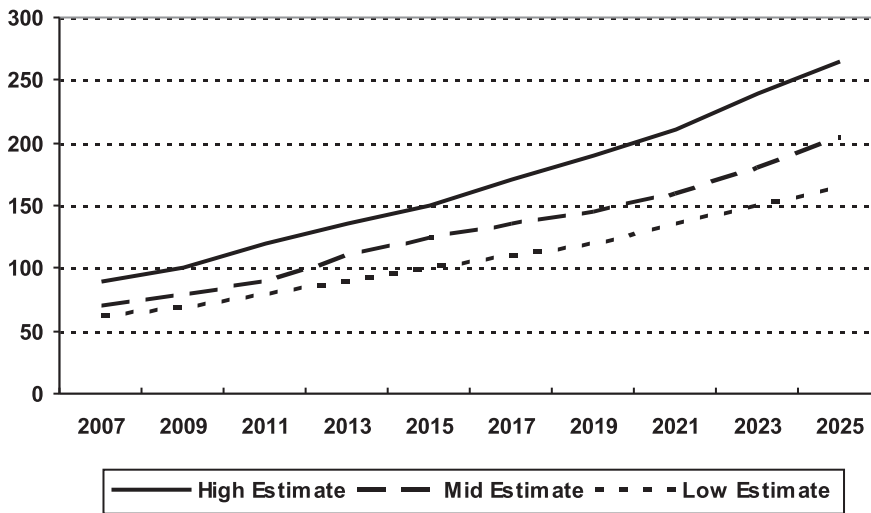
29 "China to Give Data to U.N. On Its Military Spending". Available on <http://taiwansecurity.org/ NYT/2007/NYT-030907.htm>. (accessed on September 6, 2007).

30 A substantial part of the armament and equipment acquired to Russia was made with CCP Politburo funds under the name of "National Construction", which aren't included in the defence budget numbers, contributing to the disparity in the estimates.

31 China's Defence White Papers, 1998, 2000, 2002, 2004, 2006. Available on <http://www.china.org/cn/e-white/index.htm>. (accessed on September 10, 2007).

tion of the Chinese leadership to keep military spending under control. The Law on National Defense, on Article 35, Part 6 (National Defense Spending) establishes that national defense spending is predicated not only on the level of the country’s economic development but also on “actual defense needs”. Beijing’s threat perceptions and the defence of China’s interests referred above reinforce these increases and justify the efforts of modernization and arms and equipment acquisitions, as well as research and development (R&D) according to the PLA military strategy.

Figure 3 – Estimates of PLA Budget Evolution in \$billions (2007-2025)



3. PLA Military Strategy

Compared with China’s historically reactive stance of luring the enemy in deep and destroying it through strategic defence, the present military strategy is essentially pro-active and seeks to take the battle into enemy territory. It also strives to achieve surprise in a pro-active manner that is demonstrated by new “quick-strike” tactics. The PLA now believes victory can be achieved by attacking the enemy’s vital but fragile targets such as command nodes, communication centers, transportation hubs, airfields, and high-tech weapon platforms, with all available land, air, sea and space forces (a strategy popularly known as “acupuncture warfare”). Winning the battle against an enemy’s key

points will allow the PLA to size the initiative on both tactical and strategic levels and facilitate a short decisive campaign.

While the land frontier is expected to continue to generate some local tensions, the Central Military Commission (CMC) has identified space and the oceans as the new areas where future conflict might take place (areas where U.S. has the qualitative superiority). Understandably, the quest to achieve information dominance (*zhixinxiquan*) forms the core of this PLA emerging military strategy under which the term War Zone Campaign (*Zhanqu Zhanyi*) emerges as an application of the concept “Limited, Local war under High-Tech Conditions”. The phrase “Limited, Local War under High-Tech Conditions”, like James Mulvenon pointed out, is not a doctrine, but “a menu” of conflict scenarios deemed most likely in short-to medium-term by the leadership.”The scenarios viewed within the PLA leadership are:

- (1) Limited objectives, which restrict the scale, means and the timing of the war.
- (2) Very often those objectives are more political-diplomatic oriented than military (for example, wiping out the enemy’s manpower).
- (3) The conflict process is under greater central control, with a political settlement seen at the end result.
- (4) A complicated international background, which makes the conflict more unpredictable and fast evolving.
- (5) Although the war is limited, the preparation for it requires intensity because the room for failure is very narrow.
- (6) Pre-emptive attack (surgical strike) is a major form of action.³²

To face these scenarios and win the conflicts associated with them the PLA Navy, Air Force and Strategic Forces were the services that were mostly pressed into adopting new military strategies, albeit the Army was not immune to these reforms and modernization efforts.

The People Liberation Army Navy (PLAN) maritime mission has evolved from a role of static coastal defence to one of “active offshore defence.” In this capacity, the PLAN can be used both as a tactical force and to support strategic national defence. The objectives of this new strategy are to assert China’s role as a regional maritime power, to protect coastal economic regions and maritime interests, and to optimize the Navy’s operations for national defence. The PLAN’s responsibilities now include the capture and defence of islands, and protection and blockade of sea-lanes of communication. Moreover,

³² Xinhui; “Brigade Reform and the Recent PLA Development”. Available on http://www.china-defense.com/pla/brigade_reform/brigade_reform02.html (accessed on September 2, 2007).

the PLAN is increasingly viewed by senior PLA leadership as integral to resolution of the Taiwan issue - should force be required -and for safeguarding China’s “Xisha” and “Nansha” islands in the South China Sea. Finally, the PLAN is likely to be increasingly used as an instrument of overseas diplomacy through participation in goodwill cruises and port visits.

The PLAN’s evolving strategy has been described in terms of two distinct phases and as an extension of China’s defence perimeter from coastal waters (*jinhai fangyu*) to an offshore perimeter (*jinyang fangyu*) of up to 400 nautical miles, as well as the South China Sea. In the longer term, blue water capabilities (*yuanyang haijun*) are clearly on the Chinese agenda.

More precisely, this strategy’s first phase is for the PLAN to develop a “green water active defence strategy” capability. This “green water” is generally described as being encompassed within an arc swung from Vladivostok to the North, to the Strait of Malacca to the South, and out to the “first island chain” (Aleutians, Kuriles, Ryukyus, Taiwan, Philippines, and Greater Sunda islands) to the East. Analysts have assessed that the PLAN is likely to attain this green water capability early in the 21st century. Open-source Chinese military writings also suggest that the PLAN intends to develop a capability to operate in the “second island chain” (Bonins, Guam, Marianas, and Palau islands) by the mid-21st century. In the future, the PLAN also may expand its operations to bases in Myanmar, Burma. These bases will provide the PLAN with direct access to the Strait of Malacca and the Bay of Bengal.

The fact is that comprehensibly, this Chinese naval strategy is in direct competition with its neighbour’s navies. Beijing is facing a serious expansion of naval military power in the region.

Because of this game of catch-up, Beijing has no shortage of military projects - especially naval ones. The PLAN, along with the other branches of the PLA, has made admirable improvements in the last decade. There has been progress in areas such as missile technology and nuclear submarine propulsion - progress more realistically within China’s technological grasp than for example a meaningful carrier fleet - and it is precisely these more realistic, near-term pursuits and improvements that may suffer.³³

33 The project could be announced in 2009-2012 and completed in 2013-2017. Last year, Alexander Denisov, who runs Russia’s agency for military-technical cooperation and headed the Russian delegation at the Air Show China 2006 in Zhuhai, said Russia could help China with building an aircraft carrier if they asked for assistance. This March, a senior Chinese official conceded that Beijing was studying the possibility. Available on <http://www.kanwa.com/dnws/showpl.php?id=246>. (accessed on September 9, 2007).

At the present time, the PLAN lacks a real power projection capability and it is quite unable to conduct sustained naval operations due to inadequate fleet replenishment capabilities. It is generally limited to operating within range of friendly air coverage as a majority of its large combatants lack area air defence systems. A similar deficiency exists in Anti-Submarine Warfare capabilities. There's a general lack of organic fleet air assets with only a few ships being helicopter capable. There are no aircraft carriers, and amphibious lift capabilities are limited. As command and control is rigidly centralized, the PLAN, in general and for now, cannot operate in a network centric battlespace with rapidly evolving battles as information warfare capabilities and C4ISR assets are quite limited. Training and maintainability standards also appear to be low.

The PLAN is not yet a significant naval power, even when viewed solely in a regional context. PLAN surface ships, submarines, and aircraft continue to lack the sophisticated weapons and sensor systems which characterize modern first-line naval units. These shortfalls limit the PLAN's present warfighting capabilities, and Chinese naval units are not yet up to the standard attained by the navies of Japan or the Republic of Korea. There are also significant tactical and doctrinal shortfalls that the PLAN has not adequately addressed. At-sea sustainability is modest and the PLAN has not yet demonstrated the ability to conduct complex coordinated air and surface operations. The training of individual sailors remains basic by Western standards and the PLAN lacks a corps of experienced non-commissioned officers. From the highest echelons of the service to individual commands, control is highly centralized, with little flexibility and creativity in subordinate ranks. These shortfalls will limit the ability of the PLAN to assert a significant regional naval presence for perhaps five to ten years, and the Navy is not likely to possess the longer reach associated with a maritime power-projection capability until well into the 21st century.³⁴

The PLA Air Force (PLAAF) possesses a different set of haves, wants and needs. With the potential threat of high-tech air forces around China's periphery as well as the challenge of winning a possible air campaign against Taiwan, the PLAAF has shifted its focus to prepare for offensive missions, including the advancement of strike capabilities, from fighters to strategic bombers. Like the Army, it currently possesses a mix of older equipment and modern systems.

³⁴ As recognized by several PLA Navy officers during the symposium. Their main concern is connected with operations on the "first half distance of the first island chain".

Although the PLA has always had an active defence strategy, one of the PLAAF’s most significant developments in the past couple of years has been the public emphasis by Chinese leaders, including CMC Chairman Hu Jintao, on the PLAAF’s capability to fight offensive battles. What this means is that the PLAAF is beginning to acquire the types of weapon systems, such as the Su-27, Su-30 and Il-76 which will allow the PLAAF to change its doctrine appropriately and move away from its purely defensive missions.

But there are structural problems for PLAAF modernization efforts, usually defined as “needs versus wants” which can be summarized in three factors. Firstly, the PLAAF must decide whether to downsize to a smaller, more lethal force – while building force multipliers like airborne early warning and aerial refuelling – or, alternatively, to maintain large numbers of less capable but cheaper systems. The second question is how the PLAAF reconciles its internal and external needs, because the technology requirements can be complicated by the agenda of the domestic defence industry to advance its own capabilities. Finally, the PLAAF must agree on a division of labour within the PLAN Air Force and define who gets priority on new acquisitions.

Although the PLAAF is acquiring some systems to support the air defence mission, such as refuelling, electronic counter-measures, and airborne early warning platforms, it will be several years before these systems can be fully integrated into the force, and even then, only in limited numbers. The PLAAF still lacks precision guided munitions and a battlespace surveillance capability, but China is working on these capabilities. The PLAAF is beginning to train its forces in mobile operations, but is still hindered by institutional, organizational, and equipment limitations that hinder mobile operations. Furthermore, the PLAAF is not yet capable of round-the-clock or sustained operations. There is little doubt that what the PLAAF has done over the past decade is impressive. Air combat training has become more realistic, including more live air-to-air missile launch training, but the pilots still lack sufficient flying hours due essentially to engine and airframe limitations.

The Strategic Missile Forces (*Zhanlue daodan budui*) or PLA’s Second Artillery strategy is based on the doctrine of minimal deterrence (*zuidi weishe*) but there are some signs that it may be “upgraded” to a doctrine of limited deterrence (*youxian weishe*). This doctrinal evolution represents a shift from an ability to inflict damage on an aggressor to being able to wage a nuclear war,

albeit minimally. It can essentially be classified as war fighting doctrine (*shizhan nengli*) framed by China's commitment to "no first use" policy.³⁵

This doctrinal transformation means that in order to enable Beijing to respond to any level of attack, be it tactical or strategic, the PLA will have to increase the number of nuclear weapons available. This will allow for some degree of escalation control because China will retain sufficient forces for extended exchanges.

Under this worst case scenario, PLA leadership prioritized the objectives of nuclear counterattack campaigns as follows:

- "Cause the will of the enemy (and the populace) to waver;
- Destroy the enemy's C2 system;
- Delay enemy's war (or combat) operations;
- Reduce the enemy's force generation and war-making potential;
- Degrade the enemy's ability to win a nuclear war.³⁶

The prioritized major targets for China's "Second Artillery" are:

- Enemy political and economic centers, especially important urban areas with a goal of creating great shock in the enemy population's spirit and destroying their will to wage war;
- Destroy critical infrastructure of the enemy to weaken the enemy's capacity for war (for example petroleum refining, storage and shipping links, electric power generation and transmission lines, and major heavy industries);
- Enemy transportation networks;
- Major military targets such as air force and navy staging areas and bases to degrade the ability of these services to wage war; and
- Major deployed military forces."³⁷

It is perfectly clear that all this nuclear doctrine evolution and its military objectives targets the U.S. armed forces based in Asia especially in a case of a Taiwan conflict where Washington decides to intervene in support of Taipei.

35 There are serious doubts if as a result of PLA mixing of conventional and nuclear warheads on the same kind of missiles whether China's no first use policy would hold up in a theatre and regional conflict. The Second Artillery is the "least transparent" of the four PLA services, and questions concerning her operational strategy are diplomatically deflected.

36 See http://www.defencetalk.com/news/publish/wmd/Chinas_Military_Nuclear_Forces_Operations170011824.php (accessed on September 9, 2007).

37 Liu Mingtao, Yang Chengjun (Eds); (1993); *Gao Jishu Zhanzheng Zhong de Daodan Zhan* (Ballistic Missiles Battles in High Technology Warfare); Beijing, National Defence University Press; pg. 116.

In this case perhaps the minimum and limited deterrence will not be mutually exclusive nuclear doctrines. They will be complementary at different levels of conflict. Minimal deterrence will likely be the operative doctrine at the strategic intercontinental level, while limited deterrent – which envisions offensive limited nuclear war-fighting – will likely be operational at a regional, intermediate-range, theatre level; while China’s conventionally armed Short Range Ballistic Missiles areas today likely configured in an offensive, preemptive, counterforce, warfighting posture.³⁸

4. Main Areas of PLA Military Modernization

Structurally speaking, the main areas of present military modernization are the result and encompass developments made in the previous two decades and accelerated since 1995. These can be summarized as:

- (1) Reductions in the force size;
- (2) Restructuring of the force structure, including reserves and militia;
- (3) Changes in the personnel system;
- (4) Influx of new equipment;
- (5) Doctrinal revision;
- (6) Improvements in the training methods directed to joint operations;
- (7) Transformation of the logistics system;
- (8) Enhancement of all soldier’s standard of living and pay; and
- (9) Modification of the professional military education system.³⁹

This modernization effort - as pointed out by Richard Fischer - due to foreign assistance, direct or indirect, presently gives China, a military powerful enough to cause serious troubles for its neighbours and for the United States, should it attempt, as an ally or friend, to help them.⁴⁰

But in spite of this initial “external dependency”, China does not wish to be solely dependent on foreign weapons, and the true test of this period of transition, in which it must turn to foreign sources, is the degree to which it

38 See Alastair I. Johnston; (1996); “Prospects for Chinese Nuclear Force Modernization: Limited Deterrence versus Multilateral Arms Control”; *The China Quarterly* n°146; pp. 548-576.

39 The north-American system is quite interesting for the Chinese military leadership. The NDU sponsored several research projects about comparative models between the Russian, the Chinese and the American. The author had the opportunity to talk with one of the researchers involved in this project about some conclusions reached by the NDU. Basically the PLA intends to adopt, to put it simply, an American model with “Chinese characteristics”.

40 Richard Fisher; (2006); “Top Ten Chinese Military Modernization Developments”; Available on http://www.strategycenter.net/research/pubID.65/pub_detail.asp (accessed on September 9, 2007).

can succeed in absorbing foreign technology to enable the production of equal or better next-generation weapon systems – an area where the results have been ambivalent.

Between 1992 and 1995 China purchased \$2.58 billion in weapons, between 1995 and 1999 \$3.59 billion, and between 2000 and 2003 China a total of \$10.26 billion.⁴¹ In the last four years, this rate has been sustained at about \$2 billion a year.

According to Richard Fischer, due to the foreign and “external and internal synergies” the PLA process of military modernization has been developed in ten general areas with great success globally, but in our opinion with more success in the strategic areas than in the operational ones⁴²:

- (1) “Informationalization”;
- (2) High Technology and “Assassin’s Mace” Weapons⁴³;
- (3) Military Space⁴⁴;
- (4) New Intercontinental Ballistic Missiles and Submarine Launched Ballistic Missiles to defeat U.S. Missile Defences;

41 Stockholm International Peace Research Institute, “Transfers of Major Conventional Weapons to China, 1994-2003”. Available on http://web.sipri.org/contents/armstrad/trend_ind_CHI_94-03.pdf. (accessed on September 10, 2007).

42 As several senior officers from the Army, Navy and Air Force pointed out to the author without providing many details. Basically, they mentioned that their services are trying to solve problems related with the integration of the sophisticated new systems and equipment into the operational area because strategically, these systems have a great value and are a strong asset for PLA.

43 The Chinese are world leaders in nanotechnology, energetic materials, electronic materials, infrared detection, and metallurgy. They are very good at direct energy. The PLA has a large infrastructure that is focused on exploiting and attacking computer networks that will diminish the need to attack many targets by kinetic means or will magnify the effectiveness of kinetic attacks. China’s concept involves a fusion of computer network attack and exploitation with electronic warfare. In June 2007, China’s military managed to penetrate the Pentagon’s computer network, raising fears it could disrupt the U.S. Defence Department’s systems. The US gave the codename “Titan Rain” to the growing number of Chinese attacks, notably directed at the Pentagon but also hitting other U.S. government departments, over the past few years. Reports of China hacking into German government systems were also raised in late August 2007 between Chinese Premier Wen Jiabao and visiting German Chancellor Angela Merkel. German weekly *Der Spiegel* reported that espionage programs traced to the PLA had been detected in computer systems at Merkel’s office, the foreign ministry and other government agencies in Berlin. “China Hacked into Pentagon Computer Network: Report”. Available on <http://taiwansecurity.org/AFP/2007/AFP-040907.htm>. (accessed on September 9, 2007). The British Foreign Office also suffered Chinese cyber attacks in August which is described as constant ongoing problem. “Titan Rain - How Chinese Hackers Targeted Whitehall”. Available on <http://www.guardian.co.uk/technology/2007/sep/04/news.internet>. (accessed on September 9, 2007).

44 The Chinese anti-satellite test of January 11, 2007 revealed its ability to track, locate, and attack low altitude satellites and underscores China’s progress in developing effective asymmetric capabilities. Low altitude satellites are the region where many satellites supporting intelligence and military requirements are deployed. Hence, an ability to physically attack these platforms provides an opportunity to diminish the ability of the U.S. (and other nations using reconnaissance satellites) to employ these systems in time of war, or to force users to take measures to protect the satellites from physical attack that will reduce their operational effectiveness.

- (5) Strategic Land Attack Cruise Missiles;
- (6) Large numbers of Short Range Ballistic Missiles and Medium Range Ballistic Missiles;
- (7) Modern offensive combat Air Forces;
- (8) New Nuclear and Non-Nuclear Attack Submarines;
- (9) New Advanced Surface Warships; and
- (10) Growing Airborne and Amphibious Projection Forces.⁴⁵

5. What May Lie Ahead

Basically, the PLA may choose from among the following three options for implementing a further and deeper military reform:

- The PLA could concentrate all resources on mechanization and then “make a push” for “informationization” after mechanization has been completed.
- The PLA could postpone mechanization for now and rush to “informationization”.
- The PLA could accelerate “informationization” even as it intensifies mechanization.

Of course all these options have obstacles and Chinese military scientists have candidly delineated them as depending on the degree of civilian “informationization”; the level of development of national defence industries; and the status of space support infrastructure facilities. In other words, Beijing has reviewed and knows the causes and consequences of its failure to sustain past military modernization programs. For the PLA leadership is evident that:

- The PLA must have qualified personnel to I&D and operate advanced technical equipment.⁴⁶
- China’s pursuit of self-sufficiency is understood to be achievable in the far distant future. The PLA most advanced armaments are imported,

45 Richard Fisher; (2006); “Top Ten Chinese Military Modernization Developments”; Available on http://www.strategycenter.net/research/pubID.65/pub_detail.asp (accessed on September 9, 2007).

46 During the ceremony to celebrate PLA 80th anniversary, Hu Jintao unveiled new measures to attract high-tech talent for military modernization. He declared that had signed the measures to “attract and retain high-level specialist technical talent”. Engineers and scientists were “a precious strategic resource for using science and technology for a strong military”, the official announcement said. “They play an important role in military development and preparations for military struggle.” Available on <http://www.reuters.com/article/worldNews/idUSPEK855820070803>. (accessed on September 9, 2007).

but the armed forces are currently producing indigenous systems with imported components.⁴⁷

- The PLA must understand the complexity of modern warfare and have technology for it.⁴⁸

But China's accelerated push to modernize the PLA also raises an important question concerning the internal dimension of this profound military reform: What impact will such change have upon the PLA image, status, and role in Chinese society?

No matter how carefully crafted, modernization inevitably will alter the PLA sense of identity and change its relationship over time with the CCP. Modernization may foment friction between military and civilian authorities competing for political primacy and limited resources or create within the PLA divisive social issues similar to those dogging Chinese civil society generally (corruption for example). But modernization could also significantly change internal PLA demographics, resulting in a drastic alteration of the social contract that has traditionally existed between China's military and civilian society.⁴⁹

In the external front and discounting all the alarmist visions of the "panda sluggers" we can say with a certain level of confidence that today the PLA still suffers from several insufficiencies and impediments that limits its capacity of efficiently conducting its concept of "local wars under high-tech conditions". These limitations can be summarized as:

- (1) An overall organizational command structure and deployment of forces that is not yet the best suited to joint operations.
- (2) Some interservice incompatibilities.
- (3) Relative lack of air and sealift capacity.
- (4) Limited amphibious capability.
- (5) Lack of all-weather air force capability.
- (6) A modest number of blue-water-capable surface warships and submarines.
- (7) A modest counter-electronic warfare and minimal offensive electronic warfare capability.

47 Available on http://english.chinamil.com.cn/site2/special-reports/2007-08/02/content_906101.htm. (accessed on September 9, 2007).

48 Available on http://english.chinamil.com.cn/site2/special-reports/2007-08/02/content_906103.htm(accessed on September 9, 2007).

49 For an analysis of all this possible challenges see David Finkelstein and Kristen Gunness (Eds); (2007); *Civil-Military Relations in Today's China: Swimming in a New Sea*; Armonk, M.E. Sharpe.

- (8) An information warfare capability that it is rapidly developing.⁵⁰
- (9) A fragmented logistics system.
- (10) No substantial ballistic missile defence systems.
- (11) An increased but varied ability to assimilate and use new technology and equipment.⁵¹

So, when viewed in a broader regional or global context, the PLA still has limited capabilities. The PLA has exhibited little evidence of attempting to acquire a power projection capability,⁵² lacks a single intercontinental bomber, possesses a very small fleet of in-flight refuelling tankers (and needs to fully master the skill of in-flight refuelling), and airborne command and control aircraft, it has only a small number of truly blue-water capable surface combatants, it does not possess a single military base abroad, has no space-based global network of command and control and lacks other elements that one would expect to find in a nation trying seriously to develop a power projection capability or become a global military power (notwithstanding intercontinental ballistic missiles and submarine launched ballistic missiles). A close reading of Chinese military manuals and publications gives little evidence that power projection beyond China’s immediate periphery is a priority. In sum, and for now, there is no evidence - at least from open sources - of assertive PLA attempts to develop global force multipliers capacities, and even when Chinese military have them, it may still take a decade more to muster and integrate them efficiently.⁵³

The PLA will grow more powerful and that this will alter the balance of power in Asia is not a question. The intangibles are:

- (1) How quickly the PLA will be modernized.

50 It is important to remember that as the PLA becomes more dependent on the electro-magnetic spectrum for military operations it is more susceptible to interference in that spectrum. PLA warfare experts concentrated on the weaknesses inherent in the American dependence on space and information, but this dependence is becoming a two-way street.

51 For an analysis of these limitations see David Shambaugh; (2002); *Modernizing China’s Military: Progress, Problems, and Prospects*; Berkeley, University of California Press; pp. 56-107.

52 For example, the Project 9935 to build one aircraft carrier has been plagued by technological ups and downs. See Alexandre Carriço; (2006); *De Cima da Grande Muralha: Política e Estratégias de Defesa Territorial da República Popular da China, 1949-2010* (From Above the Great Wall: People’s Republic of China Territorial Defence Policy and Strategies, 1949-2010); Lisboa, Prefácio; pp. 489-500. The author had the opportunity to visit the Dalian Shipbuilding Industry Company (DSIC) where the Varyag aircraft carrier is anchored. During the briefing the DSCI CEO declared that the company was ready to do its best as soon as it receives an order from the PLA to build an aircraft carrier. This is without, doubt a national military design because all Chinese military whom the author interviewed denoted a strong support for this project.

53 For example, the U.S. armed forces take about six to eight years to integrate optimally a new doctrine or a new force multiplier.

- (2) How effectively the PLA can integrate improvements in hardware with “software” demands of training and command and control.
- (3) How the PLA’s new power will be put to use.
- (4) How the United States and other nations on China’s periphery will adapt and respond to growing regional Chinese military capability.⁵⁴

Of course, it is not wise to undervalue the tremendous qualitative advances made over the last three decades by the PLA. But we can’t forget that new military innovations are appearing in a much faster rhythm than the PLA (and the great majority of world armed forces for sure) can adapt and assimilate. So, even though the Chinese military gap is closing, it is happening not as fast as it might seem because the PLA started its “strategic transformation” from a relatively low base. Adjusting Thomas Christensen’s phrase, we think the PLA is posing growing problems to the U.S. as it is “selectively” catching up with them in some areas of military capacity.⁵⁵

The PLA has transitioned from being a third-to-second-tier military power, but it still has a long way to go before it can be considered as belonging to the first tier. Until then, the net assessment of PLA capabilities and progress of China’s military modernization program is like that of the proverbial glass of water which is simultaneously half-full and half-empty – yet the volume is rising.

This volume has consequences. In the regional security context, the China-U.S. military dynamic is more a hostage of a self-fulfilling prophecy than one may think: if Washington treats Beijing as an enemy, it will become an enemy and the same applies to China. As a result of this dialectic – if put it on a zero sum game perspective, far different from the “win-win strategy” defended by Beijing – for the majority of China’s neighbouring countries, the security problem they face can be summarized by a Southeast Asian traditional saying: “When two elephants fight, the grass gets trampled. But when two elephants make love, the grass also gets trampled.” (Southeast Asians surely have a dry sense of humour).

54 The DoD’s *Annual Report to Congress on the Military Power of the People’s Republic of China*, the *Quadrennial Defense Review*, the *Nuclear Posture Review*, and the *Global Posture Review* all intend to analyse and give some answers to these questions.

55 Thomas J. Christensen; (2001), “Posing Problems without Catching Up: China’s Rise and Challenges for U.S. Security Policy”; *International Security* n°4; pp. 5-40.

Chinese and Russian Techno-Nationalism: Some Geopolitical Elements

Heitor Barras Romana

In China and in the former Soviet Union today, the transition from socialism is a synthesis of old patterns and new realities combining privatization and marketization, cultural liberalization and a opening up to the outside world, authoritarianism and nationalism (Mark Luper, 1996:3).

The build up of a new era has brought a huge challenge to both societies and their political elites. China and Russia have created a system which combines Weber's neo-patrimonialism and neo-authoritarianism, supported by a kind of Adam Smith' "invisible hands". This unpredictable balance has a very important outcome: the emergence of highly skilled technocratic groups closely connected with their political and military leaders and who also enjoy good relationships abroad with different western countries.

These groups' nationalistic discourse is based on economic modernization, which is the "glue" that holds their positions within their countries' political apparatus.

China: strategic goals and techno-nationalism

The emergence of China as a global player is the main goal of China's leadership toward the 21st century. This transition will be carried out through the building up of a calculative strategy based on economic modernization, military development, strengthening of external influence and a nationalist ideology that functions as a mobilizing factor in face of the fading out of the socialist model (Heitor Romana(2005).

From a realistic standpoint, a great power's behavior is determined not so much by its intentions but by its capabilities.

In the particular case of China, the calculative strategy pursued is a balance between a gradual economic and diplomatic capacity and a more assertive desire to improve its position as a player in the world system

Such strategy embodies the following four key-elements:

- a) adaptation of Party-State system to functional reforms based on a neo-Leninism organizational model;
- b) envisioning the market as means of creating the image of China as a good partner;
- c) a soft approach to strategic culture concerning the peripheral states;
- d) regional and global participation in several *fora*, bearing in mind a new multilateralism approach to the international system.

The Chinese global strategy was designed using a gradual model based on the balance between the fourth and fifth generation of political leadership. China's center of power has been preparing the country for new political, economic, and social challenges that include what we could call "*the eight managements*":

- a) The management of the transition in political leadership;
- b) The management of energy needs;
- c) The management of the gap between the coastal area and the hinterland;
- d) The management of a more assertive PLA;
- e) The management of contradictions between a Leninist state apparatus and the need for a more flexible government structure;
- f) The political and economic management of Chinese business firms' internationalization;
- g) The management of geopolitical projection to Africa and its role as a centre for "South-South" relations, competing with India;

h) The management of an engagement rather than a contending relationship with the US.

For the general Secretary of the Chinese Communist Party, Hu Jintao, the control of those eight issues has become crucial in light of a new era when authoritarianism and the preservation of power are crucial.

Therefore, in the development of his strategy, Hu Jintao is trying to set up what we call the “*Fifth Generation technocratic support team*”.

This group shares the idea of China as a great civilization as well as a nationalistic ideology. The State and the Nation, more than the Party, are the reference that can mobilize Chinese society.

Despite this nationalistic focus, the technocrats of Fifth Generation are seeking to show the world that China is a global player in both the political and economic arenas.

Most of the techno-nationalists are entrepreneurs and state managers in several economic areas, such as: energy, aero spatial industries, telecommunications and biotechnology (SINOPEC, China Mobile, China Construction Bank, Shanghai Baosteel Group, China First Auto Works Group, China Aerospace Science & Technology Corp., China National Petroleum Corp., Sanjiang Space Group, Shanghai Fosun High Technology Group, China Netcom Corp., China Netcom Corp., etc). This reality is stressed by the following analysis by Cheng Li (2005):

«China is in the midst of major changes. As a result of the rapid rise of the private sector in recent years, most ambitious young people are no longer considering political officialdom as the best channel for their upward mobility. Interestingly enough, most of the children of the third and fourth generations of leaders are engaged in business. Almost none of the children of current prominent leaders pursue careers in party or CCYL affairs. Instead, many currently serve as CEO's, trustees, general managers, and partners of major business firms. This suggests that the channel of elite selection – the game for competing for political power – in China may profoundly change in the future generation.... The most important challenge for the upcoming reshuffling is whether the top Chinese leadership can be open enough – and bold enough – to allow talented young people to become part of the ruling elite. The prevailing sign from the Chinese authorities at present, however, is at best a sense of caution and control».

Thus, the presence of the “Yuppie Corps” in the 17th Chinese Communist Party Congress that was held from 15 to 21 October 2007, was an important signal of a leadership change towards a neo-reformist strategy. This strategy combines a more open party and new social groups within the framework of a *quasi* “corporate State” with a gradual engagement in international issues.

Russia: the case of techno-Eurasianism

Russia’s transition is mostly related to the geo-strategic goals of the Kremlin leaders.

For the Russians, one critical goal is to increase economic growth and project Russia as a global power, mainly through an aggressive “energy diplomacy”. However, we can identify some problems in the fulfilling of Putin’s aims, such as:

- a) The power struggle among the Kremlin factions;
- b) The assertive approach to neighboring countries;
- c) The geopolitical insecurity – Russia is part of Europe, Asia or it is the core of Eurasia?
- d) The borders in geographical – national imagination;
- e) The position of Russia as a post-imperial power or as a transitional power.

The Kremlin’s dilemma is set on a paradox: its domestic political system requires isolation, but sustaining power requires the wealth generated by participating in the globalization process. Thus, how can Moscow deal with the international context of globalization and yet sustain patrimonial authoritarianism at home? The answer is trans-imperialism, in the words of Celeste Wallander (2007).

Trans-imperialism is based on a form of political – economic management highly dependent on personal relationships. Is also a form of geopolitics through commercial and transnational seller-client relationships (Celeste Wallander, 2007)

Despite struggles within the Kremlin (liberal versus neo-nationalist/silovikis), Putin has been able to succeed in managing a new generation of technocrats with very good academic skills, mainly on economic and engineering fields, extensive experience in management and with important network con-

nections in Russia and in several other countries. This new elite is also a product of liberal and neo-nationalists/siloviki insights on the role of technocrats in the Russian economic and technological projection of external power

The liberal technocrats are led by the current President of Russia (former First Deputy Prime-Minister and Gazprom chairman), Dmitry Medvedev. and the new Gazprom chairman, Miller Alexey Borisovich. On the other hand, Siloviki are a mix of nationalist technocrats and intelligence officials. The technocratic group within the siloviki faction is led by Sergei Bogdanchikov, the president of the state-owned oil giant Rosneft.

Both liberal and siloviki defend a more assertive Russian foreign policy and the control of national economy by Russian tycoons. They all share a nationalist ideology supported by the modernization of armed forces and the recovery of Russian pride. They believe that Russia should regain the respect that the Soviet Union once enjoyed in international affairs. In this sense, the re-emergence of “Euroasianism” is seen as the outcome of “techno-nationalist geopolitics” and the answer to those who are seeing the end of Soviet Union borders as the end of Russian power.

Like Germany, Russia has also traditionally been a geographical concept. Its external borders have defined its cultural and international identity, and its internal territorial organization has been intimately linked with the nature of the country’s political regime (Dmitri Trenin,2005:1)

Eurasianism is the assertion of a distinct civilization space for Russia, separate from the West and from Asia. After an initial “western-liberal” period in the early 1990s, when the idea of Russia “rejoining western civilization” was paramount, Russian foreign policy discourse tilted towards a vague, yet politically vital, Eurasianism. Embedded in the Eurasian approach, we can find what G. Smith, 1999, quoted by John O’Loughlin et al.(2007:1-3), defined as the creed of “statism” or official Eurasianism.

As the author stresses, this “statism” combines elements of western-style democracy with Russia’s strong state politics. The “statism” that supports the technocrats nationalist ideology sees Russia as a distinctive civilization, different from the West in its cultural values and geopolitical security concerns and interests. They consider Russia a Eurasian power with its own unique national interests and concerns. Its dealings with the West should be driven by pragmatism and realism. This Russian nationalism is based on a longstanding history of “statism”, which grew up around authoritarian centralization, impe-

rial expansion and the domination of civil society and public life by a coercive state.

“Statists”, like “westerns”, view weak economy and widespread poverty as the main threat to national security. Therefore, the task of Russian foreign policy is to ensure favorable conditions for enough economic growth to bridge the gap between Russia and the West as rapidly as possible.

China and Russia: techno-nationalism and geopolitical discourses and cultures

In Russia, the emergence of techno-nationalism is the outcome of a transition from a totalitarian to an authoritarian regime and finally to a “managed democracy”, whereas in China the phenomenon is at a different level in terms of political transition.

Actually, the combination of the technocratic approach to modernization, with the recovery of nationalistic ideals, is more a way to bridge the gap between the fadeout of socialist ideology and the elite mobilization around a nativist approach to modernization. In other words, while Russia’s techno-nationalism is partly Russia rebuilding its position in the geopolitical and geo economic arenas in the aftermath of the collapse of communism, in China techno-nationalism is part of the leadership strategy towards the maintenance of the power system.

The collapse of the Soviet Union was caused by the legitimacy crisis following economic stagnation and rapidly introduced market measures. China, though, has been able to overcome its moment of crisis and resume the path of reform. Taking a more gradual approach, China has been able to produce sustained growth and, thanks to its ideological reconceptualization, retain legitimacy. Over the past decade, the CCP has proven itself able to carry through substantial reforms and to improve the material conditions of the country, which generates greater support among the masses. Simultaneously, the party is transforming, becoming less dogmatic and bringing members of the new elite into the party ranks. Today’s party leadership is quite different from that of the 1980s in terms of personalities and views. In the beginning of the twenty-first century, China is quite different from what it was in 1989 and, for that matter, its circumstances are radically different from that of the Soviet Union in its final days (Christopher Marsh, 2005:8).

In a synthetic geopolitical exercise using the critical approach on geopolitical analysis, it's possible to identify a techno-nationalistic influence in the geopolitical discourse and geopolitical culture of China and Russia as well.

All states, as territorially embedded entities with distinctive histories and geographies, have geopolitical cultures. These cultures are formed not only by state institutions, the country's historical experiences and geographical location, but also by the networks of power within society, debates over national identity, prevailing geopolitical images, codified geopolitical traditions, and the institutional processes by which foreign policy is shaped by the state.

The geopolitical discourses are public articulations and narrative codifications of the elements that make up a geopolitical culture. Three related genres of discourse are identified in critical geopolitics: professionalized narratives about foreign policy; practical geopolitics developed by diplomatic tools, and popular geopolitics, or the narratives about world politics that find expression in popular opinion and popular culture (O'Loughlin et al. 2007:3-4).

In what concerns China's geopolitical discourse and geopolitical culture, we must stress the existence of a combination of formal and practical geopolitics as an expression of a "steering" approach to China's role in regional and global arenas. The traditional "Confucianist reading" in the building up of a foreign affairs strategy is a mark of Chinese geopolitical culture which focuses on a paternalistic view of the international system. For the techno-nationalist generation, the geopolitical discourse must be a balanced combination of tradition, nativism and pragmatism as the axis of a global ideology-strategy towards the 21st century. Pragmatist strategy is therefore ideologically agnostic, having nothing, or very little, to do with either communist ideology or liberal ideals. It is a firmly goal-fulfilling and national-interest driven strategic behavior, conditioned substantially by China's historical experiences and geo strategic environment (Suisheng Zhao, 2004:4).

In terms of Russian formal, practical and popular discourses, it seems quite clear they are greatly influenced by the idea of the return of a "great civilization" that doesn't accept Western hegemony. In a short exercise on content analysis, we could see that the geopolitical discourse is shaped by the "Russian Eurasian role" as a geo economic gateway – another role for the Russian Heartland – headed by a number of energy technocrats.

The Russian geopolitical culture has also moved towards a mobilization process of national identity whose main target is, at present, to put pressure on neighboring countries and try to keep them within Russia's circle of influence.

Conclusion

China and Russia have now a more assertive position. This is due to the emergence of technocratic elites who have a wide vision of their countries' role in the global scene and who must be seen as "challenge players" with great influence in the decision-making process within their own countries.

In both cases, techno-nationalism has as main strategic goals:

- 1) To achieve a better position in the technological race in terms of the competition with the USA, Japan and the EU;
- 2) To lead the national economy towards a faster modernization and a consequent leadership of global trade;
- 3) To use the modernization goals as national mobilization ideology.

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Russia's Policy in East Asia

Maria Raquel Freire

Introduction

Russian politics under Vladimir Putin, sustained on the vertical power formula, based on a strong hand at home and the so-called “managed democracy”, express well the country’s current trend of affirmation and regaining of influence, both internally and in its external dealings. This option has allowed some continuity in Russian politics, despite the ups-and-downs resulting from the need to adjust to an all-adapting international context throughout the post-cold war decade (1990-2001). The Yeltsin years were mainly characterized by Russia’s struggle to find and define its new place after the breakup of the Soviet Union (see Freire, 2007: 70-72). However, underlining the many difficulties, there was always the aspiration to a “great role”. If it was an aspiration then, with Putin it became more than that. The 09/11 terrorist attacks in the United States constituted, however, a turning point in the international scenario, leading to new developments in the post-cold war setting. The United States became prominent, putting forward an assertive agenda. Russia reacted and followed, adding a more affirmative stance to discourse and action.

This paper analyzes Russian foreign policy, with a focus on East Asia, understanding it as an expression of Moscow’s wish for affirmation and international recognition of its role in regional and global politics. With a focus

on the political-security and economic dimensions of the process, including military and energetic issues, this paper looks at the course of Russian policy-making, bargaining, demands, concessions and trade-offs in terms of active political engagement in East Asia. The goal of this paper is threefold: to identify the main dynamics at play, how these intersect with the Russian search for regional affirmation, and Moscow's possibilities and limits in the East Asian game. The argument rests on the assumption that the Eastern dimension in Russian foreign policy is assuming increasing relevance, and that despite the more assertive traces in Russian foreign policy, mainly sustained by a much profitable energetic sector, added to hints of pragmatism, has nonetheless been much a policy of reaction. It has been very much formulated as a negative reactive dynamic to events. However, these same events have been catalyzing proactivity, particularly associated to the Russian course of affirmation, which in the current international context demands not just creative dealings, but the gaining of international recognition and legitimacy (which in their turn requires explicit action).

In addition, the search for preponderance in regional terms and for enhanced influence in global politics fits well with the emergent power image of Russian politics, an image built and promoted by the Kremlin, with concurrent approaches and means in East Asia conferring global contours on regional policies in the area. Russia, along with China, India and Japan are key players in East Asia, but in an imbalanced game where China and India are powers on the rise, Japan is much dependent on the West and Russia is still struggling for affirmation, playing with means and capabilities; the Shanghai Cooperation Organization (SCO) is a fundamental institutional framework at scene, combining shared concerns but not always shared goals; and the United States (US) an unavoidable player further constraining/promoting regional dynamics of cooperation/competition.

Pragmatism and realism have, in effect, demonstrated their adequateness as adjectives to qualify Russian foreign policy. In East Asia, Russia faces contradictory interests, differentiated goals, and imbalanced power projection, along with cooperation opportunities that frame its policy options in ambiguity and a difficult range of choices. These intersecting and at times cooperative and other competitive interests are here focus of analysis.

The Eastern dimension in Russian foreign policy

Since gaining the Russian presidency in 2000, Vladimir Putin has defined its foreign policy as multi-vectorial and multilateral. The main documents adopted at the beginning of his first mandate state the potential destabilizing role of a “unipolar structure of the world with the economic and power domination of the United States”, the Commonwealth of Independent States (CIS) as an area of strategic importance and the Eastern dimension (the Asia-Pacific region) as a relevant region in Moscow’s external policy (National Security Concept 2000; Russian Military Doctrine 2000; Foreign Policy Concept 2000). Thus, Russia seeks for a balanced foreign policy where the search for multiple poles aims at diversifying allies and allowing the shifting of privileged relations in a constant search for counter-balance and primacy. However, by enlarging the package, Putin also got added leeway, playing with these different dimensions to his best interest and in the broader game of projecting power in a growing interdependent international order (Freire, 2008).

President Putin’s power and powerful saying in foreign policy have managed to transform internal discourses in a unified foreign policy, allowing some coherence in both wording and action. The centralized ruling as a guarantee of stability and the toughening of politics as an assurance of order are signs of an authoritarian legacy still much present in Russian policy-making. While still carrying many elements from yesterday, today’s Russia, despite growing political assertiveness, in parallel to military empowerment, centralized ruling and repressive measures, is a new Russia, seeking for affirmation and regaining of influence in a changed context. In the words of Yevgeny Primakov, “[b]y strengthening, under the pressure of circumstances, its strategic and tactical military potential, Russia demonstrates its desire to become a main stabilizing force in the world” (Primakov, 2007: 69).

September 11 introduced a new element in this foreign policy layout: a new international order under the primacy of the US. This allowed two simultaneously different trends: the projection of Russian policies with its voiced support to the US fight against terrorism, and an acknowledgement of the need for reaffirmation of its role and status in international politics. Its responses to US primacy and revisionist posture after 9/11 have shifted between cooperation and competition, in an effort of affirmation in an unfavorable context (where China and India are powers on the rise). However, in this changed context, the Russian strengthened strategy towards East Asia has been described as the “peaceful offensive at Asia” (Ivanov, 2006: 54), implying a deeper involvement

of Moscow in the processes in the area as a way of empowering its influence and projecting its power.

The new foreign policy lines, as defined by President Putin, point to a more realistic assessment of Russian capabilities and possibilities and seek to transform idealist illusions into concrete achievements. "The only realistic choice for Russia is the choice to be a strong country, strong and confident in its strength, strong not in spite of the world community, not against other strong states, but together with them" (Putin, 2000). These goals have been translated in the option for a multilateral approach in foreign policy, which should fulfill the role of advancing Russian domestic interests abroad, and a sharper focus on regional dynamics. In East Asia, the growing focus on the SCO and the more recent agreement over closer cooperation between the latter and the Collective Security Treaty Organization (CSTO), is an example, as further analyzed. These underlining trends reveal also a shift in the understanding of foreign policy in Russia as driven by the focus to establish an alternative pole to the West (as a remnant of cold war thinking) to an acknowledgement of an independent and autonomous course (see Sakwa, 2008: 276-277). This has been translated into Moscow's multivectorial foreign policy, with the western and eastern vectors playing together, though not in concert, in Russian political options.

Despite an increase in the eastern front, the western dimension in foreign policy still remains central. Nevertheless, new opportunities and the sharing of security and political-economic concerns in East Asia have led to added value in Russian policy formulation. This has been evinced in differentiated contexts, but the words of Aleksandr Medvedev, Gazprom's Deputy Chairman in charge of exports, summarize well the reach and implications of this Russian eastern option: "it is no secret that we want to be the biggest supplier of natural gas to the Asia-Pacific region" (Moore, 2007). In parallel to these developments, the economization of foreign policy is thus a concretization of the new realism in Russian foreign policy (see Sakwa, 2008: 275). Economic security with an emphasis on energetic-related dealings has assumed primacy in the Kremlin. "Multilateralism and regionalization became the overlapping principles of security arrangements for Russia. (...) These principles provided a solid base for the proclaimed policy of the so-called economic determinism" (Isakova, 2005: 110-111).

With a realist look over Russian national interest and external policy priorities, the so-called "pragmatic nationalism" (Light, 2003: 48), Vladimir Putin power projection and affirmative course rests on an internal stable order and economic growth, mainly sustained by increasing oil and gas revenues,

which have been conferring more independence and self-confidence to Russian policy regarding its role in international affairs. This course is acknowledged by Russian authorities, with Foreign Minister Sergei Lavrov stating that “Russian foreign policy today is such that for the first time in its history, Russia is beginning to protect its national interest by using its competitive advantages” [energy geopolitics] (RFE/RL 2007, 21 March). However, “Russia maintains some of the trappings of a Great Power – it has a wealth of natural resources, a large arsenal of nuclear weapons and a territory that covers much of the Eurasian landmass – but the Russian economy remains roughly the size of that of Belgium, and Russian social stability indicators (life expectancy, unemployment, healthcare, etc.) show that the country is far from fully developed” (Bremmer, 2003: 238). These internal handicaps have, nevertheless, been played by Putin to Russia’s favor, by seeking to identify sources of potential and rendering them operational, and building on what Russians consider makes them different. “With enormous reserves of hydrocarbons and other natural resources, enjoying huge technological and cultural achievements, and with an history as an ally in the defeat of continental dictators, Russia considers itself different from other medium-ranking powers” (Sakwa, 2008: 267). This pragmatic assessment, together with the understandings of a glorious past and expressions of comparative advantages running from differentiation, has worked as catalysts for Russian affirmative course.

East Asia has become an area of intersection of different interests rendering it complex contours. By assuring a margin of maneuver in political-diplomatic and economic terms, Moscow pursues simultaneously the goal of keeping this area as a special area of influence, and of counterbalancing and having a say regarding particularly China and India’s emergence as regional powers, Japan’s economic place and the US presence in the region. This balancing has encompassed, therefore, contradictory tendencies of favoring the US, with regard, for example, to the stationing of troops in Central Asia, but also of restraint as to the extent and quality of this presence. As for the Asian dimension, the major powers have been under Moscow’s close scrutiny, but Central Asia remains the preferential area for increased involvement and influence, with Moscow seeking both to assure energetic resources and to restrain the western engagement in the area.

Difficulties to the west have to some extent promoted rapprochement between Russia and China, as well as India, though the latter to a minor extent. How cooperative frameworks will be empowered remains open due to the bargaining and complex geostrategic game, particularly with regard to energetic

resources. Security issues, political sidings and economic matters are part of this game, either constraining options or opening new avenues for cooperation. The patterns change, mainly due to competing approaches, but it seems to be an underlining trend to see further collaboration in the east whenever relations between Russia and its western counterparts sour. This is a form of enhanced leverage, though limiting, due to the political confrontation between two giants, both Russia and China desire to obtain primacy in the region. Thus, the strategy is: cooperation when possible, though rivalry and competition are always present.

Triangulating power?

The post-September 11 primacy discourse of the US elicited a tougher and more assertive position from Russia. Simultaneously, it has been promoting rapprochement to the east, with the triangle formed by Russia, China and India gaining consistency. In fact, "India, China and Russia account for 40 per cent of the world's population, a fifth of its economy and more than half of its nuclear warheads" (Page, 2007), conferring on this triangulation of power interesting contours. The idea of a "strategic triangle" between Moscow, Beijing and New Delhi was put forward back in 1998 by former Russian Prime Minister Yevgeny Primakov, at the time of his visit to India, as a "force for greater regional and international stability" (Pant, 2004: 313; AFP 1998, 21 December; RFE/RL 1998, 21 December). Thus, this policy of balancing in East Asian politics is not a new post-September 11 trend, though it has certainly been reinforced after the 9/11 tragic events and the context that followed. However, this rapprochement seems more the result of a negative dynamic of countering US primacy, than being genuinely built over shared principles and common endeavors. A solid Russian-Chinese rapprochement, despite growing contacts, does not seem to have a far-reaching effect given the regional dynamics of competition, particularly regarding energetic sources and power projection (see Lo, 2004; Katz, 2006). In addition, Indo-Chinese rivalry also does not augur well for a collaborative triangulation of power.

The different weight of these different powers results in an isosceles triangle, where power relations are not equilibrated and where the linking arrangements in political, security and economic terms also differ. Although the potential for cooperation in economic and military terms is substantial, political and social factors hamper a relationship embedded in geopolitical

constraints. Issues related to minorities, illegal migration, and competition for regional affirmation between giants are example. Nevertheless, the agendas have been dominated by the powerful drive to balancing US weight, based on the assumption that “the more that Russia and other Asian nations can cooperate with each other in creating a multipolar system in this region, the more Russia and others hope they can limit the United States to pursuing goals they all (especially Russia) approve” (Katz, 2006: 147). A position that has been reaffirmed over time, with the recent trilateral summit in October 2007 defining cooperation as “beneficial to the process of global multi-polarity”, and stressing the counter-US trend along with shared support for the UN. The three also acknowledge their role in the contribution to “world peace, security, stability and prosperity” (Joint Communiqué, 2007), demanding therefore the curtailing of US hegemonism.

This follows their sharing of the multipolar and terrorism-fighting discourse, which has led to a common position. They have also taken the same path regarding Iraq in 2003, and share a common approach towards Iran, hold important commercial ties, particularly in military and energetic terms, and preclude from interference in internal affairs, such as Chechnya, Xinjiang or regarding instability in northeast India. In this context, Russians state that “[m]ultidimensional, mutually beneficial cooperation has become a distinguishing feature of relations with our greatest Asian friends – China and India” (Ivanov, 2003: 37; see also Khana, 2005: 21-27). Russia’s Energy Strategy to 2020, approved in May 2003 refers explicitly to a regional dimension, demonstrating the understanding in the Kremlin of the energetic asset as not unidirectional, since Russia is a producer, which confers on it leverage, but it is also a seller, which demands negotiation flexibility. In addition, if regionally framed, the energy issue might play to Russia’s favor in its policy of affirmation, as seen regarding for example in squeamishness between China and Japan for accessing pipeline routes of Russian origin.

The state of play of Russia’s policy in East Asia

Putin has been pursuing a policy of building closer ties with China, in the strategic partnership line, but crafting it as “a non-alliance, a non-confrontational relationship that targets no third country” (Pant, 2004: 315). A cautious approach that underlines two differentiated but inter-related dimensions: avoiding an enhanced role of China that might put into jeopardy Russia’s

place in East Asia, and a counterbalance to the US that should, however, not completely undermine relations with Washington.

China and Russia share many concerns and policy goals, particularly in the areas of defense and military technology, where trade ascends to significant levels, demonstrating the level of interoperability in arms related technology and production, though not quite a two-way diversified commercial relationship; but also in energetic issues, with production and transportation assets high on the agendas; in concerns regarding the growth of ethnic nationalism and radical Islamism throughout Asia; in political and cultural rapprochement as the basis for the crafting of closer ties, such as exemplified by the promotion of 2006 as the year of Russia in China and 2007 as the year of China in Russia; and in promoting a multipolar order, which implies balancing US power in the region.

On 16 July 2001, Putin and Jiang Zemin signed the “Good Neighborly Treaty of Friendship and Cooperation”, establishing the framework for bilateral relations and focusing mainly on countering US hegemonism and the spread of radical Islam in Central Asia; territorial aspects paving the way for the solving of the border dispute and clearly acknowledging Russia’s support to China over Taiwan; along with arms sales, technology transfers and raw materials. This follows the fact that traditionally China has been the largest arms export market for Russia (Isakova, 2005: 107). However, the Treaty was criticized for coming close to a regulatory mechanism for arms sales (Cohen, 2001), while the Russian press called it the “oil and gas” summit (Herspring and Rutland, 2005: 286). Nevertheless, Russian arms sale and technological cooperation, and joint military exercises have assumed a regular character. But despite regularity and continuity in contacts, the fact is that the levels of overall economic interdependence are not striking. The Chinese economy is two and a half times the size of the Russian, and the volume of Sino-Russian trade is just 2% of China’s total foreign trade (Moore, 2007). While in East Asia the volume of US commercial trading ascends to \$US 55 billion, Russia’s values are much lower, matching not more than \$US 2.5 billion (Herspring and Rutland, 2005: 287). And this same ratio applies to the US and Russian commercial relations with China, rendering Moscow a minor place as a commercial partner of Beijing.

These shared goals are, however, underlined by a continuous rivalry and competition dynamics, with the limits dictated by geography on these two immense neighbors, adding to fears about growing power of the other, understood as threatening. In this context, Russia plays with what it considers the limits of its engagement with Beijing in terms of military technology,

avoiding (a threatening) China in military terms. “To Moscow, the notion of an economically powerful China with a military in a better state of preparedness than Russia’s is inconceivable” (PINR 2007). Chinese cross-border immigration to Russian Far Eastern regions has also been understood as a threat to Russian national security, with concerns voiced regarding an acculturation of low inhabited Russia regions bordering China (non-confirmed sources point to 600,000 Chinese entering Russia every year). This concern remains despite the signature of the Sino-Russian border treaty settling long-time disagreements, along with the Sino-Russian Joint Declaration on the International Order in the 21st Century, in July 2005, described as demonstrating “a concurrence of fundamental views” (Rogachev, 2005: 85).

Regarding Russian relations with India, these are less strained than those with Beijing, and rely upon Russian collaboration and supply of military equipment and technology to India (for example, an arms agreement was signed in December 2000), along with joint efforts towards the containment of cross-border illegal activities, including counter-terrorism cooperation. Bilateral trade has nevertheless been declining, demonstrating a low economic interdependence to the exception of energetic and military assets. India’s “look east” policy is in full swing, driven by energetic and commercial considerations, counter-terrorism and Islamic radicalism, and the stabilization of its neighborhood (Bajpae, 2007). Launched back in 1992, this policy matched India’s post-cold war resolve to act in multiple fronts. It also carries with it geopolitical considerations about the growing power of China. Despite collaboration in joint military exercises, for example, distrust persists. Rapprochement to the US has been noticeable – “US commitment to help India emerge as a ‘world power’ by assisting India’s military modernization as shown by the signing of the ‘New Framework for the US-India Defense Relationship’ in 2005” (Bajpae, 2007; see also Lavrov, 2007: 24-29), along with the signature in March 2006 of a nuclear deal, are examples. Nevertheless, this rapprochement has to a large extent been part of an Indian effort to fight China’s rising power in East Asia. India sees Chinese moves at developing energetic routes in Pakistan, Bangladesh and Myanmar as “part of a ‘string of pearls’ strategy of economic and military encroachment into South and Central Asia” (Bajpae, 2007). In addition, “[a]s India and China seek energy access in Central Asia – a region dominated by Russia – India’s close position to Washington may cause Russia to favor China or Japan in upcoming oil and gas exploration and pipeline deals” (PINR 2006). Therefore, there is always an underlying tension to this triangular relationship, where flexibility is an essential ingredient to balance divergent interests.

As for Japan, the Kuril Islands dispute (the Northern Territories for Japan), occupied by the Soviet Union in 1945, remains a major issue of disagreement. The Islands, rich in fishery, are also said to be rich regarding offshore reserves of oil and gas. Despite efforts at finding a solution, and increased contacts at diplomatic level to the effect, there has been no success. However, the relationship between Moscow and Tokyo surpasses to a large extent this territorial dispute, as well as the fact that the parties have not signed a Treaty of Friendship, with a focus on pragmatic cooperation issues, including trade and energetic assets. In this regard, cooperation in investments in the Russian Far East, where Japan supplies the technology, and the development of joint energetic projects, such as Sakhalin-1 and Sakhalin-2 (oil and gas), are examples (see Mito, 2000: 10).

Nevertheless, the Japanese alignment with Washington is disapproved by Moscow, and the latter's moves to deploy the missile defense shield also in Japanese ground have further stigmatized relations. Russia argues this move could trigger an arms race in the region with growing potential for destabilization. Japanese Foreign Minister Masahiko Komura has stated that "under the current Japanese constitution we have purely defensive power, a shield to protect ourselves when the country is attacked. (...) And I would like to make it clear that we are absolutely not envisioning an attack from Russia" (Komura cited in Reuters, 2007). Russian Foreign Minister Sergei Lavrov replied that "Japanese-US cooperation in missile defense is cause of concern for us. We are against the creation of a missile defense system as a means of achieving military superiority. The deployment of such a system will spur an arms race, both regionally and globally" (Ria Novosti 2007, 13 October). This issue should be understood in the broader framing of US primacy in global affairs and the Russian moves to counter it.

Russia has been reacting to US assertiveness also in assertive terms, both in words and actions. It has been testing new armaments with high potential for destruction and considerable distance reach, such as a new inter-continental ballistic missile, the RS-24 or a thermobaric device – "the launch comes at a time when the country is attempting to reestablish itself as a strategic leader in the global military balance of power" (PINR 2007, 1 June; RFE/RL 2007, 1 September; RFE/RL 2007, 12 September). In this highly tension context, President Putin has affirmed Russia will proceed with its weapons development program, in the context of the nuclear triad (strategic missile forces, strategic aviation and nuclear submarines), and other kinds of weapons (Ria Novosti 2007, 18 October).

For some, this Russian militarization comes as a reply to what Russia sees as a blind-ally situation. “(...) Russia has no alternative in the new system. It can hardly make a strong and durable alliance with China (for demographic reasons) or India (New Delhi also became US-oriented quite a while ago) ... and there are no reliable partners on the horizon, other than Western countries” (Polikanov and Timmins, 2004: 231). It seems, however, too dramatic a scenario in the face of the existing potential in the area for cooperation, though nevertheless acknowledging the many competitive trends also present. But Russia cannot simply turn its back on East Asia, an area of much relevance in its policy of affirmation and where, despite adversity, Moscow has continuously to remember its parties it is a player in the game.

The Shanghai Cooperation Organization: balancing, projecting or trading-off power?

The Shanghai Cooperation Organization (SCO), founded in June 2001, following the “Shanghai spirit”, and based on mutual principles of trust, the search for joint benefits, equality among its members, consultations and respect for diversity, is aimed at promoting collaboration in security and military issues, including becoming a significant regional military area (Kapila, 2006). This demonstrates the moves to foster regional inter-linkages, described officially as a result of the regional effort at further integration and not directed at countervailing US primacy. Thus, the Sino-Russian relationship is, therefore, under Washington’s close scrutiny. While the US understands the difficulties in empowering a strategic partnership between Russia and China (two competing powers in the region), it sees with caution rapprochement between the two giants. “Russia and China have been successful in using the USA’s strong aversion to terrorism since 9/11 for their own ends – to tackle Islamic insurgency within their territories” (Pant, 2004: 315).

However, “[n]ot only are Russia, China, and India too weak to balance US power in any significant measure, the allure of US power remains too strong for them to resist” (Pant, 2004: 313). Thus, the idea of a solidly built “strategic triangle” seems still far away. US policies have driven Russia and China closer, and India has joined the duet owing to its long term and long stated concern regarding the need for a multipolar world order. However, it seems clear that “Russian policy towards Asia is not the result of doctrine, but is based on pragmatism, and dynamic policies in this area are balanced by the obvious

domination of its European policy” (Slezneva, 2003: 19). Thus, this regional engagement seems to reflect a feeling of western challenging to natural areas of influence, of a particular relevant strategic nature, such as Central Asia and the Caucasus. But one cannot ignore the fact that these same areas are subject of regional competition, and of a weight-measuring game between Russia and China, where power politics play a fundamental role. But as Russia bandwagons towards the US, China does the same, avoiding to be marginalized from the international security dealings, playing for example an active role over negotiations with North Korea, a role very much appreciated in Washington (Pant, 2004: 324).

This same reasoning applies to the possibilities and limits of the SCO, since “[t]o a large extent, common, positive targets are absent. For example, China is seeking markets and energy resources; Russia is eager to regain its leadership status within the CIS [Commonwealth of Independent States] as well as that of a superpower in the international arena; and the Central Asian regimes consider the SCO as their guarantee for political survival” (de Haas, 2006). Thus, the possibilities are all open, and the geostrategic game is still being played. It should be noted, however, that “(...) cooperation among its members and observers is essentially based upon a negative strategic objective: to counter US and western influence. To a large extent, common, positive targets are absent” (*Ibid*).

The SCO underlying goals include, therefore, keeping control of Central Asia and limiting US influence, providing an institutional context to counter terrorism and foster security related cooperation in the area, offering an institutional balance to the Russian-Chinese power, and to an overall balancing of differentiated interests in competition, working as a containment instrument. An example is the inclusion of Pakistan as an observer, upon insistence by China, to balance against a potential Russian-Indian area. Simultaneously, as part of Russian attempts at reversing of the prominent Chinese power within the Organization, Russia developed efforts to join the Collective Security Treaty Organization (CSTO) to this format. In October 2007, the two forums agreed to broaden cooperation. In addition, in July 2007, and following a proposal by Putin, the SCO founded the “Energy Club” to coordinate energy strategies. It includes large producers, such as Russia, Kazakhstan, and Uzbekistan plus large consumers, including China and India, following a strategy of uniting energy producers, consumers and transit countries with the aim of increasing energy security (de Haas, 2007; Luzyanin, 2007). Thus and besides containing each other, the SCO framing also allows for containment of the US.

In August 2007, the SCO member states signed a “Long-term Agreement on Neighborly Relations”, focusing on energy, security and cooperation, and consisting of an extension to the regional integration process. Together with large military operations in the context of the SCO, such as the Peace Mission 2007, involving all members (RFE/RL 2007, 17 August), it seems SCO is becoming a leading regional organization, building on the potential of its state parties and projecting power in the regional game. However, it also contains elements of restraint and “[t]here is still, at the root, a fundamental mistrust among the members of the cooperation group and that mistrust about the intentions of Russia – of China particularly – amongst the smaller members of the group is really the key flaw in this organization” (Innes-Ker cited in Pannier, 2007). Nevertheless, the trading-off resulting from further rapprochement regarding US containment may work as a fundamental catalyst for joint collaboration, further enhancing the SCO’s role in East Asia, following a rapid affirmative course. Thus, again, anti-US feelings might be sufficient driving forces in the current regional context to allow for the strengthening of this cooperative framework, playing a double restraint game: regarding relations among its members and the US.

Conclusion

The Russian foreign policy course has been pursued both in a proactive manner, as a foreign policy goal of regaining international recognition for its status as a great power, and in a reactive mode regarding international developments, fast-moving and requiring quick adjustments, overcoming frailties and projecting an image of self-confidence and powerful saying. Thus, Russian foreign policy, assuming gradually a more assertive tone towards international affirmation, is the result of a mixture of home and foreign politics.

These trends become clear when analyzing the main objectives of Russian political moves in East Asia, while also showing Moscow’s recognition that the Russian geostrategic power is under threat. This feeling of vulnerability, with concrete justification in the wider involvement of other actors in the area, explains the Russian ambivalent approach: on the one hand, collaboration, as a way of preserving international security, building on the multipolarity concept; on the other hand, competition, whenever Moscow feels its interests are under threat, using political and economic leverage and resorting to concrete pressure as a way to invert unfavorable tendencies. The underlying discourse of promot-

ing a multilateral posture in international relations, subscribed by partners to the east, particularly within the SCO framework, in a more explicit or implicit manner, seems nevertheless to hold discrepancies. It is a continuous bargaining between extending cooperative approaches and avoiding competitive losses that might put into jeopardy Moscow's search for primacy. Thus, Moscow follows a clearly realist option pursuing a policy of cooperation in east Asia, always based on interest, compromise, opportunities and benefits. This has been pursued either through the SCO as a regional organization, the building of "alliances of convenience" (Bendersky, 2005), or the development of "bilateral partnership nodes" with countries in the area (Luzyanin, 2007). Nothing new, just power politics in motion.

The insecurity of the international system, with all the challenges implied, along with competitive dynamics, have fostered a perception of vulnerability in Russia, in a logic of competition not always easy to deal with. This perception has allowed also a strengthening of politics and course of action, a defensive-reactive posture, sustained by the logic of affirmation and regaining of international influence – Russia is a regional and global player that must be heard and taken into account. A strategy that has been paying off, but that has been built over fragile foundations, rendering it the contours of a strong policy, but containing ingredients of unsubstantiated practice that might render it inconsistent – a strategy of clay instead of steel, drawing from a context favorable both at home and abroad, but not necessarily gathering the fundamental ingredients for sustainable development.

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Japan's New Foreign and Security Policy: Implications for China-Japan Relations and East Asia Regionalism

Miguel Santos Neves

Introduction

East Asia is one of the powerhouses of the world economy but at the same time, it is one of the most critical areas for global security given the considerable level of tension and friction between major regional powers, frequently associated with territorial disputes that are increasingly linked with the problems of energy insecurity, the acceleration of the arms race and the existence of important “hot spots” such as the Taiwan Straits, the Korean Peninsula or the South China Sea. The deficit of regional multilateralism and the inexistence of institutions of collective security further aggravate the risks of serious inter-state conflict. So far, not only has the US as the dominant power in the region prevented the escalation of tensions but also opposed any idea of East Asia regionalism thus addressing the symptoms but not the causes of the problem.

As a consequence, the two major East Asia powers, China and Japan, have developed stronger ties with the US than with each other and as such, aspects related to regional security have been addressed with the US rather

than on a bilateral basis. Consequently, in many respects the China-Japan axis tends to be a dormant relation well below its potential, with the exception of the recent boom in bilateral economic relations. Notwithstanding, this constitutes the fundamental bilateral relation in the region and a critical conditioning factor of the future evolution of East Asia. Tension and distrust between the two powers have given rise to fierce competition for regional influence and unwillingness to think together about the regional order and governance, and how to address regional problems and challenges in an increasingly complex globalization process.

Interesting enough, this picture seems to be changing dramatically. In the context of Japan's foreign policy innovations introduced by Prime Minister Abe in 2006, the new policy of rapprochement and improved relations with China emerges as a fundamental change and a major break from the previous strategy. The prospect of warmer political relations between Tokyo and Beijing facilitating the further development of existing strong economic ties, has far reaching implications not only for China-Japan bilateral relations but also for regional order and the viability of a more dense regionalism.

The purpose of this paper is to discuss the new trends in China-Japan relations and the progress achieved in order to understand their potential impact and whether this evolution is a short lasting process determined by tactical reasons or implies a long lasting structural change in East Asia. The paper is structured in three parts. The first section looks at the new developments in Japan foreign and security policies by highlighting the main priority of its relations with China and attempts to explain the motivations on both sides for engaging in a new and more positive phase in bilateral relations. The second section analyses the implications of the new scenario of warmer relations for the development of bilateral China-Japan relations in the economic, security and political spheres. The third section addresses the implications for the regional order of closer and more cooperative Sino-Japanese relations, taking into account the dominance of the US factor and the centrality of the US-Japan-China triangle.

Sino-Japanese Bilateral Relations in Perspective

Japan-China bilateral relations have been characterised by a fundamental paradox of "chilly politics and hot economics" in particular during the last phase of the Koizumi era. In fact, at the same time that there was a clear trend of

strengthening of economic ties and deepening economic interdependence, there was also growing political tension and security distrust.

“Hot Economics” reflects the strengthening of economic ties and deepening economic interdependence both in terms of trade and investment flows. Total bilateral trade increased from US\$ 189 billion in 2005 to US\$ 211 billion in 2006 (not including Japan-HKSAR trade that reached US\$ 38 billion). In 2007 total bilateral flows increased again reaching US\$ 236 billion, and a total trade surplus favourable to China of US\$ 19 billion, surpassing Japan’s trade flows with the USA of US\$ 214 billion (a total surplus favourable to Japan of US\$ 73 billion)¹. So, in 2007 China became Japan’s first trading partner and the first source of Japanese imports, accounting for 21% of total imports and 15% of total exports, while the US remained the main market for exports, absorbing 20% of total Japanese exports. From China’s point of view Japan is its third trading partner behind the EU and the USA.

As far as investment flows are concerned Japan’s FDI accumulated stock in China in 2005 was US\$40 billion complemented by an additional US\$ 6,6 billion in the HK SAR. Since 2003 China has been by far the main destination of Japanese outward FDI accounting for 35% of total Japanese FDI in 2004, 36% in 2005 and 34% in 2006². Japan became the third largest investor in China after HK, the British Virgin Islands and at times South Korea. It should be stressed that Japanese investment, unlike American investment, is more directed towards exports (2/3) rather than China’s domestic market. It is also more concentrated in the industrial sector (electrical industry; machinery industry; textile) than in services.

The process of rising trade and investment flows is a result of the interplay between different factors. Firstly, there is the complementarity between the two economies, the capital and technology of Japan and China’s labour-intensive industries. Secondly, China’s accession to the WTO in 2001 which raised the interest of Japanese investors not only in the industrial sector but also in services, in particular the financial sector, taking into account the liberalization commitments assumed by Beijing. Thirdly, Japan’s economic stagnation and the “lost decade” of the 1990s led Japanese entrepreneurs to see China more as an opportunity than as a threat. Building stronger ties with a booming economy

1 JETRO (Japan External Trade Organization), *Japanese Trade and Investment Statistics*, 2007 (www.jetro.go.jp/en/stats/statistics/gaiko200712e.xls).

2 JETRO (Japan External Trade Organization), *Japanese Trade and Investment Statistics*, 2007 (www.jetro.go.jp/en/stats)

allowed the Japanese economy to restore growth while at the same time, economic interdependence was perceived as an antidote to conflict.

The “chilly politics” dimension has been initially structurally fuelled by the strengthening of the US-Japan security alliance and the adoption of the 1997 Guidelines for US-Japan Defence Cooperation that replaced the 1978 Guidelines. Beijing perceived the inclusion of the new dimension of “*cooperation in situations in areas surrounding Japan*” as an expansion of the scope of the alliance, with clear implications for Taiwan and therefore as being directed against China and aimed at containing it. Furthermore, as China consolidated its position as Asia’s economic powerhouse and emerged as a main player in the global economy, a fierce competition between Beijing and Tokyo for economic leadership and political influence in Asia developed.

In addition, tension has been further increased by a series of contentious issues between China and Japan. The first group of issues related to the historical legacy and perceptions on WWII crimes which has recently been translated into the controversies over Japanese history books, Koizumi’s visits to the Yasukuni Shrine and the issue of abandoned chemical weapons in China by Japan’s Imperial Army³. The second set includes territorial disputes between the two countries involving the Senkaku islands and the East China Sea, strongly linked to increasing competition to control energy sources, namely the natural gas reserves in the East China Sea, in a context of growing energy insecurity. Thirdly, the divergence over the UN Reform and China’s effective opposition to Japan’s accession to a permanent seat in the Security Council. Finally, as far as security is concerned, there are bilateral concerns and new tensions associated with Japan’s New Defence Policy and what Tokyo calls China’s lack of transparency in military spending and modernization, especially following the January 2007 ASAT test (anti-satellite) which constitutes an important component of China’s space programme.

3 The existence of abandoned chemical weapons is a fact confirmed and recognised by Japan. The majority of weapons have been buried and spread over a vast area stretching from Heilongjiang province in the North to Guangdong province in the South. Japan assumes the responsibility for the financial costs and provision of technical expertise to destroy the weapons. See Japan Diplomatic Bluebook, 2006, pg. 42.

Japan New Foreign and Security Policy

The Abe Government introduced important changes and innovations in Japan’s foreign policy. A new pillar was introduced, the “Arc of Freedom and Prosperity”, whose guidelines were presented by foreign minister Taro Aso in November 2006⁴ aimed at promoting a new philosophy of a “value-oriented diplomacy”. This constitutes a new fourth pillar which has complemented, not replaced, the three traditional pillars of Japanese foreign policy: the US-Japan alliance; relations with neighbouring countries in particular China, South Korea and Russia; development cooperation and aid.

This new priority implies that Japan should act proactively to promote universal values, in particular democracy, freedom, human rights, rule of law and market economy in its external action with a view to build the “Arc of Freedom and Prosperity” in the Eurasia region⁵. In this effort Japan is supposed to coordinate efforts to consolidate democratic and market economy transitions with strategic partners that share the same values: the US and Australia in the Eastern part of the arc; India in the central part; and the EU and NATO members in the Western part of the arc. This constitutes a major breakaway with the traditional orientation that has dominated Japanese foreign policy since the 70s, the Fukuda doctrine, based on a clear separation between economics and politics (*seikei bunri*) and the assumption by Japan of a neutral, pragmatic and non-ideological status able to mediate between communist and non-communist regimes in Asia which explains both Tokyo’s close relations with the then dictatorships of Southeast Asia and closer relations with China since 1978.

Despite the fact that the US-Japan alliance remains the anchor of Japanese foreign policy and that Tokyo is committed to reinforce it, namely by means of the new joint defence project based on the BMD (ballistic missile defence) in order to ensure the continuity of US engagement in the region, the new pillar is aimed at three fundamental objectives. Firstly, to strengthen the

4 See the speech “Arc of Freedom and Prosperity: Japan’s Expanding Diplomatic Horizons” by foreign minister Aso in the seminar of the Japan Institute of International Affairs on 30 November. Certain aspects were further elaborated in the speech “ On the Arc of Freedom and Prosperity” made on 12 March 2007 on the occasion of the 20th anniversary of Japan Forum on International Relations.

5 The Arc involves a group of Eurasia countries which begins with the Nordic countries, the three Baltic states and the countries of Central and Eastern Europe, in particular the Visegrad group (Czech Republic, Hungary, Poland, and Slovakia) and GUAM (Georgia, Ukraine, Azerbaijan , Moldova); then going down to Turkey and Central Asia (Kazakhstan, Uzbekistan, Tajikistan, Turkmenistan, Kyrgyzstan), through the Middle East and South Asia, in particular India, Southeast Asia CVL (Cambodia, Vietnam, Laos) and finishing in East Asia, Korea and Mongolia.

US-Japan alliance to ensure greater coherence between the foreign policies of both partners thus reducing the risks of tensions that emerged at times under the Fukuda doctrine. Secondly, to achieve a certain degree of differentiation in relation to China in the context of an increasing competition for regional leadership between the two Asian powers as a way to counteract the increasing prestige and influence of Beijing in the region. Thirdly, to pursue a strategy of diversification of Japan's external relations, building closer ties with the EU and NATO in order to gain some autonomy and "room for manoeuvre" in relation to Washington at the same time that it signals a political will to play a more proactive role in international security.

The second major innovation introduced by Prime Minister Abe was precisely the new bilateral policy towards China aimed at reducing the level of political tension that reached an unprecedented level during the last phase of the Koizumi era. Abe chose a line of appeasement and pacification of relations with China thus departing from the previous policy fearing that the "chilly politics and hot economics" could evolve to "chilly politics and cool economics". This was translated into a new attitude and concrete signs of change as Abe decided to suspend the visits to the Yasukuni Shrine and to promote high level visits. Symbolically, Abe's first official visit abroad was to Beijing in October 2006 signalling the high priority attached to bilateral relations and the willingness to normalise ties between the two countries. This visit contributed to breaking the ice and had an unexpected positive impact on Beijing, thus paving the way to China's initiative to reciprocate with Chinese Premier Wen Jiabao's visit to Tokyo in April 2007⁶. The fall of the Abe Government did not imply any change of direction as the new Japanese Government led by Prime Minister Fukuda has continued and even strengthened the policy of warm relations with Beijing. In late December 2007 Fukuda paid a 5-day official visit to China, clearly showing his full political commitment and closing the commemorations of the 35th anniversary of the normalization of China-Japan diplomatic relations very formally. In the period of a year, there were a total of three high level state visits constituting an unprecedented fact in the history of bilateral relations.

There are several motivations behind Japan's new policy towards China. Firstly, a short-term economic aim, related to the preservation and consolidation of Japan's economic recovery, increasingly dependent on the China engine. This implies the smooth expansion of trade and investment flows and the ability of

6 On the details of Wen visit see James Przystup, "Japan-China relations: Wen in Japan: Ice Melting but..." in *Comparative Connections*, July 2007.

Japan to benefit more from China’s economic boom. Secondly, the objective of further developing the normalization process of Japan’s international status which has been effectively blocked by China, in particular by denying Japan the possibility of a permanent seat in the UN Security Council, hoping that the normalization of relations with China can help soften the hardline position adopted by Beijing at the international level. Thirdly, there is also an attempt to dilute Beijing’s increasing influence in the region by getting closer to China and attempting to set jointly some basic rules to ensure regional stability. Finally, Tokyo suddenly realised the improvements in the US-China relationship and that Japan was lagging behind as the US was one step ahead in terms of cooperation with China.

The new policy reflects an important change in Japan’s strategy. Facts have shown that the re-emergence of Japan and the accession to a “normal status” can not be achieved against China in a context of open conflict and fierce competition, but only with China in a new setting of rationalised competition and cooperation. Moreover, a weak Japan, both economically and politically, will not be able to counterbalance China’s increasing regional predominance in the long term. Only a more influential Japan will be able to restrain and above all to actively contribute for the development of a regional multilateral framework where China can be integrated and behave responsibly in building a more stable regional order.

On the Chinese side there is also a change in the approach on relations with Japan. Beijing has concluded that open friction with Japan has further strengthened the US-Japan alliance, an outcome Beijing does not wish insofar China perceives the alliance as a fundamental mechanism to contain her⁷. In this respect, the confrontation strategy proved to be counterproductive and not efficient in terms of weakening US influence in the region. On the contrary, improved relations with Japan and furthering bilateral interdependence is likely to be conducive to the opposite effect of undermining and weakening the US-Japan alliance. This is consistent with China’s new strategy in the strategic competition with Washington which is not to confront the US power directly but rather indirectly by projecting China’s soft power⁸ and filling the gaps left

7 The 2006 China Defense White Paper clearly expresses Beijing concerns over the strengthening of US-Japan alliance, Japan’s constitutional revision to amend article 9 and the deployment of Japanese Forces abroad (see www.fas.org/nuke/guide/China/doctrine/wp.2006)

8 Soft power as defined by Nye “the ability to get what you want through attraction rather than coercion” see Joseph Nye, *Soft Power: the means to succeed in World Politics*, New York, 2004. Nye has applied the concept in the Asia context stressing Japan’s high potential soft-power resources see “*Soft Power matters*

open by the US diminishing soft power, undermining Washington's economic and diplomatic influence in East Asia⁹.

The second key motivation of China is to reinforce Japan's contribution to its own domestic development, especially now that China is confronted with the limits of its unsustainable and "non-harmonious" development model and has to face the challenge of the transition to the Knowledge Economy and to a more intensive, efficient and environmentally sustainable path of growth¹⁰. Japan is an important source of technology, managerial skills and capital and is therefore seen as an important alternative, as well as an asset to strengthening the bargaining position vis-à-vis the US and the EU, following Beijing's strategy to stimulate competition between key external players, playing one against the other in order to maximise benefits and prevent excessive dependence on a single player. This objective is clearly reflected in the list of priority areas for the new bilateral cooperation proposed by Wen Jiabao during his visit to Tokyo in April 2007 which includes five main issues: energy; environment; SMEs cooperation; financial sector; and joint investments. All of them, in particular energy, the environment and the financial sector are weak and vulnerable areas in China's development process in which Japanese expertise would be much welcomed. During the Fukuda visit to Beijing last December, one of the issues addressed was precisely Japanese assistance in solving some of China's environmental problems, namely how to cope with sandstorms in Northern China and to improve the quality of water in the Yangtze River.

As far as Japan's new foreign policy is concerned, there is a clear contradiction between the "Arc of Freedom and Prosperity" dimension and the new approach to China considering that the new value-oriented diplomacy sends a negative signal to Beijing which is excluded from the list of priority partners, with an obvious implication: the isolation of China. This contradicts the new commitment to warm relations with Beijing. Indeed there seems to

in Asia" The Japan Times 5.12.2005 and China's increasing use of soft power, see "*The rise of China's soft power*" The Wall Street Journal 29.12.2005.

9 See Joshua Kurlantzick, *Charm Offensive: How China Soft Power is Transforming the World*, Yale University Press, 2007 where he stresses that China invests in soft-power strategies using different tools (investment, aid, culture, diplomacy) because it considers that the US weakness is its soft power not its hard power.

10 Since 2004 the PRC Government has been committed to rebalancing the economy and implementing the strategy of the "harmonious society" which implies a shift from a industry-led growth to a services-led growth, greater concern with social justice and environmental sustainability. So far the targets set have not been met. For example China's economy is characterised by a high level of energy inefficiency and the objective to reduce energy consumption per unit of GDP by 4% by 2006 was not met as the reduction achieved was only 1,2%. Similarly the share of services in GDP has declined, not increased (from 41,7% in 2002 to 39,5% in 2006) while that of industry has increased putting further pressure on energy and the environment (Asian Development Outlook 2007, ADB pp. 132-139).

be a rationalised dualism and ambiguity in Japan's attitude towards China as a result of the perception of China as both a threat and an opportunity. A possible interpretation is that Japan adopted a more sophisticated and subtle strategy moving away from direct confrontation with China aimed at containing its dominance, highly exhausting and costly for Japan and instead tried indirectly to reach a similar objective by mobilizing other players to collectively perform the task of strategic containment of China.

Japan's new security policy

Japan is attempting to redefine its security policy and to play a new and more relevant role in the defence and security realm as a consequence of the interaction between three key factors. Firstly, the US pressure on Japan to take new strategic responsibilities both inside the US-Japan alliance and in Asia security framework. Secondly, the political objective to strengthen its international status, namely the political and security profile which requires a more active role in global security and participation in operations of collective security. Thirdly, the changes in regional security situation which accentuated Japan's own perception of vulnerability and created political pressure to strengthen its defence capabilities as a consequence of two key factors: the North Korea threat, following the re-emergence of the nuclear programme in 2002 and the various missile tests carried out by Pyongyang culminating in the nuclear test of October 2006; and the process of China's military modernization and increasing military expenditure.

The implementation of the new defence policy involving important recent steps has developed rapidly. The creation of the new Ministry of Defence in January 2007 signalling the upgrade of the political status of the Self-Defence Agency; the approval of various new laws namely those concerned with the definition of the priority external missions of the Self Defence Forces and their participation in international cooperation for peace; the relocation of the US forces stationed in Japan; the strengthening of the level of compromise in the US-Japan alliance focused on the new projects of joint defence and the BMD system; the upgrade of the level of dialogue and cooperation with NATO; the new priority of defence cooperation with Australia translated in the Joint Declaration of March 2007.

The Japanese Constitution is the major obstacle to the implementation of the new policy. That is the reason why constitutional revision is presented as a

key issue, in particular the amendment of article 9 which enshrines the “pacifist clause”. According to the interpretation consolidated since 1954¹¹, the clause allows for Japan’s right of self-defence and the possibility of having self-defence forces but prohibits the existence of normal and full armed forces, the possession and use of offensive weapons as well as the participation of Japanese forces in any external mission which is not directly related with the defence of Japan or in collective security operations. The constitutional framework not only sharply contrasts with the current military capacity of Japan, which possesses the most sophisticated navy in Asia and has a high level of military expenditure, the fifth largest in the world¹² but prevents Japan from assuming greater responsibilities in international security and participating in operations of collective security.

In this context, the Abe Government launched two simultaneous processes: (i) the revision of the Constitution by promoting the approval of the new law of the referendum in May 2007 to enter into force in 2010 paving the way for a referendum which constitutes the last phase of the revision process; (ii) the creation of a panel of experts to carry out the re-interpretation of article 9 as it stands, making it more flexible and adapted to current reality, seen not only as a solution to speed up the implementation of the new policy but also as an alternative in case the constitutional revision strategy fails.

The short term objective is to remove obstacles to the implementation of the joint BMD system with the US according to which Japan will assume obligations to defend the US namely through the interception of intercontinental missiles targeted at US facilities in Asia. In the mean time, the key motivation is to create conditions that will strengthen Japan’s participation in collective security operations which implies removing the current restrictions imposed by article 9 that prevents the SDF from defending themselves when attacked, thus requiring the direct protection of allied forces, and from giving support, even logistic, to allied forces except in zones outside the theatre of operations. The best example of the system’s incoherence was the situation of

11 The interpretation of article 9 of the Cabinet Legislation Bureau (CLB) allowed for the creation of the Self Defense Forces without any amendment of the Constitution and paved the way for the approval of the SDF Establishment Law. The argument was that Japan as a sovereign state had the right to self-defence under certain conditions which were specified: it could only respond with “minimum necessary force”; could not participate in any collective security arrangements; can not send forces abroad. On Constitutional revision see Richard Samuels, 2004, *Constitutional Revision in Japan: the future of article 9*, the Brookings Institution Paper.

12 According to the Stockholm International Peace Research Institute (SIPRI) Yearbook 2007, in 2006 Japan’s total military expenses reached US\$ 43.7 billion, the 5th largest military expenditure in the world accounting for 4% of global military expenditure. In 2006 China maintained the trend of rising military expenditure reaching a total value of US\$ 49.5 billion and for the first time surpassed Japan ranking 4 in the list of major spenders, after the US, UK and France.

SDF ships in the Indian Ocean and the failure to approve the extension of the Anti-Terrorism Special Measures Law in September 2007¹³ which would allow Japanese ships to keep on refuelling NATO coalition forces vessels involved in the anti-terrorist operation in Afghanistan. This implied the discontinuation of the refuelling operations, affecting the credibility of Japan as a reliable partner. The operations were resumed only a few weeks after the recent approval of the new Replenishment Support Special Measures Law in the Diet, which was one of Fukuda’s successes.

The new Fukuda Government has already clarified its priorities in terms of the foreign and security policies in the recent Prime Minister Policy address to the Diet in January 2008¹⁴. There is both continuity and change in comparison to Abe’s priorities. As to continuity, the US-Japan alliance is considered the cornerstone of Japan’s foreign and security policies and the new policy of rapprochement with China is to be continued and further developed. Moreover, there is an important emphasis on strengthening Japan’s participation in peacekeeping operations and collective security which was identified as a top objective to be pursued on the basis of a more stable and clear legal framework. In this context, Fukuda announced the proposal to enact a permanent law for the dispatch of the SDF overseas when necessary to take part in international peacekeeping operations, thus overcoming some of the current limitations and the objective of turning Japan into a centre for research and international cooperation for peace-building. In this context, the objective of becoming a permanent member of the UN Security Council was identified as an important priority and a fundamental condition for Japan to fulfil its role as a “Peace Fostering Nation”. The process of constitutional revision was also mentioned although it is unlikely to be one of the top priorities.

Two important innovations should be noted insofar as changes are concerned. The first is the introduction of a new “environmental diplomacy” to be the priority axis of Japan’s external action. Building on its environmental technology capacity, Japan intends to lead the process of creation of a low-carbon society at the international level and face global environmental challenges. In this respect Fukuda seems to follow a similar orientation to the strategy adopted by the European Union. Secondly, there is no reference to the “Arc of Freedom

13 The Anti-Terrorism Special Measures Law was enacted in 2001 with the aim to allow the Government to dispatch Maritimes Self-Defense Forces ships to the Indian Ocean for refuelling operation to support coalition efforts to fight terrorism in Afghanistan and was subsequently extended in 2003, 2005, and 2006.

14 Policy Speech by Prime Minister Yasuo Fukuda to the 169th Session of the Diet, 18.1.2008 (www.kantei.go.jp/foreign/hukudaspeech)

and Prosperity” nor to a value-oriented diplomacy which signals that this is no longer a priority for Japan foreign policy, thus dropping the innovation introduced by Abe and returning to traditional pragmatism. This clearly has an important implication for relations with China insofar as it reduces the explicit contradiction between the new policy towards China and the value-oriented diplomacy mentioned above, therefore reducing the level of ambiguity of Japan’s foreign policy and removing a source of potential bilateral tension.

Implications for bilateral relations

This new climate in bilateral relations has already led to concrete progress in specific areas regarding some of the most contentious issues, at least in terms of the creation of institutional channels to assess the problems and put forward solutions. This was the case of the creation of the Joint History Study Group in December 2006 formed by Chinese and Japanese scholars aimed at bridging differences over the interpretation of history, in particular the issues related to Japan wartime aggression and to attain eventually a joint recognition of history. The group which has had three meetings so far, the last one held in early January 2008, has been addressing sensitive issues like the Nanjing massacre and the Yasukuni Shrine¹⁵ and reached an agreement to publish separately authored articles in June 2008. Similar progress was registered regarding the issue of abandoned chemical weapons as the two sides established the “Japan-China Joint Organization on Destruction of Japanese Abandoned Chemical Weapons in China” in order to accelerate the destruction process.

The East China Sea constitutes another area in which there have been signs of progress. There is a renewed political commitment to speed up the process of a plan for the joint development of the East China Sea as a way out of the controversy over the disputed area where the two exclusive economic zones of the two countries overlap. The principle of the joint development was reaffirmed during the Abe-Wen meeting at the ASEAN+3 summit in Cebu and again during Wen Jiabao’s visit to Tokyo where the idea to speed up the joint development of oil and gas fields was agreed upon. As a result, the process of consultations in 2007 was intensified in contrast with the slow progress since the process started in 2004, but a final agreement has yet to be reached.

15 China Daily 7.1.2008.

The third and particularly significant area of progress is that of security where direct dialogue has evolved positively in spite of the new sources of tension such as China’s ASAT test in January 2007, the increase in China’s military spending and Japan’s advances in installing the BMD missile system. Progress was particularly visible in terms of confidence building measures. There was an intensification of consultations, namely the Japan-China consultation on disarmament and non-proliferation issues in May 2007, and of bilateral military and defence exchanges. Japan has even decided to create a hotline to connect Japanese and Chinese military defence officials. This new climate culminated in two symbolic and significant events that constitute crucial confidence building measures. Firstly, the historic visit of the Chinese Defence Minister Cao Gangchuan to Japan in September 2007, the first visit in nine years of a defence minister, to strengthen defence cooperation and discuss issues not only related to bilateral relations but also to Asia regional security. Secondly, the port call of the Chinese destroyer “Shenzhen” in November 2007 in Tokyo, the first call by a Chinese navy ship to Japan since 1949.

The progress in confidence building might also lead to more long term structural changes in bilateral relations with important consequences for the region. One potential area is that of economic relations, in particular the development of trade and investment flows and advances of an eventual project to create a China-Japan Free Trade Area. This is not a completely new idea as China had already put forward an informal proposal for the creation of a trilateral FTA between China, Japan and South Korea in 2002 but without success. Indeed, one of the trends in the region has been the intensification and densification of East Asia intra-regional trade flows which increased from 45% of total trade in 1990 to 57% in 2002 and 55% in 2006¹⁶. The densification is associated with the growing interlinkages between the different economies in the region and the rapid proliferation of Free Trade Areas (FTAs) or Economic Partnership Agreements (EPA).

Despite being a late comer, there is currently a considerable number of regional agreements signed or under negotiation in Asia. Until 2000 the only existing FTA was the ASEAN – AFTA, but since 2001 there has been a rapid and unprecedented proliferation of agreements starting with the Singapore-New Zealand and Japan-Singapore FTAs and including the largest world FTA between China and ASEAN. This trend resulted in a total of 25 FTA/EPA agreements signed or implemented until 2007 (12 among Asian countries

16 Asian Development Bank, *Asian Development Outlook 2006* (table 3.1) and Kawai, M., Asian Development Bank Institute, *Overview of FDI: US, Europe, Japan and Emerging Asia* (November 2007)

and 13 between Asian countries and countries outside the region), under the leadership of Singapore which is involved in 10 FTAs out of the total. These agreements follow the APEC model combining 3 pillars: trade liberalization; trade and investment facilitation; technical and economic cooperation. This rapid proliferation can be seen as the result of the interplay between various factors: a response to the rapid expansion of FTAs in other parts of the world; slow progress in WTO Doha negotiations; a strategy to promote domestic deregulation and economic reforms putting external pressure on domestic policymakers; and the growing rivalry between China and Japan which use the FTA as an instrument to strengthen privileged ties with specific countries and assert regional influence¹⁷.

In recent years China has pursued an active FTA strategy aiming at projecting its soft power and Japan has abandoned its antagonism towards RTAs and also embarked into various bilateral FTAs with countries in the region, especially ASEAN members. In contrast, the creation of an FTA in East Asia involving ASEAN+3, recommended by the East Asia Vision Group, has not been seriously considered nor has progress been registered which is partly due to China-Japan rivalry. The new climate in Sino-Japanese relations might just offer an opportunity to think about a regional project again. Moreover, there is also greater awareness about the costs and risks associated with this trend of proliferation of uncoordinated bilateral FTAs which puts a great deal of pressure on countries and might just prove impossible to manage in the face of cross commitments and inconsistencies, the “spaghetti bowl” syndrome. In this context, a more coordinated regional project could not only control risks but also contribute to strengthening the overall position of East Asia in the global economy. However, any project of a China-Japan FTA or an East Asia FTA will be time-consuming, involving complex and lengthy negotiations and probably require not only the normalization of relations between the two Asian powers but eventually a true reconciliation and share of common objectives, even though this is a distant prospect.

In the financial and monetary area there are also good prospects for the intensification of bilateral cooperation which is instrumental to further advance the ongoing development of financial regionalism already translated into visible achievements. Firstly, the deepening of the Chiang Mai Initiative (CMI), a network of bilateral swap arrangements among ASEAN+3 countries with two main objectives: to address short-term liquidity difficulties through emergency

17 On trade agreements in Asia see Shujiro Urata, *Proliferation of FTAs in East Asia*, paper presented at PECC Trade Forum, 2005

funds (a total of US\$ 83 billion) to support member countries that experience short-term balance of payments deficits to prevent an extreme crisis; to supplement the existing international financial arrangements. In May 2007 the Kyoto meeting of finance ministers approved the principle of multilateralisation of the CMI through a self-managed reserve pooling arrangement governed by a single contractual arrangement, a gradual process which will transform the bilateral mechanism into a multilateral one and thus constitute an important step towards the creation of an Asian Monetary Fund.

Secondly, the Asian Bond Market Initiative (ABMI) launched in 2003 in the context of the ASEAN+3, aimed at developing efficient and liquid bond markets in Asia with a critical strategic objective: to tap the considerable pool of savings in Asia and to retain them in the region to finance investments in Asia, therefore reducing the cost of capital to Asian firms, especially SMEs and reversing the current trend of a large proportion of Asian savings being channelled to the US and the EU. The development of these markets, for which Japan has provided important leadership, would have far reaching consequences for the US economy insofar China and Japan, the two largest foreign holders of US Treasury Bonds, will shift from US bonds to Asian bonds and therefore will be less willing to finance the US Government debt.

Thirdly, the project of the Asian Currency Unit (ACU) a proposed currency basket, a weighted index of currencies inspired in the old European Currency Unit, involving the most important East Asia currencies. The main objectives are to reduce the exchange rate volatility among member countries, to support the creation of the regional bond market and to strengthen the defence against speculative attacks from outside the region.

All these initiatives seem to be driven by two strategic objectives. On the one hand, there is the objective of strengthening the financial weight of the region and preparing it to cope with an eventual financial crisis. On the other, the creation of regional alternative solutions and institutions as a response to East Asia’s perceived lack of influence in global financial institutions, despite its considerable financial power, a manifestation of what has been called East Asia counterweight strategy¹⁸. The progress of these initiatives critically depends on an active and effective cooperation between China and Japan.

18 Injoo Sohn *East Asia Counterweight Strategy: Asian Financial Cooperation and Evolving International Monetary Order*, (mimeo), 2006 and Saori Katada “Japan’s Counterweight strategy: US-Japan Cooperation and Competition in International Finance” in Ellis S. Krauss and T.J. Pempel (eds.) *Beyond Bilateralism – US-Japan Relations in the New Asia-Pacific*, Stanford University Press, 2004

There are also important implications in the security area. Warmer relations can have a positive impact in terms of greater bilateral cooperation in non-traditional, non-military issues further reinforcing the new regional security dynamics which put new emphasis on these matters (terrorism, transnational organized crime, trafficking of drugs and human beings, maritime piracy or environmental degradation). A more intensive and dense Japan-China regional functional cooperation on non-traditional security areas such as energy, terrorism, maritime piracy or the environment will set a good example and have a relevant demonstration effect on other regional players. Cooperation in energy security and the capacity to achieve a balanced agreement on the exploration of East China Sea resources will be a critical test case. However, in contrast with the non-traditional security sphere, it is unlikely to see a major progress in hard security cooperation or a halt in the trend of rising military expenditures on both sides in the medium term.

All these developments have an important implication for the future evolution of Sino-Japanese bilateral relations: the increase in their level of complexity. The normalization of China-Japan relations will be associated with the emergence of a complex three-tier structure of (i) structural friction (in strategic matters) (ii) rationalised competition (in the economic sphere and for regional leadership) (iii) functional cooperation (in financial and economic matters, energy and the environment) where the different levels interact and the final outcome might vary overtime. Relations are bound to become more mature but at the same time marked by greater contradictions insofar as competition and cooperation coexist.

Implications for regional order

The implications for regional order and Asia's balance of power are also important. Traditionally, the role of the US in Asia's security architecture has been and still is dominant, operating in the context of the US-China-Japan triangle, certainly one of the most complex trilateral relations in the world where the US plays a pivotal role. The US factor has been a determinant variable in China-Japan relations. As pointed out by Yahuda ¹⁹, in security matters China and Japan feel "more comfortable in discussing these issues with Washington" rather than talking directly to each other. In this context, the US

19 Michael Yahuda, *Chinese Dilemmas in Thinking about regional security architecture*, in *The Pacific Review*, vol 16, n°2 June 2003, (pp.189-206), p.195

role in East Asia has been seen as the “cork in the bottle” performing crossed containment - from China’s perspective preventing Japanese re-militarization and from Tokyo’s point of view containing China’s rise - thus preventing the escalation of tension but at the same time failing to address the root causes of distrust and rivalry or to facilitate closer relations and cooperation between the two Asian powers.

This seems likely to change as the new atmosphere opens the door to direct dialogue and there are already positive signs of a political will to address and resolve contentious issues. This will require an adaptation of the US role and a redefinition of the operating dynamics of the US-China-Japan trilateral relation as the China-Japan axis becomes stronger. In the security sphere, one possible scenario is a dual regional dynamics involving a distinction between traditional hard security matters, where the US retains a dominant position and China-Japan relations remain controversial, and non-traditional security matters, where China and Japan play a more active role and regional cooperation arrangements develop rapidly.

Secondly, there is the decline of the US soft power in the region. Stronger Japan-China economic relations, the possible emergence of a regional East Asia FTA and improved financial cooperation as a result of closer Japan-China cooperation will not only challenge US dominance in global markets but will also contribute to the further erosion of the US soft power in the region. The projection of China’s “soft power” based on economic and diplomatic extended influence has recently been the main strategy followed by Beijing of reducing Washington’s influence and to prevent the risk of Asian countries joining with the US to collectively contain China. This constitutes a more subtle approach that contrasts with the traditional confrontational approach to challenge directly the US strategic dominance which prevailed in the 1990s. The new relationship with Tokyo can serve Beijing’s purposes to further deepen this strategy. In the long term, a scenario of gradual erosion of US economic and financial power in East Asia is likely to undermine ultimately the US dominance in the security sphere.

Thirdly, this might create some prospects for a potential qualitative progress in East Asia regionalism. There is already a trend of a rising regionalism in East Asia, still unstructured taking new and unprecedented forms combining bilateralism, limited forms of multilateralism and functional cooperation. There has been an emergence of ad hoc mechanisms of cooperation on anti-terrorism, energy, health risks, anti-piracy, transnational organized crime and the development of limited forms of regional multilateralism in specific areas

and consolidation of mechanisms of cooperative security with a multi-layered structure at both the regional (ARF, Shangri-la Dialogue) and sub-regional levels (Six-Party talks, Shanghai Cooperation Organization, joint military exercises).

This trend has been the consequence of the interaction between two fundamental factors: the 1997-98 Asian financial crisis and China's rise. The financial crisis confronted the Asian countries with their vulnerability and the need for enhanced cooperation in order to control risks and threats, paving the way to a more open attitude towards regionalism. The rise of China, led many countries in the region to be concerned with the potential risks of Chinese hegemony and to favour the development of regional multilateral arrangements as a means to engage China and promote its multilateralization.

In the past, rivalry between China and Japan, the US opposition to regional multilateralism and the predominance of concepts of absolute sovereignty were the main impediments to progress towards deeper levels of integration in the region. Warmer relations between Beijing and Tokyo create positive conditions for advancements in regional cooperation and even to see marginal progress in the East Asia Community project. It is more uncertain whether this will lead to a qualitative progress in the direction of deeper regionalism based on multilateral institutions. This seems to be possible only in a scenario of a Sino-Japanese co-leadership which in turn presupposes a structural political reconciliation between the two, an interesting parallel with the EU process where reconciliation between France and Germany and their co-leadership was a driving force of the European project. However, we are only witnessing the normalization of Japan-China relations not the reconciliation which is still a distant prospect. The emergence of a Japan-China co-leadership seems to depend critically on two dynamics: the evolution of bilateral cooperation and the extent to which this will lead to joint thinking about regional order; the pressure created by the need to solve concrete and complex regional problems. So, joint leadership is only a gradually emergent concept but might be seen in the near future not only as increasingly appealing but also as increasingly necessary for stability and prosperity in the region²⁰. In addition, the fact the US own strategy for East Asia is not well defined and that thinking about the future of the region remains unclear offers additional space for China and Japan to take the initiative.

20 On prospects for joint leadership see Julie Gilson, *Strategic regionalism in East Asia*, in *Review of International Studies*, 2007, n° 33, pp. 145-163

Conclusions

Within the scope of important changes in Japan foreign policy, a turning point in China-Japan relations following the October 2006 initiative of Prime Minister Abe is of noteworthy importance. The new policy towards China is one of the key innovations that the new Fukuda Government regards as a priority to be maintained and even deepened. Japan initiative is explained by different factors: the objective of consolidation of Japan’s economic recovery for which China’s growth has been a fundamental engine, preventing “chilly politics” from harming “hot economics”; the process of normalization of Japan status, in particular by assuming a more active role in regional and global security, requiring softening China’s opposition; a response to Beijing-Washington improved relations which left Tokyo behind having to pay the costs for China containment; the redesign of the balance of power in the region and Japan’s strategy to engage China in multilateral arrangements.

China’s positive response to the new initiative is partly explained by Beijing’s concern of ensuring a stable regional environment as a condition for preserving its vibrant domestic growth but also by Beijing’s objective to mobilizing Japanese assistance to tackling the major structural bottlenecks that threaten the sustainability of its “extensive” development model, and to promote a qualitative transition. But the hidden agenda also includes the objective of weakening the US-Japan alliance and eroding the US soft power in the region and Washington’s capacity to mobilize other Asian countries to collectively contain China.

There is sufficient evidence to conclude that China-Japan bilateral relations are entering a new and more positive phase in political terms, attenuating the paradox of “chilly politics, hot economics” and eventually moving towards a scenario of “warm politics, hotter economics”. As a consequence the bilateral relation is becoming more complex and ambiguous with a three-tier structure – structural tension, rationalized competition, functional cooperation – involving a new mix of competition-cooperation. However, although we are witnessing a progress towards normalization of bilateral relations, we are still far from true reconciliation insofar as there is suspicion and distrust on both sides, competition for regional leadership and important divergences about what the format of the regional order should be.

The consolidation of a scenario of increasing cooperation and “warm politics” between the two Asian powers will enhance the centrality of this bilateral relation in the regional context, now for positive rather than negative

reasons as in the past, and it is likely to have important implications for regional governance and security. Firstly, it has consequences for the equilibrium of the US-Japan-China triangle as the China-Japan side is strengthened and might gain some autonomy, thus implying a redesign of the regional balance of power. Secondly, it might lead to a further erosion of the US soft power in the region and an adaptation of the US role as the security guarantor though not challenging its dominance in the medium term. Thirdly, the new climate in bilateral relations can facilitate a new thinking about regional problems and regional order and advancements in regional multilateralism in specific areas, namely the financial area, and of cooperative security arrangements in particular in non-traditional security areas.

However, any prospect for progress towards a comprehensive and deeper regionalism capable of ensuring structural conditions for greater stability and prosperity in the region is still a distant one. This would only be possible if both China and Japan abandoned the “competition for regional leadership” approach in favour of a “Sino-Japanese co-leadership” approach. This scenario depends upon the dynamics of this new phase in bilateral relations and the extent to which it might lead to meaningful reconciliation, a pre-requisite for joint leadership, as much as upon the attitude of the US, its Asia strategy and whether Washington will be more inclined to divide and rule, creating indirectly irritants in China-Japan relations that might poison it, or on the contrary, support and encourage reconciliation as it once did in Europe.

The ASEAN Group as “Main Actor”: Constraints and Potentialities

Nuno Canas Mendes

The Association of Southeast Asian Nations (ASEAN) has undoubtedly been a “main actor” in East Asia, not only for its economic relevance but also for its institutional structure, the only one in this part of the world allowing a group of countries to act as regional actors. However, the cohesion and cooperation needed to develop a more prominent role for ASEAN in international relations are still limited by post-colonial mechanisms, which have been a constraint to face very serious problems such as 1997’s financial crisis or terrorism. The organization’s consensus and non-interference approach have been considered a paralyzing method for a group of countries forming a gigantic market full of potential despite their very heterogeneous levels of development.

In this essay, a description will be made of the main steps of the organization through its 40 years of history, since its creation in 1967 up to the present, depicting the international relations context in which the main decisions and institutional developments were taken. It will also focus on ASEAN’s constraints and potentialities, giving special attention to the most challenging issue of security, the most delicate for the organization.

1. Introduction

It would be useful to start by trying a conceptualization of ‘Southeast Asia’, having in mind how difficult is to find coherence in a regional classification felt by the ‘native’ as strange and imposed from the outside. It is indeed a colonial designation for a variety of ethnic groups, cultures, religions, political systems, afterwards used for nationalist purposes in order to give body to a desired unity of the colonized people¹. In the post-colonial *scenario*, the concept was fed by the binomial security-development, having as a common pattern the strength of the sovereignty paradigm in individual nation-building processes. This particular feature was originated in the pacific coexistence principles of non-intervention and will be very important in the future as one of the main sources of the “ASEAN way”. One cannot forget that during the Cold War period, the region was crucial for The United States in the fight against continental communism expansion. This was the environment in which the Organization of Southeast Asian Nations was created.

Founded in 1967 by Indonesia, Malaysia, Philippines, Singapore and Thailand, ASEAN has been pursuing three inter-connected goals, all of them reinforcing sovereignty: softening intra-ASEAN tensions (a kind of “non-aggression” pact); reducing foreign actors’ influence and promoting socio-economic development (Marine, 2005). Vietnam’s reunification, in 1975, gave ASEAN’s countries political leaders the willing to reinforce the organization’s anti-communist posture. The Bali Conference, in 1976, was the first where the various heads of government met and approved a Treaty of Amity and Cooperation. The document postulates the principles for member-states’ behaviour within the group, proposing pacific resolution of conflicts and the respect for sovereignty and independence. The intention was to build a platform for stability, balancing the asymmetric development and different political regimes.

The end of the Cold War and the Cambodia conflict (1991) put the stress in the need to re-evaluate ASEAN’s role, which became more oriented to a deepening of economic integration. In the 90’s, economic growth was qualified as the “Asian miracle”. This was the spirit of the ASEAN Free Trade Area project (AFTA), defined in 1992. It was also in this context that Vietnam

1 It would be hard to find affinities or common elements to support a Southeast Asian identity. The exceptions are rice culture, water as a channel of communication, Chinese communities overseas and a mobilizing antagonism caused by foreign colonization. Southeast Asia itself, as a region, was and remains a mirage. In the 90s, Asian values rhetoric tried to diffuse a cohesive image of the whole region but the 97-98s financial crisis ruined all the efforts by Singapore and Malaysia authoritarian rulers, whose purpose was rather to reinforce their power internally than to build an identity for the region.

(1995), Myanmar (1997), Laos (1997) and finally Cambodia (1999) joined the organization, introducing a high disparity in development levels.

The 1997 financial crisis was a severe test to the solidity of the building and affected the Indonesian most promising leadership. The needed cohesion was absent and the solutions were found within the States which remained the central actors in appealing to international aid, downsizing the organization and its institutional capacity for facing common challenges.

The political implications of this crisis led to the fall of Suharto, Indonesia's head of State, followed by the East Timor crisis, in which a common response to a common problem was not found. This attitude underlined the worries even within ASEAN member-states caused by a particular type of auto-limited socialization. ASEAN would be severely tested again in the aftermath of Bali's terrorist bombing in 2002 and, finally, new issues with serious health and extended security implications came out: Severe Acute Respiratory Syndrome (SARS) and the 2004's tsunami. All these facts questioned the organization's principles and capacities, showing a number of shortcomings.

One of the main features is ASEAN's traditional consensus attitude. It is very hard to build a consensus in such a complex and varied region. All the decisions are based on the logic of minimum common denominator, but even so, they are not neglectful. The security issue has also a very important place in the agenda's organization since the 90s, articulating economic regionalism with the tensions and threats which affect member-states. The respect for sovereignty and non-intervention resulted into institutional procedure flexibility, with some paralyzing effects.

The last decade, since the 1997's financial crisis, bring into discussion ASEAN's nature and future, particularly in what concerns its communitarian orientation (defined in Bali-Concord II declaration [2003])² and the dialogue with the nearby great powers (ASEAN+3, ASEAN+1). Meanwhile, the preference for bilateralism and strong auto-focused national interests are still heavy obstacles to give common answers to common problems. However, as a diplomatic tool, ASEAN is a place to manage reliable relations and to soften divergences. Further institutionalisation, through a charter of principles, could be a step forward (as was convened in Cebu Summit, in January 2007, consensus decision-making process shall be changed in order to achieve the suitable coherence within the organization).

2 <http://www.aseansec.org/15159.htm>

2. Security issues

When ASEAN was created, its main goal was to forge cooperation among the member states on non-sensitive economic areas. When security agenda became a part of ASEAN's agenda, in 1992, it was seen as a response to a changing strategic world *scenario*, not really as an effort to “foster intra-mural security cooperation” (Sukma, 2006).

In fact, during the Cold War, the United States were the security umbrella for the region, especially through bilateral agreements. Multilaterally the results were not very successful: China as well as Soviet Union matched points in French Indochina. SEATO treaty, formed during the Cold War, ended in 1977, after the American defeat in Vietnam. The only structure that lasts is Five Power Defence Arrangement, whose mission was to guarantee the security of the Malacca Strait. It was signed in 1971, between the United Kingdom, Malaysia, Singapore, Australia and New Zealand.

During its first decade, ASEAN tried to present a proposal for a “peace zone”, but its state members were divided regarding what they perceived as a foreign threat. Indonesia and Malaysia, for instance, were much more frightened by China than by Russia. Since the beginning of the Sino American *détente*, US's allies – Thailand and Philippines – started re-evaluating their vision of China. As far as economic aspects were concerned, the progress was limited. Japan's economic growth increased the prosperity of some ASEAN states (Singapore and Malaysia). Oil shocks in the 70's have favoured regional producers, namely Indonesia and Brunei.

Security and conflict prevention were not absent from the leader's worries, having in mind the regional neutralization through the creation of a zone of peace, freedom and neutrality (ZOPFAN, 1971). Some of the ASEAN states feared a few of their fellows' hegemonic tendencies and preferred the defensive cooperation with extra-regional states. Because of that, The United States presence was desired. Otherwise, ASEAN embraced a set of principles – the ‘ASEAN way’ – that, as a matter of fact, subsume a policy of conflict prevention and conflict resolution. The same method flexibility that contributed to a solution found at internal or international levels, but not regionally. This really contained some post-colonial conflicts, as well as the great Asian powers: China, India and Japan.

Post-Cold War ASEAN was then integrated into a broader security structure. That's why ASEAN Regional Forum (ARF), created in 1993, becomes important as a network for dialogue in the Pacific area. Including

external countries such as China or the United States³, ARF has been a forum for dialogue, consultation, mediation and negotiation, a “talking shop” implementing confidence-building measures and preventive diplomacy (Cameron, 2005). Using two-track diplomacy, ARF has a limited role, being a meeting point where a very heterogeneous group of countries discuss security issues in a fluid and informal style, preferring to reach a consensus or negotiating bilaterally (Yeo, 2006)⁴.

However, ASEAN, despite the constraints pointed out above, gave a sense of whole to the Southeast Asia region and prevented conflicts as well as inter-state crisis. As a matter of fact, ASEAN sustained the divergences among its members – especially territorial disputes – and also its diplomatic commitment in the Cambodian peace process (Dosch, 2004). Another important achievement of the organization was the idea of cooperative security, including conventional military security and, more recently, the fight against terrorism. The project of a security community is still vague; afterwards it will start only in 2015. At the same time, this project reflects a certain discomfort from Indonesia and Malaysia because of the growing intrusion in security of the USA, China and even Japan, Australia and India.

3. Classic threats

The probability of armed conflicts occurring between Southeast Asian countries is not high, although the territorial and maritime disputes continue to be the source of potential tensions. There is a boundary dispute between Myanmar and Thailand. In what concerns maritime disputes, the most noticeable one is that of the South China Sea between China and Vietnam regarding Paracels and another between six states – China, Taiwan, Vietnam, the Philippines, Malaysia and Brunei – which claim their rights to the Spratly archipelago. Interested in energetic resources from Spratly – natural gas, oil and fish –, those countries are committed to avoid any friction in the area. This agreement was promoted by ASEAN and was established by Manila Declaration in 1992. China ignored this commitment and approved a law claiming a U

3 The external countries are USA, UE, Japan, Russia, China, India, Pakistan, Bangladesh, Mongolia, North Korea, South Korea, Timor-Leste, Papua-New Guinea, Australia, New Zealand and Canada.

4 Quoting Yeo (2006), “it lacks institutional structure and cohesion among members to respond effectively to regional security concerns and challenges (...) The ARF needs to move from an exchange of views to problem solving and concrete cooperation”.

shaped territorial sea that covered almost all the South China Sea. Beijing has proposed a joint exploration but refused multilateral negotiations. However, the United States' growing military presence since 2001 influenced China to start a new deal with ASEAN. Very recently (October 2007), the opposition to the Myanmar military regime became a source of instability, but the resolution of the crisis is reported to be in the hands of China and India, leaving ASEAN a limited role.

4. New threats

ASEAN has had to face a lot of new - in the sense of non-traditional-threats and risks: environmental degradation (e.g., pollution, massive deforestation), trans-national crime (human, arms and drug trafficking, piracy, smuggling), migrations, pandemic diseases (SARS, avian flu) or natural catastrophes. The main concern is obviously terrorism.

Since September 11, and the Bali bombing attacks in 2002, the need and willingness emerged to coordinate the fight against terrorist organizations inspired by violent Islam. According to a report from the US Congress, 37% of the biggest terrorist actions happened in Southeast Asia and 15% of Al-Qaeda found a shelter in the region (Heiduk, Möller, 2004). Islamic groups (some of them linked to Al-Qaeda) have very different natures and goals: Jemaah Islamiyah, Abu Sayyaf and Kumpulan Mujahideen Malaysia (KMM) have a terrorist nature. Other groups associate Islam to autonomic or separatist goals, such as Moro Liberation Front or the Islamic Moro Liberation Front in Philippines; the Aceh Independence Movement and the Mindanao Islamic Liberation Front, in Indonesia; Patani National Liberation Front or Patani Liberation United Organization, in southern Thailand; those have wide popular support, effective political programs and tend to limit violence to military targets. These groups are connected to Saudi Arabia, Egypt, Yemen, Afghanistan and Pakistan. Para-military Islamic inspired groups must also be considered, such as Laskar Jihad in Indonesia.

Trying to face this phenomenon, ASEAN approved several declarations in their annual summits appealing to a joint action to fight terrorism. ASEAN has also defined strategic plans to this very sensible dossier and reinforced the inter-governmental cooperation and intelligence services.

The fact that some of ASEAN states are very fragile and economically disruptive, as well as separatists (Aceh, Papua), tends to create a climate of

instability in the region. In fact, all the new threats pointed out above tend to create dependence from the United States and calls for a growing interference from China and Australia.

5. Foreign Powers in ASEAN

• The United States Shadow

With deep roots in Southeast Asia, in fact since World War II, the United States shadow is overwhelming, not only in the security but also in the economic field. The superpower has established a network of bilateral military alliances with Philippines and Thailand and even with Singapore. After September 11, the United States reinforced their security assistance and launched the ‘Enterprise for ASEAN Initiative’ in order to create free trade agreements between USA and each ASEAN country. Although China is increasingly becoming an important competitor, ASEAN still gives a very relevant role to the USA (and also to India) to avoid hegemonic Chinese presence, especially in economic terms.

• China Connection

There are variations in ASEAN’s member-states’ feelings about China. Traditionally, Thailand and Singapore regard China with less apprehension than those which have maritime disputes over the China South Sea. Since the end of the 90’s, Chinese diplomacy has been deepening economic and political relations with several countries in the region. This new orientation has its most relevant event in the signature in 2002 of the cooperation agreement between China and ASEAN, where the creation of free trade area for 2010 was defined. Noteworthy is also the strategic partnership for peace and security in 2002, for pacific settlement of disputes in South China Sea⁵. China is also a member of ARF and is very enthusiastic with the ASEAN+3 initiative, which will form, in 2010, the greatest free trade area in Eastern Asia, with 1.8 billion people and a GDP of \$2000 billions (Boisseau du Rocher, 2006).

5 Declaration on the Conduct of Parties in the South China Sea, <http://www.aseansec.org/13163.htm>

•The European Link

Europe has a significant relationship with ASEAN through ASEM dialogue and ARF membership and also through bilateral and multilateral trade agreements.

Europe is indeed ASEAN's third trade partner and its second export market. Economies oriented towards exportation and a huge market above 500 millions people makes this part of the world not neglectful. EU-ASEAN trade represents 5,8% of the total amount of UE exchanges and 14% of ASEAN's (Niquet, 2007). The project of a free trade area between the two areas is becoming a reality.

As a matter of fact, the then EEC, in the eighties, established a cooperation agreement with ASEAN – the oldest inter-regional connection in the world (Neves, 2004) -, even if the East Timor and Burma issues were a relevant political shadow in this relationship. In addition to this, the 97-98's financial crisis was a major challenge to the deepening of the dialogue, especially in a context of a stronger China's and UE influence in the region. Both are becoming dominant in the area, in economic and security fields, and ASEAN is trying to strengthen the relationship with Europe as a means to reach a more balanced consortium with foreign partners.

Historically, this relationship was established when China did not have diplomatic or trade channels with Europe, so ASEAN was a channel to Far East, and a way to promote commercial exchange. In fact, various trade agreements were convened. During the 90's the biggest decisions were made, including on security issues, through the creation of ARF, where EU has a seat or by setting up of a structure of permanent contact with a broader geographical area, ASEM. It is also a noticeable feature that ASEAN – a project of regionalism – has always looked upon European model, although with a different and peculiar style, named the *ASEAN Way*.

Dialogue has been fruitful in areas such as transportation, sanitary risks, environmental and energetic issues, technical and scientific cooperation; it is also generally accepted that European discourse on preventing conflicts and integration progresses is taken into account (Niquet, 2006). Ache's example is perhaps the best to show the success of an integrated solution for which UE contributed a lot.

6. ASEAN's Constraints

The whole ASEAN project is strictly connected to individual state-building processes which have to face irredentism, natural catastrophes, contrasting levels of development, rumours of *coup-d'État*, political opposition and Muslim fundamentalist inspired terrorism, a myriad of troubling and destabilising issues.

There are a number of constraints not favouring the emergence of a Eurasian world order focused on soft power, which is list below:

- Integration cannot be regarded in terms of economy or trade and implies other relevant issues, such as security, justice or culture (including human rights)⁶. A “holistic perspective” is needed (Neves, 2004). Asian side is still not predisposed to accept this reality, even if certain concepts have been put forward, such as “comprehensive security” or the Bali-Concord II project, in which the constitution of a security community is included⁷. The question raised a new dimension when integrated in the global fight against terrorism and other type of new threats (pandemics, natural catastrophes, piracy, arms smuggling...). This kind of phenomena has strong manifestations in the region.

- The United States reinforced their military presence in Southeast Asia and are thinking of a more prominent role for APEC as well as more active presence in ASEAN; ASEAN does not manage to continue without this protection and uses it to balance China's expansion.

- Prevailing institutional deficits and asymmetries explains a weak inter-regionalism and are preventing a more efficient regional integration process. ASEAN has above all been a sum of *nation* and *state-building* projects, with strong roots in the sovereignty paradigm inherited from pacific coexistence principles. The importance accorded by Europe to governance and human rights questions has been a severe limitation to a deeper relationship.

- Although ASEAN is a major actor in defining Asian's regionalism, its role has essentially been that of bridging the perennial divisions. In this sense, as an institution, it does not reflect a real political weight.

6 Political-strategical dimension is given in the European's Commission communication *Europe and Asia: A Strategic Framework for Enhanced Partnership* (2001), in which is supported the reinforcement of European presence in both economic and political dimensions.

7 In the EU-ASEAN Ministerial Meeting, January 2003, it has been convened that counter-terrorism action would be a priority for both and was approved a *Joint Declaration on Cooperation Against Terrorism*.

7. Concluding Remarks

Socialization processes and normative production in ASEAN still present nuances resulting not only from the differences among its member-states but also from the full respect to sovereignty and consensus decision-making. The shadow of American security is again essential (after a downsizing in the 90's), particularly in the fight against terrorism. Southeast Asia was considered the 'second front' by the American administration.

Being such a heterogeneous region, with very weak countries, some of them potentially "failed-states", as well as a succession of complex facts, made it certainly hard for ASEAN to fulfil its goals. There is an urgent need to strengthen regional cooperation in order to make the group relevant in international relations and a significant regional player. Benedict Anderson's *imagined community* concept could be applied to the ASEAN project.

The financial crisis of 1997-98, followed by East Timor crisis⁸ and then the terrorist threat, placed ASEAN under stress and denounced its institutional weakness and the lack of effective cooperation. In fact, all the evolution of this organization has shown that the multilateral approach is limited by the "ASEAN Way" and its usual low level of formality and intrusiveness. In these circumstances, it is extremely difficult to define common answers to common challenges and problems. Cooperation is still seen as a potential danger to sovereignty and one cannot avoid feeling the integration project as very attractive in a way, but sometimes lacking substance and credibility.

Nevertheless, ASEAN is a group of countries with economic strength, representing 33% of the world population and 25% of World GDP (Boisseau du Rocher, 2006). Export-oriented economies allied in a market above the 500 million consumers make this part of the world not neglectful. It should be noted that ASEAN is the only regional integration project with some degree of institutionalization (especially since the financial crisis) and, despite the constraints pointed out above, there is a group dynamics which contributes strongly to the whole being a major partner for the rest of the world, not far from East Asian great powers: China, India and Japan.

8 None of the ASEAN countries was able to lead the United Nations mission of peace enforcement. This is mainly explained by its resistance to break non-interference principle. Even during Indonesia's political transition to democracy, the intervention in East Timor was seen as rather embarrassing.

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“Non-Resident” Main Actors

The United States and East Asia

Carlos Gaspar

In 1942, Nicholas Spykman wrote, “the remarkable similarity of the geographic position of the United States in regard to Europe and Asia is, however, not paralleled by a similarity in political relations. On the contrary, they have been quite different. The United States has usually accepted and supported the continental policy of Great Britain but the continental policy of Japan, the dominant maritime power in Asia, has been systematically opposed.”¹

The United States has commonly used different strategies for Europe and Asia. In 1905, the United States, Great Britain and Japan were allies against Russia, Germany and France, which wanted to accelerate the process of China’s disintegration. The convergence between the three major maritime powers re-emerged during World War I. However, in the 1921 Washington Conference, the United States demanded that Britain severed its alliance with Japan, and opposed the Japanese attempt to establish the British balance-of-power model in the Far East, which included the division of China and the forming of new states in the industrial regions of Northern China and Manchuria. Hence, in 1932, the United States did not recognize the State of Manchukuo and, in 1937, condemned the Japanese invasion of Northern China. This invasion was unable to overcome Chinese resistance as the Japanese only managed to occupy the

1 Nicholas Spykman (1942). *America’s strategy in world politics*: 137. New York: Harcourt, Brace and Company.

coastal provinces. During this period, the United States tried to restrain Japan, both by establishing an alliance with non-Asian colonial powers, such as Great Britain and the Netherlands, and by empowering Asian states, namely China, essential to counterbalance the Japanese imperial expansion. The German-Japanese alliance, reiterated in September 1940, confirmed the differentiation rule and in World War II, in Europe, the United States were on the side of the dominant maritime power against Germany, and in Asia they were against the dominant maritime power.²

The reversal of alliances at the beginning of the Cold War confirmed the old rule. The main allies of the United States in the effort to contain the Soviet Union were their former World War II enemies – Japan and Germany. The convergence with Japan was strengthened after the communist takeover in China, as the People’s Republic of China became a part of the “socialist camp” and because of the Korean War. At that moment, United States established alliances with Japan, South Korea, Taiwan and the Philippines, which form the North American regional security system in East Asia. This system of “hub and spokes” in which the United States are the hub and the bilateral alliances with their Asian partners are the spokes³, is fundamentally different from the European model, in which the United States created a multilateral regional security system through the Atlantic Alliance⁴.

Thus, during the Cold War, the differentiation rule was evident both by the continental alliance against a continental power in Europe and by the maritime alliance against a continental power in Asia, as well as by the difference between the multilateral model of European alliances and the bilateral model of Asian alliances. An explanation for choosing different models may lie in the importance attributed to the European front by the strategy of containment. Notwithstanding, American military interventions were more frequent in the

2 Nicholas Spykman: 159.

3 “**Hub and spokes**” seems to have become the most common name to describe the American security model in East Asia. Older definitions include “**balanced wheel**” or “**spoked wheel**”, as well as an eastern version, the “**open fan**” model, introduced in 1991 by the Secretary of State, James Baker III. For contemporary references, see, *inter alia* Daniel Twinning (2007). “America’s grand design in Asia”. *The Washington Quarterly* 30 (3) : 79. For older references, see James Baker III (1991). “America in Asia. Emerging architecture for a Pacific Community”. *Foreign Affairs* 70 (5) : 1-18. Gary Klinworth (1992). “Asia Pacific : more security, less uncertainty, new opportunities”, *The Pacific Review* 5 (3) : 226-227. Hee Kwon Park (1993) “Multilateral security cooperation”, *The Pacific Review* 6 (3) : 254.

4 In 1942, Nicholas Spykman proposed that this model - “**a regional League of Nations with the United States as an extra-regional member**” were applied both in Europe and in Asia. Spykman considered that the bilateral alliance with Japan was inadequate and introduced a regional collective security formula as an alternative to European integration, since an European federation would go against American interest. Nicholas Spykman (1942) : 466-468.

Asian front, as was made evident by the war in Korea and later the war in Vietnam.⁵ (The Soviet Union responded to the creation of the Atlantic Alliance with the establishment of the Warsaw Pact, which did not include China, North Korea or North Vietnam. The territorial continuity of the “socialist camp”, from Berlin to Hanoi, did not stop the Soviet Union from following the same pattern of different institutional models for Western and Eastern alliances).

The re-emergence of China made a difference in international and regional balance. The United States supported China as a Permanent Member of the United Nations Security Council. With the defeat and occupation of Japan, the Sino-American alliance should have guaranteed the stability of East Asia. However, the civil war compromised this strategy and the unification of mainland China in 1949-1950 was ultimately achieved under the aegis of China’s Communist Party with crucial support afforded by the Soviet Union. The Korean War and Chinese intervention were decisive for the United States to be able to complete the *renversement des alliances*, in Europe and in Asia, and to strengthen maritime control to restrain their continental foes, the basis of the balance of power in East Asia.

However, the ideological convergence between China and the Soviet Union was not enough to overcome the strategic divergences between the two largest continental powers. In 1972, the *rapprochement* between the United States and China marked a significant change in international politics. The bipolar competition became triangular, as the United States tried to take advantage of the rivalry between the two communist powers to reinforce its position. On the other hand, the quasi-alliance between the United States and China, in the aftermath of the Soviet invasion of Afghanistan in 1979, put a temporary halt to the Sino-American competition in East Asia. The parallel process of normalization of relations between China and Japan occurred in this context and it was a crucial factor for the success of post-Maoist succession and of the “Four Modernizations” reform program, which depended on the gradual opening of Chinese economy.

Thus, the strategic transition in East Asia preceded the end of the Cold War. The re-emergence of China, delayed by the civil war and the crises of the communist regime, finally began in December 1978 with a new leadership ready to side with the United States against the Soviet threat.

5 G. John Ikenberry (2007). **America and the reform of global institutions**. Peter Katzenstein values identity and cultural dimensions. Cf. Peter Katzenstein (2002). “Why there is no NATO in Asia? Identity, regionalism and the origins of multilateralism”. **International Organization** 56 (3) : 575-605.

The rise of China was obviously a decisive factor in the shift of regional strategic balances. Its impact had been predicted long before: “**A modern, vitalized, and militarized China of 400 million people is going to be a threat not only to Japan, but also to the position of the Western powers in the Eastern Mediterranean**”.⁶ This prediction justified the early recognition of China’s power, in 1945, and the acknowledgement that its strategic potential – a vast continental mass with a long coastal strip – would condition all other Asian powers, including the US.

The re-emergence of China

The international and domestic dimensions of China’s modernization process prove to be incongruent: the alliance with the US consolidated the post-Maoist communist regime. On the Chinese side, the nature of the communist regime allowed for rapid changes in external alignments and, from 1985, the American alliance was replaced by a new strategy of “equidistance” towards both the US and the Soviet Union. The second *détente* ensured not only the Soviet withdrawal of SS20 missiles aimed at Western Europe and China, but also a bilateral treaty on the borders between the Soviet Union and China. However, the Sino-Soviet *rapprochement* did not stop the Chinese communist leaders from rejecting *perestroika*, violently repressing demonstrations in Tian’anmen in June 1989: the Chinese reform did not include political liberalization but focused on economic modernization.

The end of the Cold War was not the beginning of the Asian democratic transition but it was a decisive turning point, in particular for China. Firstly, the dismembering of the Soviet (and Russian) empire increased China’s security, since there was no longer a permanent military threat on continental borders. Moreover, the borders between Russia and China were significantly reduced due to the separation of the New Independent States of Central Asia and the increasing autonomy of Mongolia. China expects to overcome Russia in the ranking of world powers⁷ and, simultaneously, wants to consolidate a bilateral strategic partnership with the Euro-Asian power. Secondly, this shift offered a unique opportunity to relocate the strategic centre of China from the **hinterland** to the coast, allowing for its inclusion in the maritime axis of East Asia.

6 Nicholas Spykman (1942) : 469.

7 Yan Xuetong (2006). “The rise of China and its power status”. *Chinese Journal of International Politics* 1: 5-33.

The regional dimension became a priority in China's foreign policies and its re-insertion in Asia was crucial to consolidate the dynamics of regionalization of East Asia. China normalized its diplomatic relations with all the regional states, including Indonesia, Vietnam, and South Korea and soon became an indispensable economic partner and the main destination of Asian investment. The country's behaviour during the regional financial crisis of 1998 was decisive to consolidate its credibility. Once again, China became the main Asian power and the international recognition of such status will be a crucial step in its rise. Thirdly, the end of the Soviet communist regime and the victory of the democratic alliance in the Cold War exposed the political vulnerability of the Chinese communist regime. Communism was no longer a relevant international movement and had lost its ideological appeal. To respond to the legitimacy crisis of the communist regime, Chinese leaders started to value nationalism and the restoration of China's prestige. However, they rejected political liberalization – the “fifth modernization” – and denounced the strategies of “peaceful evolution”, which destroyed communism from the inside in Europe, as a strategic weapon of the US against its autocratic opponents, always with the aim of restraining the rise of China.

China's regional projection encompasses a revisionist dimension⁸ made manifest in its sovereignty demands over the Senkaku islands (Diaoyu), claimed by Japan, and the Spratly archipelago (Nansha), located at the centre of the Asian maritime corridor, claimed by Indonesia, the Philippines, Malaysia and Borneo. Similarly, China's exhibition of its military power against Taiwan during the presidential elections of 1995 confirmed the regional perception of threat posed by the re-emergence of East Asia's traditional hegemonic power.

Chinese leaders tried to soften that image. In 1997 they presented a new “security concept” in which they adopted the principles of “cooperative security” as the rule for international relations, in contrast with the military alliances inherited from the Cold War. Moreover, China gradually tried to join regional and international institutions, namely the World Trade Organization (WTO) and the Association of South East Asia Nations (ASEAN), to show its recognition of the virtues of multilateralism.⁹ (One of the virtues is the pos-

8 On 25 February 1992, China implemented the Law on Territorial Waters and Contiguous Areas which include Taiwan and the islands of Diaoyu, Penghu, Dogsha, Xisha, Nansha and others in the People's Republic of China.

9 China's embrace of multilateralism in 1997 was analyzed by Alastair Iain Johnston, Paul Evans. China's engagement with multilateral security institutions in Alastair Iain Johnston, Robert Ross, editors (1999). **Engaging China**. New York: Routledge. On the evolution of China's foreign policies, see Gates Bill (2007). **Rising star. China's new security diplomacy**. Washington: Brookings Institution.

sibility of excluding the US from regional institutions, such as the Shanghai Cooperation Organization (SCO), which members are China, Russia and the five post-Soviet republics of Central Asia, as well as the East Asia Summit (EAS) or a future East Asia Community).

Since 2003, the Chinese leadership has allowed for the development of the “peaceful rise”¹⁰ theory, trying to demonstrate that China’s re-emergence would contribute to international stability and would not have the same dramatic consequences as the rise of Germany or Japan in the last century. It is not clear why this original theory is no longer officially endorsed.¹¹ Its premises could have been construed as a renunciation to the use of force in the case of a Taiwanese declaration of independence, an anathema for the dominant nationalistic ideology and, its reference to the “rise of China” could evoke the restoration of China’s imperial status, as a hegemonic power.¹² Yet, the main ideas of the theory of “peaceful rise” are still valid, even when a number of Chinese strategists defend the need for a more assertive position, matching the growing confidence of national elites.¹³ For China to fulfil its strategic potential, it must modernize, which implies greater access to European, Japanese and American markets, investment and technology. It also needs regional stability in order to focus its political resources on home priorities. China is still a backward, developing country, trying to solve its huge social and economic problems. It is not yet in a position to be considered a serious strategic threat to the US.

Obviously, the denial of the inevitable strategic consequences of China’s rise, including the consolidation of its regional hegemonic position, may be interpreted as a ploy to neutralize the responses by the US and the Asian regional powers that are engaged in maintaining the Asian balance of power.

The normalization of Japan and the revelation of India

Both Japan and India, as major powers, have an increasing importance in the definition of the strategic transition in Asia as a whole.

10 Zheng Bijian (2005). **China’s peaceful rise**. Washington: Brookings Institution.

11 Bonnie Glaser, Evan Medeiros (2007). “The changing ecology of foreign-policy making in China: the ascension and demise of the theory of ‘Peaceful rise’”. **The China Quarterly** 190: 291-310.

12 Yan Xuetong (2006): 13.

13 On China’s increasing confidence, see David Lampton (2005). “Paradigm lost. The demise of weak China”. **The National Interest** 3: 73-80.

After the Cold War, Japan went through an economic recession and successive political crises, which conditioned its international policies. However, the rise of China, the enduring Asian conflicts of the Cold War and the US' strategic redeployment at the end of bipolar competition, made it imperative for Japan to review its international strategy and domestic political consensus on foreign and defence policies, namely the need to overcome its constitutional constraints regarding external military intervention.

The first Korean nuclear crisis, in 1994-1995, and the US response revealed a double risk to Asia's main maritime power. Japan was threatened both by the development of North Korea's offensive ballistic capacity and the risk of abandonment by the US, Japan's sole defence against a nuclear threat. The Taiwan crisis in 1996 showed the Chinese determination to engage in a war against the US if Taiwanese authorities declared independence, as well as the high probability of Japan becoming involved in this conflict due to its American alliance.

In Europe, the Cold War conflicts disappeared after the bipolar dispute, resolved with Germany's reunification and the democratic change in the political regimes under Soviet influence. In Asia, the two main regional conflicts of the Cold War – the division of China and the division of Korea – not only remained open but became more acute since 1991. The issue of Taiwan is a critical issue for the Chinese leadership - **“C'est notre Alsace-Lorraine !”**¹⁴ - and the isolation of the North Korean regime made it even more unpredictable and dangerous.

Moreover, China's regional projection in the South China's seas demonstrated that it is reinforcing its naval capabilities in order to control major sea lanes, which are vital to Japan's security and economy, given that regardless of its civilian nuclear program, it remains the most dependent Asian power on energy resources' imports.

The Japanese response to regional change became clear with the 1996 US-Japan joint declaration, with the new Japanese military and strategic doctrines and, in particular, after 9/11, with the new internal consensus on Japan's “normalization” allowing for the recognition of its status as a military power, which parallels Germany's evolution after the war in Kosovo and its growing presence in UN, NATO and EU international military missions. These “coalitions of the willing” are led by the US in the Middle East, in Central Asia and in the Indian Ocean, where the Japanese navy, for the first time since World

¹⁴ The analogy was used by a Chinese diplomat, as quoted by Thérèse Delpech (2005). **Lensauvagement. Le retour de la barbarie au XXIe siècle** : 278. Paris: Grasset.

War II plays an important logistic role in supplying the Western allied forces, namely in Afghanistan.¹⁵

The continuity of the US-Japan alliance was challenged after the end of the Cold War¹⁶ but the main purpose of Japanese strategy remains the strengthening of its alliance with the US, on a model similar to the “special relationship” between Great Britain and the United States.¹⁷ One hundred years later, the three old maritime powers become closer once again. However, Japan is more dependent on America than Britain. Japan, just like Germany and unlike Great Britain, is not a nuclear power and must face two nearby regional conflicts involving major powers. Besides, Japan has no multilateral framework, like the European Union or the Atlantic Alliance, to leverage its relationship with the United States. The quality of the Japanese strategy lies precisely in its assumption of extreme dependency in every dimension, though attempting to safeguard its position within the bilateral alliance and the possibility of becoming a nuclear power.

Japan’s strategic decision and the corresponding modernization of its armed forces are crucial to regional balance and to counteract the re-emergence of China. However, it limits the ability of the major Asian maritime power to become an autonomous pole in East Asia’s power structure.¹⁸ Similarly, the “special relationship” also limited Great Britain, a major European maritime power, in playing a greater role in the European Union’s integration process. Perhaps this explains why Japanese diplomacy wants to move beyond the strict East Asia regional framework, namely by engaging in relations with India, as part of a “broader Asia”¹⁹, or by bringing together Australia, India and the US

15 Christopher Hughes (2005). **Japan’s emergence as a ‘normal’ military power**. London: IISS Adelphi Paper 368-9.

16 Michael Mastanduno. Incomplete hegemony and security order in the Asia Pacific in G. John Ikenberry, editor (2002). **America unrivaled. The future of the balance of power**: 201. Ithaca: Cornell University Press.

17 The analogy is mentioned in the Nye-Armitage Report on the relations between the United States and Japan, signed by Robert Armitage and Joseph Nye, among others. Institute for National Strategic Studies. **The United States and Japan: advancing toward a mature relationship**. INSS Special Report, October 2000.

18 Robert Ross has a similar argument when he tries to demonstrate that the bipolar structure in East Asia is dominated by the US and China, while Japan’s position is one of regional strategic inferiority. He is partially right when he underlines the limits of Japan but China has not yet showed its qualities as an ordering power in East Asia and, like Japan, it does not guarantee security of any of its regional allies. Robert Ross. Bipolarity and balancing in East Asia in T.V.Paul, James Wirtz, Michael Fortmann, editors (2004). **Balance of power. Theory and practice in the twenty-first century**: 267-304. Stanford : Stanford University Press.

19 The former Prime Minister Shinzo Abe chose this theme for his last official visit to India, saying that “a ‘broader Asia’ that broke away geographical boundaries is now beginning to take on a distinct

as democratic partners on the “Quadrilateral Initiative”²⁰, or by promoting the inter-continental “Arc of Freedom and Prosperity”.²¹

The end of the Cold War and the rise of China have also caused a radical change in both India’s domestic and foreign policies.

The dissolution of the Soviet Union made India lose its only ally; the end of the divide between the two world powers made non-alignment superfluous. Besides, with the demise of communism and China’s embrace of the virtues of market economy, India faced the risk of remaining the last stronghold of socialism. Since 1991, Indian elites responded to these new developments by radically changing their economic policies, allowing for a rapid modernization and an impressive growth and, simultaneously, by changing their foreign policies.

In international terms, India’s crucial decision was to impose the recognition of its status as a nuclear power. In 1998, India’s (and Pakistan’s) nuclear tests were condemned both by the United States and by China. Yet, the following year, the United States started the process of acknowledging India as a major power. Firstly, the US valued India as a democratic partner – the world’s “largest democracy” – as it adopted a moderate position on the Kashmir question and distanced itself from Pakistan, in order to be able to mediate the two rival powers of South Asia, in 1999, in the Kargil War. Secondly, the recognition of the rise of India was associated to the identification of China as a “strategic competitor” of the US. The relations between India and the US grew stronger with the “war on terrorism” in the aftermath of 9/11. India not only has the largest national Islamic community but also a long experience in fighting pan-Islamic terrorist organizations. Thirdly, the India-United States Strategic Partnership, the agreements on defence cooperation and civil nuclear cooperation and, the July 2005 bilateral presidential summit, all contributed to the strategic convergence between the two powers. (India, where anti-Americanism ideas were prevalent in domestic and foreign policies, became one of the few countries in which US image has improved in the last few years).

form.” MOFA. “**Confluence of Two Seas**”. Speech by H.E.M. Shinzo Abe, Prime Minister of Japan at the Parliament of the Republic of India, 22 August 2007. In his book, “Towards a beautiful country”, published in July 2006, Abe wrote that “it will not be surprising if in ten years time, Japan-India relations overtake Japan-US and Japan-China relations.”

20 Japan, US, India and Australia met in May 2007 on the sidelines of the ASEAN ARF in Manila as the “Quadrilateral Initiative”. Brama Chellaney. “the New Great Game”, *Asian Age*, June 2, 2007. C. Raja Mohan. “Asia’s new ‘democratic quad’”. *ISN Security Watch*, 19 March 2007.

21 MOFA. **On the ‘Arc of Freedom and prosperity’**. Address by H.E.M. Taro Aso, Minister of Foreign Affairs, Japan Forum on International relations, 12 March 2007.

This convergence represents a revolution in terms of Indian foreign policy²², yet it is incomplete and still reversible. India's main motivation is the rise of China, which has an influence beyond the limits of East Asia.

The creation of the Shanghai Cooperation Organization (SCO), into which Iran was admitted as an observer, the consolidation of the alliance between China and Pakistan and the identification of Chinese naval facilities in the Indian Ocean (in Myanmar as well as in Pakistan) point to a pan-Asiatic Chinese strategy that involves a maritime dimension. This has become more relevant due to the increasing dependence of all the major Asian powers on the access to energy resources in the Persian Gulf. India tried to respond to Chinese penetration with the strengthening of its position as the main regional power of South Asia, which implies controlling bilateral tensions with Pakistan and the strengthening of its relations with small and medium states within the frame of the South Asia Association for Regional Cooperation (SAARC), which was enlarged to include Afghanistan. India stepped up its participation in the multilateral Asian network including the East Asia Summit (EAS) and the ASEAN Regional Forum (ARF). India's application to the Asia Pacific Economic Forum (APEC), presented by Australia is yet to be accepted. India is also engaging further with the United States through the development of stronger relations with democratic regional allies of the United States, namely Japan and Australia, which have come together as partners in a tentative Quad-rilateral security arrangement.

The parallel re-emergence of China and India, as well as Japan's "normalization" are transforming the strategic landscape in Asia. The old regional boundaries defined by the imperialist program of the Greater East Asia Sphere of Co-Prosperity, which led the Japanese expansion up to Burma and East Timor, are being challenged by the rise of Greater Asia as an international region, including East, South and Central Asia and, eventually, Australia and the South Pacific.

The contrast between the immobility of Western Europe, which seems to be locked in the Kantian democratic peace, and the dynamism of Asia driven by the simultaneous rise of two great continental powers, as well as the attempt by Japan to restore its role as a maritime power, shows how deeply international

22 C. Raja Mohan (2003). **Crossing the Rubicon. The shaping of India's foreign policy.** New Delhi : Penguin Books. See also Brama Chellaney (2006). **The Asian juggernaut. The rise of China, India and Japan.** New Delhi : HarperCollins.

politics has changed since the beginning of the 20th century. In response to the new trends, America's "strategic eastward movement has accelerated"²³.

The Strategies of the United States

The importance of China to the United States' international and regional strategy is gaining recognition in American politics: the relations with China are becoming the most important bilateral relationship for the United States in this century²⁴.

However, there are many different interpretations as to the meaning of such an historical change, which is placing Asia at the top of the United States' priorities, and no consensus on the most effective American strategy to address this new situation. Firstly, there are conflicting positions as to whether the US should avoid over-extension or intervene in accordance to its responsibilities as the keeper of international stability²⁵. Secondly, there are the different interpretations on the significance of the re-emergence of China: the pessimism of the "offensive realists", who consider the confrontation between the United States and China to be inevitable, opposes the pragmatism of the more moderate realists, or "defensive realists" for whom the rise of new powers is part of natural process and as such, try to combine the need for their integration with the consolidation of international balance²⁶.

The strategy of offshore balancing claims the US should distance itself from regional conflicts in order to limit its military intervention to those in which its core national interests are at stake. The United States should recognize that nothing can be done against China's rise if it is not willing to resort to preventive war to stop it. On the other hand, multipolarity may be considered positive for the United States' international position considering that new

23 In a phrase ascribed to Hu Jintao, the paramount leader of the People's Republic of China. Andrew Nathan, Bruce Giley, editores (2002). **China's new rulers. The secret files** : 207. London : Granta.

24 G. John Ikenberry. Anne-Marie Slaughter, co-directors (2006). **Forging a world of liberty under law. U.S. National Security in the 21st century. Final Report of the Princeton Project on National Security** : 51. Princeton : The Princeton Project Papers, The Woodrow Wilson School of Public and International Affairs. Ver também Francis Fukuyama, G. John Ikenberry. **Report of the Working Group on Grand Strategy Choices** : 14-25. Princeton : The Princeton Project on National Security, September 2005.

25 See, respectively, Christopher Layne (2006). **The peace of illusions**. Ithaca : Cornell University Press. Robert Art (2003). **A grand strategy for America**. Ithaca : Cornell University Press.

26 See, respectively, John Mearsheimer (2001). **The tragedy of great power politics** : 401-404. New York : W.W. Norton. Kenneth Waltz. Structural realism after the Cold War in G. John Ikenberry, editor (2002). **America unrivaled. The future of the balance of power** : 54-65.

emerging powers may be counter-balanced by other regional powers. American strategy in Asia should recover the liberty to choose its allies – China or Japan, China or India²⁷ – without having to become hostage to its former alliances. The question of Taiwan should be immediately eliminated as it represents an unacceptable risk of war between the United States and China and it does not concern essential American interests, which must exclude the principle of democratic solidarity²⁸.

On the contrary, the strategy of selective engagement avoids the breaking up of the Cold War alliances. Those “permanent allies” are a unique means for the United States to maintain international stability, though they should not trap the US in the inertia of the past that hinders a flexible reaction to changes imposed by emerging powers. If China remains united and competent, its rise will be inevitable: the best response is to recognize its legitimate interests, to integrate China within international institutions and to counter-balance its increasing weight. The alliance with Japan and the naval mastery of East Asia are essential to guarantee the United States’ status as a great Asian power and simultaneously, to avoid reviving the former alliance between Russia and China²⁹. The Taiwan question represents a risk that the United States cannot overlook: Chinese leaders must be convinced that the unification of China should not lead them to risk military escalation between two nuclear powers, which may be triggered by miscalculation.³⁰

The opposition between “offensive realists” and “defensive realists” is based on the analysis of the international status and the meaning of China strategies, which still raise many doubts given the extreme opacity of Chinese decision-making and the seclusion of its political elites.

The rise of a great power is a classical topic in international relations but it does not always take on the same meaning, considering that not all emerging powers follow the same pattern.

The first phase of the rise of Germany as a great continental power has striking affinities with the rise of China, a century later, as a great continental

27 John Garver (2002). The China-India-U.S. triangle. Strategic relations in the post-Cold War era. **NBR Analysis** 15 (5).

28 Christopher Layne. China’s role in American grand strategy : partner, regional power or great power rival ? in Jim Rolfe, editor (2004). **The Asia-Pacific: A Region in Transition** : 54-80. Honolulu : Asia-Pacific Center for Security Studies.

29 Kenneth Waltz. Structural realism after the Cold War in G. John Ikenberry, editor (2002). **America unrivaled. The future of the balance of power** : 62-64.

30 Robert Art (2007). “Agreeing to agree (and disagree)”. **The National Interest** 89 : 36.

power³¹. Essentially, both tried to avoid that their rapid growth was interpreted as a risk and thus avoid the interference of counterbalancing coalitions during vulnerable stages of their emergence. Hence, Bismarck concentrated on the integration of unified Germany within the existing European and international order. The problem seems to be in the second phase, if and when integration strategies are substituted by competition strategies challenging the predominant maritime powers and embarking on imperialist expansion. In the case of Germany, Great Britain was unable to stop the European central power from becoming a revisionist power and tried to counter-balance the **Weltmachtpolitik** by means of alliances with France and Russia. Insofar as China is concerned, what must be assessed is whether the Asian central power has limited objectives, if it wants to be a part of international order, or if on the contrary, its is a revisionist power determined to disrupt regional and international stability³².

For “offensive realists”, the shift to an expansionist stage is only a question of time since the quest for maximizing power is inherent to the rivalry between the United States and China. For “defensive realists”, Chinese security interests exclude a voluntarist strategy, which would have to overcome the limitations imposed by the technological and military gap and by China’s vulnerable geographical position in challenging the international pre-eminence of the United States whose position is much stronger than that of Great Britain in the beginning of the 20th century.

In a sense, “offensive realists” consider it inevitable that China will become a strategic challenger of the United States, thus leading to the confrontation of the two powers³³. Thus, they favour a strategy of containment similar to the one that was able to bring about Soviet defeat during the Cold War.

As a great continental power and communist regime, China has affinities with the Russian empire and with the former Soviet Union. Common charac-

31 The German analogy was developed by Avery Goldstein. An emerging China’s emerging grand strategy. A Neo-Bismarckian turn in G. John Ikenberry, Michael Mastanduno, editores (2003). **International Relations Theory and the Asia Pacific** : 57-106. New York: Columbia University Press.

32 The opposition between an emerging power with limited objectives and a revisionist power with unlimited objectives is not well elaborated. The classic distinction established by Hans Morgenthau and Raymond Aron separate revisionist powers – the Germany of 1914 – from revolutionary powers – the Germany of 1939 – only the latter have unlimited objectives. As the Popular Republic of China’s status as a revolutionary power does not portray great credibility, what is questioned is whether it may be considered a power with **status quo** – the objective of its strategy is integration – or if it should be considered a revisionist power – its strategy has the goal of altering the way international power is currently distributed. Cf. For further information on this matter, see Alastair Iain Johnston (2003). “Is China a status quo power ?” **International Security** 27 (4) : 5-56. Denny Roy (2004). “China’s reaction to American predominance”. **Survival** 45 (3) : 57-78.

33 John Mearsheimer. **Why China’s rise will not be peaceful**, 17 September 2004.

teristics of continental totalitarianism include resentment towards predominant powers, opposition towards democratic liberalism, considered by autocratic leaders as a threat to political stability and state unity, and anxiety towards the risk of encirclement and isolation. The combination of increasing international projection with the legitimacy crisis of the political regime – the Soviet Union in 1945 and China in the Post-Cold War – may stimulate offensive external strategies in order to respond to the extreme domestic nationalist demands. Notwithstanding these common traits, they represent different threats. On the one hand, while the Soviet Union could simultaneously threaten Europe and Asia's main industrial centres, as well as the Middle East's energy reserves, China is a comparatively peripheral continental power without the conditions for a strategic projection in Europe or the Persian Gulf³⁴. On the other, not only has China renounced communist internationalism from the beginning of post-Maoist transition but Communism has also lost its projection as a universalist ideology. Hence, there is no ideological competition between the Imperial Republic and the Middle Kingdom comparable to that of the relations established between the United States and the Soviet Union during the Cold War. China fears the strategies of “peaceful evolution” and “communist capitalism” does not have the necessary conditions to present itself as an alternative to the political, economic and social model of liberal market economies, except in specific cases³⁵.

On the opposing side, “defensive realists” believe that China's interests must be taken into account and its policies orientated towards gradual integration in the international system³⁶. Its premises tend to mirror those of the Chinese theory of “peaceful rise” to demonstrate that the new power is not in a position to threaten international stability or the United States' key role in East Asia and has reached an unprecedented level of integration in international norms and institutions³⁷. This “general line” is in fact very much in accordance with both China's interests and its classic strategic culture³⁸. Contrary to the

34 Robert Art (2007) : 35.

35 But Robert Kagan anticipates the solidarity between despotic regimes, including the Sino-Russian authoritarian convergence as a distinctive trait of Post-Cold War international politics. Robert Kagan (2007). “End of dreams, return of history”. *Policy Review* 4.

36 For further information on engagement strategy see Alastair Iain Johnston, Robert Ross, editores (1999). **Engaging China. The management of an emerging power.**

37 The comparison is legitimate but not very demanding considering that until the 1970s The Popular Republic of China was a revolutionary power, lagging behind international institutions. Alastair Iain Johnston (2003).

38 Deng Xiaoping's strategic premise for this phrase “do not rush and hide one's own capacities”. Michael Pillsbury (2000). **China debates the future security environment** : xxiv. Washington: National Defense

Soviet Union, China has become an essential economic partner due to the importance of its industrial production and investments in American economy. An hostile containment strategy would damage the United States' economic interests (and would be useless because China's Asian and European partners would not sustain an American boycott). Moreover, a compromise is possible as there are no relevant strategic issues opposing the United States and China. The Six-Party Talks have both powers committed to putting an end to the North Korean nuclear program namely because China does not want to lose its status as East Asia's sole nuclear power. China should defend the continuity of the alliance between the United States and Japan to avoid the risk of the resurgence of Japanese revisionism and maintain the status of a great Asian maritime non-nuclear power³⁹. Both the United States and China want a stable and open East Asia, as its development is equally important for Chinese modernization and the American economy. The United States' nuclear superiority will not be questioned because of the modernization of China's nuclear power, which is necessary to ensure minimum credibility to its strategic deterrent. The United States may accept the "finlandization" of Korea, with the withdrawal American military and the end of the bilateral alliance, contrary to what happened in Germany⁴⁰. The issue of Taiwan represents a real problem, which should be limited by demonstration of the irrationality of risking a nuclear escalation⁴¹.

In recent years, American strategy has tried to combine elements of integration and containment to bring China's rise under control and consolidate the international system⁴². In this sense, when Robert Zoellick endorsed the importance of the transformation of China into a "responsible stakeholder" of the international system⁴³, he also said that the uncertainty as to a "peaceful rise"

University Press. Ver también Michael Swayne, Ashley Tellis (2000). **Interpreting China's grand strategy: past, present and future**. Santa Monica : Rand.

39 Thomas Christensen. China, the U.S.-Japan alliance and the security dilemma in East Asia in G. John Ikenberry, Michael Mastanduno, editores (2003). **International Relations Theory and the Asia Pacific** : 25-56.

40 Robert Art (2007)

41 Robert Sutter emphasizes the question that Taiwan is the only country that may cause a war between great powers involving the United States. Robert Sutter (2003). "Why China matters". **The Washington Quarterly** 27 (1) : 85. See also Richard Bush, Michael O'Hanlon (2007). **A war like no other. The truth about China's challenge to America**. New Jersey : J.Wiley&Sons.

42 In a phrase ascribed to Wen Jiabao, the two lines are presented as a single strategy: "**The core of American policy towards China is still 'to engage and contain'**". Andrew Nathan, Bruce Giley, editors (2002): 208.

43 At the time, Robert Zoellick was Deputy Secretary of State. See Robert Zoellick. Whither China: from membership to responsibility? Remarks to the National Committee on U.S.-China relations, 21 September 2005. **NBR Analysis** 16 (4): 8, 13.

would lead the United States to adopt a hedging strategy⁴⁴. The reference to the need to hedge against the risks of a downturn in the Chinese strategy was reiterated on the 2006 National Security Strategy⁴⁵. (This hedging strategy is not followed by the United States alone, but also by the Asian powers in their relations with China, as well as by China itself in its relations with the sole remaining international superpower⁴⁶).

In this context, and in tandem with the continuation of the traditional alliances and of the military presence in East Asia, the regional strategy of the United States now has a new dimension to respond to the rise of new regional powers.

The Cold War alliances – the five bilateral alliances between the United States and Japan, South Korea, the Philippines, Thailand and Singapore – continue to be the essence of the regional security architecture and ensure American preponderance in East Asia⁴⁷. Along these same lines, the United States maintain a significant military presence, with the deployment of permanent military forces in regional bases, namely in Japan, in South Korea and in the Philippines, which safeguard their naval mastery in East Asia and the control of the major sea lanes that ensure energy supply flows from the Middle East. Obviously, there is a certain symmetry between the permanence of the

44 The concept of hedging was first used by Robert Art to describe the strategies of the European allies vis-à-vis the United States in the post-Cold War period. In this context, the European powers do not follow a balancing strategy, or even a soft balancing strategy in relation to their main ally, but rather pursue certain precaution policies for those cases of strategic retreat from the United States. The example is the European defence policy, which results from the awareness of the unavailability of North America to intervene in the Balkan civil wars, when the Europeans were unable to intervene and depended on the decision of America in the North Atlantic Treaty Organization (NATO) to mobilize the military resources necessary to respond to the regional crisis. To prevent this situation from repeating itself, in 1998 Great Britain and France initiated the European Security and Defence Policy (ESDP) within the framework of the European Union. The concept of hedging is applied to the Chinese strategy of the United States not only by Robert Zoellick, but also by Evan Medeiros and Daniel Twining. David Lampton tried to develop an intermediate formula – “hedged integration”. See Robert Art. *Europe hedges its security bets* in T.V. Paul, James Wirtz, Michael Fortmann, editors (2004). **Balance of power. Theory and practice in the twenty-first century**: 179-213. Evan Medeiros (2005). “Strategic hedging and the future of Asia-Pacific stability”. *The Washington Quarterly* 29 (1): 145-167. Daniel Twining (2007). “America’s grand design in Asia”. *The Washington Quarterly* 20 (3): 79-94. David Lampton (2005): 75-77.

45 The fourth principle of relations with other “independent power centers” indicates that, “while we do not seek to dictate to other states the choices they make, we do seek to influence the calculations on which those choices are based. We also must hedge appropriately in case states choose unwisely.” The White House. **The National Security Strategy of the United States of America**, March 2006, VIII: C: 36.

46 Rosemary Foot (2006). “Chinese strategies in a US-hegemonic global order: accommodating and hedging”. *International Affairs* 82 (1): 77-94.

47 David Shambaugh (2006). “Asia in transition: the evolving regional order”. *Current History* 4: 153.

alliances and the military position of the United States in Western Europe and in East Asia since the end of the Cold War.

Besides continuity, the United States have to adapt the formula of regional balance of power to the emergence of the new Asian powers and to limit the risks linked to the re-emergence of China, which could yet become a strategic competitor. The hedging strategy represents the dimension of change in the American position. The need to counterbalance China is translated into the support by the United States to the emergence of India as a superpower⁴⁸ and the enlargement of its regional partnerships to Indonesia and Vietnam⁴⁹ – and ultimately Afghanistan, Central Asia and Mongolia, which could maintain additional pressure on the borders of the greatest Asian continental power. India, Indonesia or Vietnam may not become formal allies of the United States, but they do have strong motives to engage in their own hedging strategies to prevent the re-establishment of China's regional hegemony and preserve the regional balance in Asia.

The strategic priority of China is naturally to recover its traditional status in East Asia⁵⁰, which is the key to its international status and an essential pre-condition to be able to question the international predominance of the United States. However, the American strategy sets difficulties to the Chinese strategy as it extends the scope of regional competition beyond the borders of East Asia, including South Asia and Central Asia and connecting the Indian and the Pacific oceans.

The restructuring of the regional alliances of the United States tends to confirm the Asian model in which bilateral relations play a crucial role: the Atlantic Alliance model does not apply to East Asia⁵¹. There is a tendency to strengthen bilateral relations among United States' allies, such as a new defence alliance between Japan and Australia, which are coordinated with the United States within the Trilateral Security Dialogue, which in turn, could be extended to India if the Quadrilateral Initiative establishes itself as a security mechanism. This scenario could point to a convergence between regional democracies, an

48 Daniel Twining considers the US decision of March 2005 – “helping India become a great power” – as an unprecedented strategy in their external policy. However, the United States not only re-established Germany and Japan as superpowers after 1945, but also supported the creation of a unified Europe, the only superpower that could stand as an effective strategic rival of the United States besides the Soviet Union. Daniel Twining (2007): 82.

49 Daniel Twining (2007): 83-86.

50 Robert Sutter. “China's regional strategy and why it might not be good for the United States” in David Shambaugh, editor (2005). **Power shift. China and Asia's new dynamics**: 289-305. Berkeley: University of California Press.

51 Daniel Twining (2007): 88.

important additional cleavage in the Asian competition; however, not all of the United States' regional allies meet the criteria required to join an Asian alliance of democracies.

Between continuity and change, the new American strategy seeks to consolidate its position as the holder of the regional balance in Asia. However, the problem regarding the institutionalization of a regional security architecture remains unsolved⁵². For liberal internationalists, the growing importance of East Asia makes it necessary to set up regional security multilateral structures in order to integrate China and to include the United States. The possibility of transforming the Six-Party Talks into a permanent forum for multilateral concertation among main regional powers – United States, China, Japan, Russia and Korea⁵³ – is interesting. Likewise, is the possibility of replicating the Organisation for Security and Co-operation in Europe (OSCE) model in an Asian security institution that includes not only the United States, China, Japan, India, Russia and Korea but also the ASEAN states and Australia and New Zealand⁵⁴. However, political heterogeneity, nationalist ideologies, as well as the dynamics of emerging powers play against the reproduction of an European and western model of multilateral institutions in Asia.

In a sense, the old differentiation rule of United States strategies in the transatlantic relation and in the transpacific relation is still the rule.

52 Like Evan Medeiros, Robert Art defends the importance of multilateralism in East Asia and admits the possibility of the setting up of a sub-regional security institution in North-East Asia, including the main regional powers – United States, China, Russia, Japan – following the **Six-Party Talks**. See Evan Medeiros (2005): 206. Robert Art (2007): 38-39.

53 Francis Fukuyama, G. John Ikenberry. Executive Summary. Working Group on Grand Strategic Choices in G. John Ikenberry. Anne-Marie Slaughter, co-directors (2006): 63.

54 Robert Art (2007): 39.

The Indian Rediscovery of East Asia

Rui P. Pereira

Introduction

During most part of the 20th Century, especially during the Cold War period, the relationship between India and East Asia was far from significant, clearly suggesting that East Asia was not an Indian priority at the time. However, in the past years much has changed in the way the world views India and its relations with East Asia.

Key factors such as the new awareness of the emergence of India as a major power, world wide interest in the rise of Asia and its implications for the international system, the current dynamics in favour of Asian economic integration, and the unfolding debate on the construction of a new security architecture for the region, have made it very reasonable to discuss the evolving Indian role in East Asia.

Therefore, the present article attempts to undertake an analysis of the evolution of India's relations with East Asian countries under its 'Look East' policy, including such aspects as the current status of economic exchanges and the emerging security architecture in Asia. The article ends with some concluding remarks.

Brief Historical Background

India has a long tradition of trade and cultural exchanges with East Asia. Trade relations date back from the Silk Road and the period that Calicut emerged as a major trading port in South Asia. As to the cultural and religious bonds, they are historically linked to Emperor Asoka's spread of Buddhism beyond the Indian subcontinent, during the third century BCE.

The exchange of pilgrims, explorers and traders continued to develop until the 18th century, when India was under British rule. From that period onwards, India's contact with East Asia was subordinated to the rivalry of colonising powers, as Indian opium and soldiers were frequently used to gain markets and control rebellions in other parts of Asia.

During the 1940s and 1950s, India tried to reengage with East Asia, under the charismatic leadership of its first prime minister, Jawaharlal Nehru. The Asian Relations Conference, held in New Delhi, April 1947, was one of the earliest attempts to create a pan-Asian identity in the context of the modern nation-state. Together with such like-minded leaders as Indonesian President Sukarno and Chinese Premier Zhou Enlai, Nehru helped to forge the 'Bandung Spirit' of 1955, as it was known the precursor for the Non-Aligned Movement (Bajpae, 2007).

A principal objective was to revive India's millennia-long cultural, political and economic links with East Asia, which had atrophied under the weight of pernicious competition between colonising European powers. However, the supposed Asian solidarity never materialised, mainly as a result of the impact of the Cold War politics on the region, and, to a lesser extent, the tensions between India and China. Therefore, India's leadership of the Non-Aligned Movement and its opposition to US-led regional security architecture effectively closed the door to its East.

India's 'Look East' Policy

With the launch of the 'Look East' policy in 1992, together with the economic liberalisation programme, under the leadership of Prime Minister Rao, India finally began to reengage with East Asia. A distinctive aspect of previous engagements is the fact that operations took place on multiple fronts. Consequently, India's trade and cultural links were complemented with an in-

creasing economic interdependence and a more diverse bilateral and multilateral cooperation, including in the security area.

From this perspective, the Look East policy can be considered as a multi-faceted and multi-pronged approach to establishing strategic links with many individual countries, evolve closer political links, and developing strong economic bonds with the region. Secondly, it was an attempt to carve a place for India in the larger Asia-Pacific. Thirdly, the Look East policy was meant to showcase India's economic potential for trade and investment. Although both India and ASEAN refused to openly admit it, the rise of China also played an important role in the evolution of the Look East policy (Naidu, 2004: 337).

Former External Affairs Minister, Yashwant Sinha, in a speech delivered at Harvard University in 2003, noted the transformation in India's attitude toward East Asia: "In the past, India's engagement with much of Asia, including Southeast and East Asia, was built on an idealistic conception of Asian brotherhood, based on shared experiences of colonialism and of cultural ties. The rhythm of the region today is determined, however, as much by trade, investment and production as by history and culture. That is what motivates our decade-old 'Look East' policy. This region already accounts for 45 percent of our external trade" (Mohan, 2003).

Whereas phase one of the policy was characterised by the reinforcement of trade and investment linkages, phase two, according to Mr Sinha, is marked by "arrangements for Free Trade Agreements and establishing of institutional economic linkages between the countries of the region and India".

Other features of this second phase include a larger geographic scope of the initiative, from the initial focus on Southeast Asia to include East Asia and South Pacific and a much broader agenda namely, security cooperation, including joint operations to protect sea lanes and more concerted efforts in the war against terrorism.

As described by Raja Mojan (The Hindu, 2003), three other features stand as pertaining to the second phase of India's Look East policy. The first one relates to the development of a vast number of physical connections with Southeast Asia, especially air and land links. Secondly, and with greater consequences, for the first time since Indian Independence, the conditions were met to break out of the political confines of the subcontinent.¹ Finally, Indian leaders clearly expressed the idea that the 'Look East' policy, by any means, is directed

1 A good example of this is the creation of a new economic grouping, BIMSTEC, bringing five nations of the Subcontinent (Bangladesh, Bhutan, India, Nepal and Sri Lanka) together with two countries from Southeast Asia, Myanmar and Thailand, with a view to promote regional cooperation.

against China. On the contrary, the focus of bilateral relations should be the solution to pending bilateral issues on a pragmatic basis and the complete exploitation of new opportunities for economic cooperation.

Also, as a consequence of the Look East policy, India became involved in a growing number of East Asian forums on economic, political and security issues. In addition to being a sectoral dialogue partner with the Association of Southeast Asian Nations (ASEAN) as of 1992 and full dialogue partner in 1995, a member of the ASEAN Regional Forum in 1996, a summit level partner (on par with China, Japan and Korea) in 2002, and its accession to ASEAN's Treaty of Amity and Cooperation in 2003, India is also a member of the East Asia Summit process.²

India is also involved in several track-two (non-governmental) dialogues as well, such as the Council for Security Cooperation in the Asia Pacific, as well as in numerous sub-regional forums including the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation, the Ganga-Mekong Cooperation Project and the Kunming Initiative in the Indochina region.

Economic Relations and Energy Security

Further to an impressive record of GDP growth in the last two decades, with an average of around 6% (or 8%, if only the last four years are considered), India is already the third-largest Asian economy, after Japan and China and it is projected to be the fourth in the world in 2050.

In the past years, the Indian government has become more engaged in the negotiation of Economic Partnership Agreements, namely with Southeast Asian countries such as Singapore and Thailand (a Comprehensive Economic Cooperation Agreement and an Early Harvest Scheme, respectively, were recently signed). Other negotiations of similar agreements include Japan and South Korea, which will be concluded by the end of 2009.

India's trade with ASEAN has grown phenomenally in the last few years, increasing from \$9.7 billion in 2002 to about \$30 billion in 2007. At the sixth India-ASEAN Summit in Singapore, November 2007, India proposed

2 In many cases, India's membership to these forums has been the result of the region's attempts to balance China's growing influence in the area. Notably, Japan brought India into ASEAN+6 to dilute the ASEAN+3 process, where China is dominant, while Singapore and Indonesia played a significant role in bringing India into the East Asia Summit.

to enhance bilateral trade with ASEAN countries to a target of \$50 billion by 2010.

Negotiations to create a Free Trade Area (FTA), under the Framework Agreement on Comprehensive Economic Cooperation of October 2003³ are still ongoing. Although more than 16 meetings of the ASEAN-India Trade Negotiation Committee have already been held, both sides failed to reach an agreement by the estimated date of January 2007, which is now foreseen to be completed until March 2008.⁴ If that is confirmed, the FTA should be implemented as of January 2009.

An India-ASEAN FTA will be a market of 1.5 billion people and a combined present GDP of \$1.8 trillion, covering trade in goods, services and investment. However, to increase the trade potential further, such areas as science and technology, information technology, biotechnology, tourism, and human resources development may have been incorporated in the agreement.

India, as part of the East Asia Summit process, is also involved in the study group in charge of undertaking a feasibility study on a future Comprehensive Economic Partnership Agreement (CEPA) involving the 16 members,⁵ to be completed by mid 2008. India sees it as the building block for the East Asian Community as envisaged by many, including Prime Minister Manmohan Singh.

Indian trade with China is currently booming (close to \$30 billion in 2007) and is expected to cross \$60 billion by 2010. However, while China has emerged as India's second-largest trading partner, India is only China's tenth-largest trading partner. Additionally, Chinese investment in India has lagged recently, as India's national security establishment has opposed Chinese investment in strategically important Indian sectors such as ports and telecommunications.

India's trade with Japan is less significant, about \$10 billion in 2007, but both countries decided to enhance it to \$20 billion by 2010. Japanese investment in India was approximately \$2 billion in 2006, far less than the \$57 billion that Japan invested in China.

However, some important Japanese investments in India are underway, most notably in New Delhi's metro subway system and Maruti. The Japanese

3 The text and annexes of the Agreement can be consulted at: <http://www.aseansec.org/15278.htm>

4 Two main issues have come in the way: India's sensitive products list and the typology of rules of origin. Under the FTA, tariffs would be brought down on 73 per cent of tradable items. Tariff cuts should be completed until July 2018.

5 It comprises the 10 ASEAN countries, China, Japan, Korea, India, Australia and New Zealand.

government and corporate sector will also provide one-third of the funding for the \$100 billion, 1,500 kilometre Delhi-Mumbai freight and industrial corridor, which is to begin construction in 2008 and should be completed by 2012.

Insofar as energy is concerned, India imports more than 70 percent of its oil consumption and half of its gas consumption. Its energy dilemmas are shared by many states in the region, as Asia accounts for a quarter of the world's energy consumption, meets 41 percent of its energy needs from burning coal and holds 3.5 percent of the world's proven oil reserves, while having the world's second-, third-, fifth- and sixth-largest oil importers, namely Japan, China, South Korea and India.

These shared concerns demand a joint, multilateral approach. India, like other major energy consuming countries in Asia, would better cooperate on addressing shared concerns to their energy security, such as developing regional strategic petroleum reserves, collective bargaining to address the Asian premium on imported oil, encouraging joint development of disputed energy-rich territories, and improving energy conservation and efficiency (Bajpae, 2007).

In 2004, India took the first step in promoting regional energy cooperation by convening the First Roundtable of Asian Ministers on Regional Cooperation in the Oil and Gas Economy in New Delhi, which brought together the four principal Asian oil-consuming countries - China, Japan, South Korea and India - and engaging in a dialogue with major oil-producing countries in the Middle East and Southeast Asia.

A controversial side of India's Look East policy has been New Delhi's pragmatic engagement with Myanmar since 1993, moving from its previous opposition to the military junta's rule, mainly fuelled by the desire to gain access to Myanmar's energy resources, as well as balancing China's influence in the region and obtaining Yangon's support in countering insurgent groups in India's Northeast.

However, it is not apparent that India has made any significant gains so far. For instance, while Indian energy companies Oil & Natural Gas Company Videsh Ltd. and Gas Authority of India Ltd have a 30 percent stake in Myanmar's A1 and A3 blocks in the Shwe field in the Bay of Bengal, a proposed natural gas pipeline to India has been threatened by an agreement between Myanmar's military junta and PetroChina to supply China with 6.5 trillion cubic feet (TcF) of natural gas via a pipeline from the A1 block to Kunming in China's Yunnan province.

The Emerging Security Architecture in East Asia

India has also stepped up engagement with East Asia on the security front, fuelled by its need for cooperation on counter-terrorism, humanitarian relief, anti-piracy, maritime and energy security, confidence-building, and balancing the influence of other powers, notably China. Driven by the fact that more than 50 percent of India's trade passes through the Malacca Straits, the Indian Navy has established a Far Eastern Naval Command (FENC) off Port Blair on the Andaman Islands.

If security initiatives were conspicuous by their absence in the first phase of India's Look East policy, they have begun to acquire a new importance in the second phase that began halfway through this decade. Although India initiated a range of bilateral and multilateral military exercises with global and regional players from the early 1990s, it was the conclusion of a bilateral defence cooperation agreement with Singapore in 2004 that launched vigorous security diplomacy in the region (Mohan, 2007).

Other bilateral security cooperation agreements across the region followed. During the last few years, India has signed defence cooperation agreements with a number of Southeast Asian countries, including Indonesia, Vietnam and Cambodia, involving Indian assistance in military training and arms transfers, among other objectives.

Therefore, it was not surprising that, at the end of 2004, Indian Navy was quick to respond on its own to the tsunami disaster and later joined the navies of the US, Japan and Australia (Regional Core Group) to provide relief in Southeast Asia. In 2005, the Indian Aircraft carrier, *INS Viraat*, arrived for the first time in the ports of Southeast Asia - Singapore, Jakarta in Indonesia and Klang in Malaysia.

More recently, in the Spring/Summer of 2007, the Indian Navy sailed all the way up to Vladivostok and conducted a series of bilateral and multilateral exercises with a number of nations that included major powers like the US, Japan, Russia and China, as well as regional actors like Singapore, Vietnam and the Philippines.

India's military diplomacy in 2007 culminated in large scale naval exercises with the US, Japan, Australia and Singapore in the Bay of Bengal. While these exercises might have raised alarm about a potential "Asian NATO", especially among Chinese strategists, India appears to be clearly focused on expanding its own regional profile, rather than creating a new alliance. A good

example of this is the Indian Navy's first time initiative to convene an Indian Ocean Naval conclave in February 2008.

Not least important is the fact that, India has been conducting joint military exercises with China in recent years as an attempt to build mutual confidence. Apart from the first joint counter-terrorism training in November 2007, the two Asian giants have also held joint naval exercises in the East China Sea and in the Indian Ocean (November 2003 and December 2005, respectively).

Is there a grand strategy behind the frenetic pace of India's military diplomacy? According to Mohan, India argues it has no desire to align with any one power against another and that its interest lies in contributing to a stable balance of power in a "multipolar Asia".

India's Relations with Great Powers⁶

Since the end of the Cold War, India has enjoyed an unprecedented and simultaneous deepening of its relations with all the great powers. India's bilateral relations with China, the US and Japan are today in their most prosperous period since the 1950s. India has proclaimed "Strategic Partnerships" of varying intensity with all the three powers.

Yet, as expressed by Mohan (2008), the fact remains that none of India's three great power relationships has arrived at a plateau. All three remain susceptible to significant swings – up or down. Changes in one relationship are bound to affect the other two.

China

The ties between India and China are extraordinarily complex and sometimes misunderstood, but the future direction of Sino-Indian relations will be a key element of the incipient balance of power in Asia. For India, the resurgence of China in the middle of the last century and its emergence as a neighbour was a geopolitical development of great importance. As the two nations re-emerged on the world stage after a long period of relative decline, India and China did not find it easy to build good neighbourly relations.

6 Relations between India and Russia will not be considered in this article.

Even as they proclaimed high principles of friendship, the two giants drifted towards inevitable conflict. Distrust over Tibet resulted in India concluding bilateral security treaties with Nepal, Bhutan and Sikkim during 1949-50. As India drew closer to Soviet Union amidst the Sino-Soviet conflict, China was wary of Indian policies that appeared to focus on balancing China. New Delhi, in turn, was concerned about what it considered to be hostile policies of China, especially its support to Pakistan in its quarrels with India and the strengthening of Islamabad's strategic capabilities, including its nuclear and missile programmes.

This behaviour of mutual balancing has been partly mitigated in recent years, as India and China have worked hard to construct a more cooperative relationship. After a tentative rapprochement that began at the end of the Cold War, India and China have successfully deepened and broadened their relationship. The two countries are embarked on a dialogue to resolve their differences over Sikkim's integration into India, and engaged in an intensive political exercise to find a fair and reasonable solution to their difficult boundary dispute. Meanwhile, the interaction between the two societies is rapidly expanding.

These positive trends, however, do not necessarily imply that the sources of competition between the two countries have dried up.

The East Asia Summit (EAS) process is a good example. As a sign that India's participation in the EAS would not be welcome, in early 2005 Beijing was diplomatically active in dissuading nations in the region from lobbying for India's membership; this received no support from any country except for Malaysia, which was interpreted as reflecting in general the keenness of regional power to balance China's growing profile in the region (Rajan, 2008).

Also on the desirable security order in East Asia, the formulae of India and China are at variance. New Delhi's prescription for a 'polycentric' security concept for East Asia would imply India's opposition to any one country dominating the regional security architecture when set up. Beijing, on the other hand, talks about a "regional security environment of mutual trust guaranteeing stability by bridging differences through dialogue on an equal footing" (Rajan, 2008).

At the same time, according to some Chinese academics, India's role in building up the Asia security architecture may not be very clear. First of all, India's self-perception of its position in the region may not be shared by other major powers, which might still see India as an Indian Ocean power rather than an Asia-Pacific power. Secondly, India's increasing influence in the Asia-Pacific is mainly demonstrated through bilateral developments such as India-US stra-

tegic partnership, India-Japan cooperation, India-Singapore exchanges, etc. In some important multilateral mechanisms, like the Six-Party Talks, India is not included. Thirdly, whether the Asia security architecture in the future should be built on a pan-Asia assumption remains debatable. Finally, there is little doubt that India wants to enter the Asia-Pacific and play its role as significantly as possible, but the issue is how. Currently, India has militarily maintained its moderate presence in the West Pacific, joining relevant exercises in anti-terror and anti-piracy operations, mostly focusing on non-traditional areas, which is important, but in more crucial areas such as the Korean Peninsula, Taiwan Straits, and South China Sea, whether India has both intention and capacity to take a part remains to be seen (Gancheng, 2006).

Moreover, as both nations acquire greater economic and political clout, there is also a sense of competition between them across a broad front, from the maritime domain to outer space. From Latin America to Siberia, and from Southern Africa to Central Asia, China and India are locked in a global competition to ensure resource security. Citing the protection of their sea lanes of communication, China and India are determined to expand naval power and ensure maritime presence far away from their shores.

This does not mean that India's relations with China will inevitably become adversarial. Rather, the Sino-Indian relationship is likely to see enduring elements of both rivalry and cooperation, and the challenge before Beijing and New Delhi is to continuously expand their relations and develop a better mutual understanding and prevent any potential misreading of each other's intentions.

United States

While Sino-Indian relations are being managed between security dilemma and cooperative security, Indo-US relations are moving from the prolonged estrangement during the Cold War to a conscious effort to build a strategic partnership.

Over the last seven years, the Bush Administration has made a sustained effort to change the very fundamentals of the relationship with India. On a traditional bone of contention, nuclear non-proliferation, the Bush Administration has made a big move to accommodate India into the global nuclear order. It has changed its own domestic non-proliferation laws to facilitate renewed

civilian power cooperation with India and is working with the international community to change the global rules on nuclear commerce with India.

As a nuclear-arms power since 1988, India has been impeded from engaging in civilian nuclear cooperation by the United States and other countries, following its refusal to sign the Nuclear Non-Proliferation Treaty (NPT). However, the US has decided to change its India nuclear policy recently. According to *The Economist* (August 2007), “it would supply India with civilian nuclear fuel and technology provided it submits to safeguards on its civilian nuclear programme and separates it from its military one”.

Therefore, based on the nuclear cooperation agreement signed in July 2005, the US recognises India as a nuclear power and provides for some measure of international regulation of its nuclear capabilities and resources and also for US civilian-nuclear exports to India. This accord’s geopolitical importance lies on the fact that it represents America’s open acceptance and acknowledgment of India’s rising capabilities, ambitions to be a great power in Asia, and the consequences thereof (Blank, 2007: 1).

The proposed agreement envisaged the separation of India’s military and civilian nuclear programmes and the placing of the latter under international safeguards. India would gain indirect recognition of its status as a nuclear power and access to nuclear materials and technology hitherto denied it. In return, the non-proliferation regime would expand the scope of its controls over the Indian nuclear establishment and obtain India’s full cooperation in stemming the global spread of nuclear weapons (Basrur, 2007).

Notwithstanding, opposition to the deal is strong, both in the US and India. In the US, there is widespread concern that it will be a fatal blow to the non-proliferation regime, which revolves around the Treaty on the Non-Proliferation of Nuclear Weapons. In India, the collective memory of colonial subjugation drives resistance to the test option, viewed as vital to national security as it is foreclosed by a stronger power.⁷

In the meantime, as the US-India agreement moves from a bilateral issue to a multilateral one, with necessary endorsement from the International Atomic Energy Agency, India will need to obtain approval from a large number of countries, including relevant Asian players.⁸

7 Consequently, it is not totally surprising that the agreement hasn’t entered into force yet, due to the opposition from the Communist Party of India. The Congress-led government of Manmohan Singh needs their parliamentary support to pass legislation.

8 The recent willingness by Australia to sell uranium to India is significant, given that Australia holds 40 percent of the world’s uranium reserves. The quiet acquiescence by Japan to the US-India nuclear agreement is also a milestone, given Japan’s staunch opposition to nuclear proliferation. China, while initially

The political motives behind the Indo-US deal appear to be far more important. While maintaining good relations with China, both countries are hedging against possible threats from the emerging superpower. The US wants rising India on its side and is pushing for a coalition of democratic powers – with Japan, India and Australia – in Asia. This coincides well with India's own desire to stave off a potential challenge from China and with its quest for admittance to the big league. The emerging coalition would, both, not only make China more inclined toward cooperation, but perform the more general function of maintaining stability in the region vis-à-vis diverse threats such as failing states and terrorists (Basrur, 2007).

Underlying this unique American readiness to spend political capital on India is the recognition that New Delhi is bound to emerge as the crucial swing state in future global balance of power. The Bush Administration has publicly declared its commitment to assist India's rise as a great power,⁹ and has offered it a full range of military cooperation from advanced conventional weapons to missile defence.

Symptomatically, the US commitment to help India emerge as a world power by assisting India's military modernization, as evidenced by the signing of the "New Framework for the US-India Defence Relationship" in 2005 and the "Next Steps in Strategic Partnership" in 2001, has prompted US allies in Asia to step up military-to-military engagements with India.¹⁰

The deal on resuming civilian nuclear cooperation and the growing military relationship between New Delhi and Washington have raised some important questions. How far is India willing to go in partnering the United States? Is India in fact ready for an alliance like relationship with Washington? The record of India's foreign policy and its reluctance to accept the dictates of other great powers suggest that India will never sacrifice its freedom of foreign policy action in favour of a tight alliance with the US that might constrain its options (Mohan, 2008).

expressing discomfort about the U.S.-India civil nuclear agreement by labelling it as creating a "nuclear exception" and undermining the non-proliferation regime, has recently toned down its opposition to the deal by calling for "innovative and forward-looking approaches to civilian nuclear cooperation."

9 In March 2005, Secretary of State Condoleezza Rice stated that it was US policy "to help make India become a major world power in the twenty-first century".

10 For instance, in March 2006 Australian Prime Minister John Howard signed a memorandum on defence cooperation with India. In April 2007, Australia and Japan, along with the United States, held a trilateral naval exercise off the Boso Peninsula in central Japan, and the "Malabar-07" US-India joint naval exercises in the Indian Ocean in September included the navies of Japan, Australia and Singapore as well.

From Mohan's view (2008), India's interlocutors will then have to keep two broad propositions in mind, when assessing New Delhi's future relationship with the United States and China. Firstly, India's main objective is to emerge as an indispensable element in Asian balance of power. Secondly, India's emphasis will be on the simultaneous expansion of political and economic relations with all the great powers and avoid choosing sides between them.

Japan

An intensified relationship with Japan fits naturally into the broad framework that India has set for itself.

Japan has been the last among the great powers of the world to sense India's rising power potential. But during the final years of the premiership of Junichiro Koizumi and the brief tenure of Shinzo Abe, Japan has moved rapidly to define a new approach to India.

Further to Prime Minister Singh's visit to Japan in December 2006, the "Joint Statement Toward Japan-India Strategic and Global Partnership"¹¹ was signed, and India is the only country with which Japan will have annual prime ministerial level talks.

Also, Japan has sought closer relations with India in the context of its "value-oriented diplomacy." In his speech before a joint session of India's parliament in August 2007, Shinzo Abe described India as part of a "broader Asia" that spans "the entirety of the Pacific Ocean, incorporating the US and Australia." Abe noted that these states comprise an "arc of freedom of prosperity" of "like-minded countries" that "share fundamental values such as freedom, democracy and respect for basic human rights, as well as strategic interests."¹²

As a result, the idea emerged that the 'four major Asia Pacific democracies' - US, Japan, India and Australia - should step up their cooperation in regional security. However, as stated by Mohan (2007), "none of the four countries is ready for anything more than a low-key consultative mechanism, even the US. The four nations, including India, have an expansive relationship with China and no wish to invent a new Cold War in Asia."

Although India's improved relationship with the US and the fluidity in Sino-Japanese relationship has cleared the ground for an improved Indo-

11 Full text is available at: <http://www.kantei.go.jp/foreign/abespeech/2006/12/15joint.pdf>

12 The full text of Abe's speech is accessible at: <http://www.mofa.go.jp/region/asia-paci/pmv0708/speech-2.html>

Japanese relationship, there are other factors driving the bilateral strategic partnership. For instance, the likely change in Japan's policy on sensitive exports to India can open the door for a very rewarding high technology partnership between Tokyo and New Delhi, and both countries have also agreed to expand their current defence cooperation which is currently focused on securing the sea-lanes in the Indian Ocean.

Traditionally, India was not part of Japan's conception of Asia. In expanding its geographic definition of Asia to beyond Myanmar in the West, and drawing India into a strategic partnership, Japan believes it has a better chance of coping with the unfolding redistribution of power in Asia and establishing a stable balance of power in the region. India, in turn, sees huge strategic complementarities with Japan.

Concluding Remarks

Although India's engagement with East Asia is not a recent phenomenon, the current drivers of the relationship, under the 'Look East' policy, far exceed the previous trade and cultural exchanges, being clearly focused on economic interdependence and common security concerns.

Consequently, India's foreign policy appears to be finally moving beyond the confines of South Asia toward East Asia, and is now closely linked to such key players as China, Japan and the United States.

However, that doesn't necessarily mean that India will aspire to a leadership position in Asia in some years' time. Rather, India will most probably maintain a low profile in its foreign policy and favour the emergence of a "multipolar" Asia, cognisant with the extraordinary political diversity of the continent.

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Part III. Discord and Cooperation

New Trends in the Taiwan Strait Conflict: the Cooperative and Quarrelsome Framework

Jorge Tavares da Silva

*“Taiwan problem should be resolved while the older generation
of cadres is still around”*

Jiang Zemin (2000)

The Taiwan Strait witnesses one of the world’s most intricate contemporary political anomalies and plausible scenario for a military confrontation between the People’s Republic of China (henceforth: PRC or China), Republic of China (henceforth: ROC or Taiwan) and the United States (US). The conflict represents both an old reminiscence of Chinese civil war that shattered the Middle Kingdom in the first half of the 20th century, and the last episode of a world divided by two hegemonic superpowers. According to Professor William Zartman (2005), the parties of this claim “revived an animal thought to have been made extinct by the melting of the Great Ice Age that constituted the Cold War – a Balance of Terror”. On the one hand, great China, a country that lives under a hybrid political system, in no way resigns to the idea of recovering the “renegade province” and doesn’t accept any kind of independence. On the other, there is a democratic and modern island that resists the incorporation

of its founding country. This issue, however, should not only be seen from a confrontational point of view but also by cooperation opportunities that are bringing forth new tendencies. This chapter explores both these perspectives, comparing these with the last political, social and economic developments in order to understand current negotiations and trends and to provide suggestions for the region's future.

Taiwan, also known as Formosa by ancient Portuguese sailors, is situated only 160 kilometres from PRC and has been a refuge to nationalist faction since 1949. At that time, Mao Zedong forces defeated Chiang Kai-shek and more than a million desperate Guomindang (GMD) followers fled to the far and safe island of Taiwan. Chiang set up a government-in-exile and, in spite of its feeble position, promised to get back mainland as soon as possible to maintain the sovereign claim for all China. As the military was unable to invade Formosa, communists asked Moscow for help, however, when they seemed prepared for an offensive, the US showed up and put them on the ranks. In fact, the US had supported GMD before, but the corruption and inefficiency of Chiang's regime excluded American troops from the war even though Stalin supported Mao's soldiers. Soon the US would enter the red scared era of McCarthy (1950-1954) which is characterized by the pursuit and removal from public employment of all those believed to be communist sympathizers, in other words, a *witch hunt* against *red evils*. So, in a very ostensive international policy, the US systematically segregated mainland China and its more than 800 million people from being represented in the United Nations (UN). China's seat in the UN was occupied by the small island of Taiwan with its only 14 million people (Huerta and Tamames, 2000: 509). China abandoned its intention of invading the island but has never given up getting its possession and always refers to it as its 23rd province. Within a short period of time, the US determined the external and internal political framework of ROC and the Nationalist émigré regime was basically an expression of the American economic and strategic desires although the one party system rule remained (From the Chinese point of view, the small territory has been a "hard nut to crack" and with ups and downs, the situation was the same until the beginning of 1970's (Yun-han e Jih-wen Lin, 2001: 102).

By means of a magic diplomatic trick and some "ping pong" plays, it did not take long for circumstances to radically change. In July 1971, after some of Henry Kissinger's flights to Beijing, the world was surprised by the rapprochement between the "communist" China and the "imperialist" US. Richard Nixon, supported by his right hand man, Henry Kissinger who made

use of Sino-Russian schism and blinked an eye to Beijing in an amazing *triangle diplomacy*. The following year, President Nixon visited China and signed the “Joint Shanghai Communiqué” (February 28), on “the week that changed the world” as it was referred to at that time (Kissinger, 1994: 613-639). In a split second, the Formosa Island was suddenly removed from the UN (resolution 2758) as if it didn’t matter anymore. The Communiqué had intended to provide a fundamental structure regarding the Cross-Strait issue, to normalize the relations between Washington, Beijing and to pave the peace on the Strait. However, it maintained the ambiguous and wily language that has led some analysts to consider it a “diplomatic lie”. Clearly, the document only took note of the differing positions of the US and mainland China and failed to clarify the ROC status. When it states that “there is only one China”, it doesn’t specify which China is mentioned as each part has different points of views on the same political principle. The American tactic towards Formosa is known as the “strategy of ambiguity”, a smart and intentional policy in a state of ambivalence, using ambiguous and unclear statements, while supporting both sides of the same problem. This “lexical” strategy is named as an “outmoded relic” by T. Y. Wang (1996), frequently causing misunderstandings and risk. Other observers prefer referring to it as good – probably the best- opportunity for the US to sell weapons to the island and achieve diplomatic advances with China, weakening the Soviet Union position. In 1979, the US Congress passed Taiwan Relations Act after having officially made sure that “Taiwan with arms of a defensive character”, in order “to maintain the capacity of the United States to resist any resort to force or other forms of coercion that would jeopardize the security, or the social or economic system, of the people on Taiwan”. The Act was not recognized by Beijing which viewed it as “an unwarranted intrusion by the US into the internal affairs of China”, but even though it did not apply to Taiwanese small islands of Matsu and Quemoy, it was a special opportunity for achieving peace in that region (Lampton, 1999).

Taiwan and Chinese coast



Source: <http://www.andrew.cmu.edu/user/dcwang/aboutme.html>

The truth is that Taiwan remained in international political isolation for decades while quietly watching mainland China point heavy military weaponry towards insular territory. Taipei started a desperate international strategy for seducing new supporters while many countries removed embassies from there to settle in Beijing. This was one of the biggest diplomatic migrations from one country to another in contemporary history incited by the simple drawing of political desires of a great power. Meanwhile, Deng Xiaoping put out the red carpet to Taipei proposing reunification under the scheme, “one country,

two systems” (一国两制 *yi guo liang zhi*). The Taiwanese government refused the proposal but trade exchanges that were technically illegal in the Strait, increased drastically while some informal contacts between them also started. Soon, both sides would witness one of the world’s most intense trade zones despite Taiwan’s refusal of direct transport and post links. Some political barriers were removed and thousands of Taiwanese tourists and investments went to PRC. In a few years, Taiwan created a firm economic system turn-up to international trade, based on low cost production and became one of the New Industrialized Countries (NIC), also known as one of the four “Asian Tigers”. The “tiger” grew up side by side with the great sleepy “dragon”, which has opened an eye to its “renegade province” while learning the advantages of capitalism.

Unfortunately, economic proeminence was not followed by the same political and diplomatic performance and Taiwan’s status remained within a very intricate sovereignty conundrum. Without any doubt, realistic thinkers put China and Taiwan under a real possibility of military involvement promoted by power confrontation and sovereignty claim., On the other hand and in a more optimistic perspective, liberals accept as true that economic cooperation based on a gradual interdependence in the Strait, puts aside the creed in violence and could evolve to a consequent solution for the problem. In fact, both believe in a solution for the same problem, what is different is the way they look at that solution. In other words, we can say these two ranks mean no more that the revival of two classical ideological confrontations: war and commerce. States use (or used) the war as a way of obtaining territorial sovereignty and as a guarantee of minimum independence, self-sufficiency and a unilateral hegemonic position on a certain piece of land. Within this scope and in the old Hobbesian tradition of ignoring economic interdependence between people, the states are like snooker balls that hit one another while searching for balanced power. The *leviathan* state tries serving itself by the damage caused on others. The commerce, consubstantiated by the idea of multilateral trading and cooperative framework, could serve several countries at same time in a symbiotic relationship (Ferreira et al., 1997: 15-18). The Swiss economist Henri-Benjamin Constant (1767-1830) was one of the authors who widely studied the relation between commerce and war, simultaneously demonstrating a clear preference for strongly trading societies and refusal towards military ones. According to the author, war is prior to trade; trade and war are two ways of reaching the same objective and obtaining what is desired. However, for Constant, “war is all impulse, commerce, calculation” (1816). This is the seed of the next *laissez-faire*, the *laissez passer* era and the seed of Adam Smith’s formulations that has inspired contemporary

neoliberals like Michael Doyle. But there are other authors who defend that the trading system is not enough to create peace relationships. We are talking about Samuel P. Huntington (2001: 255) for instance, who believes that the trading system only brings people together and doesn't necessarily force them into an agreement. He is highly suspicious of the Asian economic euphoria as a guarantee for peace and harmony between nations.

Like Huntington, many other international relations experts have serious doubts when trying to explore the deepest elements of liberal peace. But while arguments have been expressed, Cross-Strait ambience has been involved in new factors that could put tendency in scales. The claim could be divided into two important branches [cooperation and confrontation], reinforcing both arguments and giving us a well known perspective of this issue. It's important to know what exactly these new traces are, to identify new political and economic adds and to understand what is really being altered in each framework in order to identify the new trends of this conflict.

The quarrelsome framework

John J. Mearsheimer (2005) is one of the observers who most strongly believes in a military confrontation in the Taiwan Strait. He is a defender of "offensive realism", which defends that states seek hegemony by means of security. Mearsheimer defends that the US and PRC are "likely to engage in an intense security competition with considerable potential for war". At the same time, the author accepts as true that most of China's neighbours, including Russia, India and Japan, could be involved in the contention (Brzezinski and Mearsheimer, 2005). The augur will not bring good memories if we recall the words of Thucydides in the Peloponnesian War, when he says that the belief in conflict could inevitability be the first and main reason for a real military confrontation (Nye, 2002: 20-21). The pieces of the game are on the table: China continues to claim sovereignty over the quasi-independent island, to reiterate the principle of "one China" (一个中国 *yige zhongguo*), advocating that the Chinese Communist Party (CCP) is the only legitimate government and has admitted to "employ non-peaceful means and other necessary measures to protect China's sovereignty and territorial integrity", as can be read in article 8 Anti-Secession Law (反分裂国家法 *fan fenlie guojia fa*). The law reinforces the existing principles of just one China; reunification as a national matter and warns against the use of military forces. But at same time, it reinforces the

intensification of cooperation and a possibility of a political solution by means of the model “one country, two systems”, the same used in the Macao and Hong Kong transition process. The truth is that the conflict was eminent for several times while at others, it was appeased partly due to US involvement which provoked a political equilibrium that endured for years. Between 1949 and the early 1970s trade and tourist trips were interdicted for both sides and political high individualities looked at each other in suspicion. In 1958, Beijing tried to get military nuclear support in Moscow to develop an attack against the GMD enclave but Eisenhower proposed to put nuclear weapons on the island despite its non-execution. Fortunately, these two episodes (which were clearly a part of the Cold War) did not lead the conflict to a higher instance.

At same time, many international reports coming from the US, turned world attention towards China’s new military power. In 2005, a 45-page Pentagon report to Congress emphasized China’s brisk modernization as a very sharp point to the island of Taiwan. In the same year, a Rand report referred to Chinese military outlays as being likely to rise to \$185 billion by 2025, “a little over 60 percent of the United States 2003 defence budget” (Crane et al., 1995: 246). But the question was particularly dreadful when Hu Jintao told George W. Bush in September (2007), during the last Asia-Pacific Economic Cooperation (APEC) summit, that the next two years would be “a highly dangerous period” for the Taiwan Strait. In fact, People’s Liberation Army (PLA) simulates the invasion of the “renegade province” on large-scale military stirrings on a regular basis and currently keeps about 1000 missiles targeted at the island, with 32 conventional and nuclear-powered submarines monitoring the coast. Taiwanese authorities fear that in 2010 the number of military projectiles and guided missiles deployed by China will surpass 1,800 and the number of submarines could reach 50 in 2015. The latest CCP National Congress (October 2007) confirmed the endorsement of new central leadership with younger officers that many analysts consider a strong political message for ROC. In fact, at least five new members of Central Military Commission (CMC) have Taiwan affairs in their recent *curriculum* topics. Wu Shengli used to be the chief of staff and commander of a navy base in Fujian, the neighbour Chinese province of Taiwan; Chen Bingde and Liang Guaglie worked Military Area Command in Nanjing in the 1990s. Li Jinai and Jing Zhiyuan are experts in missile deployment (Fong, 2007). Is China indirectly adverting Formosa or is it gradually preparing military line-ups for a future confrontation?

In fact, China never had great empathy towards Taiwanese president, Chen Shui-bian, the island first native-born and the first GMD party opposi-

tion after 55 years of power. The Democratic Progressive Party (DPP) leader was a man with strong attitude and charisma who was known for delivering populist speeches in spite of being involved in corruption scandals. It was the inveterate pro-independence stance -Taiwanese separate identity and state-to-state relationship that provoked Sino-American concerns. Beijing reiterated its suspicions, accused him of constitutional changes that would ruin dialogue and wishes for an eventual reunification. Two of Chen's challenges were the so-called island's entry into the UN under the name of "Taiwan" and the referendum for UN membership. As People's Daily referred (September 21, 2007), it "represents the biggest audacious political gambling for himself and also DPP ever since its establishment over two decades ago". China labelled him as a "troublemaker" and "saboteur" of peace and stability and has accused him of trying a desperate strategy in order to make Ma Ying-jeou, the GMD candidate lose the elections in March 2008. The idea was that DPP would win the elections and Chen would maintain his influence on the party, far from the judicial *de jure*. In fact, 2008 promised to be a very decisive year for the issue but, at same time, very risky for the maintenance of peace. The Taiwanese government predicted that among the 8 million voters that will deposit their ballots in the 2008 referendum, 90 percent will be in favour of the UN bid under the name "Taiwan". Some military sources referred that Taiwan could install missiles in Quemoy and Matsu islands aiming at Shanghai and Fujian. It could draw both parties to a military confrontation, jeopardising China's diplomatic image and risking business agreements in a zero-zero sum. In fact, GMD has a more collaborative posture with Beijing in spite of also having defended the referendum proposal. We can say that while DPP used political strategies to get followers in the upcoming legislative and presidential elections, GMD tried to adapt the populist opposition in order to win some votes. Both parties' proposals were very similar, with the exception that GMD did not specify the name with which the island should enter the UN, while DPP wanted to use the name of "Taiwan". At this time, Peking feared that Chen could the Olympic Games to declare the independence of the island but the political outcome of the event turned out very favourably. The threat ended up coming from Tibet where the presence of China was greatly manifested against. The recent legislative and presidential elections confirmed the defeat of DPP with much lower results than expected while economic cooperation is expected to overlap military confrontation. Additionally, voter's fatigue towards the Taiwan referendum, with only about 35% of votes, is insufficient for its validation and

international recognition which means that its status quo in the region will remain unchanged.

China is still trying to squeeze Formosa into the international community and into a political “apartheid” that has lasted for almost forty years in a cat and mouse chase. While Taipei seduces foreign partners, Beijing puts pressure on international organizations for the island to remain isolated. Taipei allies are essentially located in Latin America but there are also some in Africa and Asia Pacific islands. It has used a diplomatic offensive and financial support in order to promote modernization by using new technology industries and getting international hold of its position. Many of those allies have been voiced in the UN and have put some pressure on discussing ROC’s international recognition. Beijing has reiterated that Taiwan doesn’t exist as a country because it is simply a province of China. In 2005, for instance, during the annual World Health Organization (WHO) meeting in Geneva, China signed a secret document weakening the Taiwanese position in that organization by forcing it to first submit the matters to the Chinese Ministry of Health. At the same time, a letter was refused by a careless Secretary-General Ban Ki-moon who referred to Taiwan as a “part of the People’s Republic of China”. China quickly planned to pressure the UN into confirming Beijing’s claim but Ban changed the speech after the US corrected his statement. However, China’s boycott on Formosa’s entrance into the international organization was confronted with a very passive response from Washington’s. This attitude is not in accordance with the Taiwan Relations Act, approved by Congress (Public Law 106-113) in 1979, which only foresees peaceful measures to determine the future of Taiwan, “including boycotts or embargos”. The refusal of Taiwan’s proposal into the WHO and the General Assembly discussion are by no means peaceful.

The cooperative framework

Although economic ties across the Taiwan Strait have been frequently considered secondary in relation to political and geostrategic factors, they have gained gradual importance in relation to the future of this unfortunate region. More than ever before, Chinese and Taiwanese decision-makers in political hierarchies are dominated by commercial impulses that profoundly change the trends of the Cross-Strait ambience. Trade, investments and other business ties have linked the US, China and Taiwan into mutually dependent relationships so that none of them would dare to create policies that would risk war (Cop-

per, 2006: p. 219). In 1978, the reforms and openness policies (改革开放 *gaige kairfang*), headed by Deng Xiaoping, involved China in an overflowing and even unprecedented economic programme that soon brought forth good results. According to Jeffrey Sachs, the Chinese economic *renaissance* is the most beautiful and well succeeded development process that the world has ever seen (Sachs cited in Izraelewicz, 2005: 13). Never before has millenarian Chinese history witnessed so many changes in so little time. This is the opportunity for this huge country to draw the curtain over the past and show the world that it is no longer the feeble land that Western powers used to play with. Deng started economic reforms when China was one of the poorest countries in the world. Little did he know that in less than 20 years it would become the fourth economic world power and one of the most promising in the emerging countries. In less than thirty years, China increased production ten times, GDP seven, exports 45 and took 400 millions of people out of deep poverty. With about 20% of the world population, this country went from an autocratic and agriculture-based system to the highest industrialized system that produces great proportions of just about everything for anywhere in the world, in such a way that many people call it the “factory of the world”. China produces 70 percent of toys, bicycles, DVD recorders, 60 percent of digital cameras, 50 percent of portable PC’s, 29% of mobile phones and more than half of the world’s textiles and shoes (Izraelewicz, 2005: 19). The old, mysterious, strange and threatening China has shown the world that it has changed. Beijing has opened its doors to capital and has also allowed the world to have a look inside China. China has expressed its good intentions towards foreign countries including Taiwan Island.

This economic explosion has strongly influenced Strait relations, influencing people’s desire for wealth. In 1981 Taiwanese exports to the mainland were only US\$22 billion while PRC to Formosa were US\$ 20 billion. In eight years, Taiwanese exports triplicated and business progressively substituted conflict. The Strait ties became so intense that Beijing created a Special Economic Zone (SEZ) in Jianmen especially dedicated to foster Taiwanese projects, trade and investment. For more than twenty years, Taiwanese business people, known as *taishang*, have fled and settled in the mainland in order to obtain advantages in lower production costs. In the last decades, mainland China and Taiwan have clearly passed from virtually isolated territories to one of the most intense and dynamic economic zones in the world (Tanner, 2007: xiii-xiv). This phenomenon has particularly increased since 2001 when both markets entered the World Trade Organization (WTO) and placed China and Formosa over the same commercial convergence. Becoming part of the WTO will translate

into greater bilateral trades and investment that will continue to bring benefits to businesses. The number of businessmen, researchers, professors, students and tourists crossing the Strait has increased not only due to economic reasons but also cultural ones. In 2004 there was an agreement allowing direct flights between China and Taiwan on the occasion of the New Lunar Year which broke prior measures like the “three NOs”. Over the last decades, Taiwan’s entrepreneurship has been capitalising on China’s cheap labour and property. The trade linkages between both sides have risen sharply despite Cross-Strait tensions and investment restrictions imposed by the Taiwanese government. In fact, Taipei has been trying to stop the hollowing out of Taiwanese economy by “mainlandmania” since the 1990s. In 2004, more than four million Taiwanese tourists visited PRC and 98,550 mainland Chinese visited Taiwan, which is remarkable if we consider that until 2001 no one had done so before (Paradise, 2007). Since 2001, China has become the main market for Taiwan exports and the main destination for foreign investment. In 2006, the overall investment from Taiwan to mainland China was USD\$7.64 billion, an additional 27.2 percent than the previous year and trade with Formosa grew 15.4 percent according to Taiwan’s Mainland Affairs Council (Paradise, 2007).

Most Asian countries tend to be more in favour of a Cross-Strait resolution under a cooperative framework rather than under a conflict scenario. The members of the Association of Southeast Asian Nations (ASEAN) want Taiwan to take on a more active participation in Asian affairs, creating the necessary conditions for economic opportunities without affecting its political *status quo*. None of them want ROC to move toward *de jure* independence because it may provoke military conflict and instability in the region, which means that Asian countries only recognize “one China” and see the Taiwan claim as an internal issue of China. But at the same time, they recognize the political and economic progress of Formosa in essential matters as the sensitive containment of epidemic diseases and technological development. One of the most frequent complaints of other Asia countries is the non-participation of Taiwan in the WHO, despite the fact that it is one of the countries that has most helped in the fight against diseases. Taiwan has specialized institutions and research centres especially in technological areas that could easily contribute to educational exchanges under more cooperative programmes. ROC has also blocked the entry into other organizations including the Chiang Mai Initiative (CMI), Asia Bond Market Initiative (ABMI) and ASEAN in spite of it being one of the countries with the most financial reserves in the world with its own independent currency, a central bank, own financial policies and is part of the

Asia Development Bank (ADB), Asia-Pacific Economic Cooperation forum (APEC) and WTO. Taiwan had an important role in the 1997 Asia Financial Crisis but it was blocked from participating in ABMI, an important instance of regional cooperation in Asia characterized by disposable swap lines and other credit mechanisms in accordance with the ASEAN+3 countries. This agreement reflects the wish to support financial stability and the acceptance that Asian governments can better achieve this assembly as a group rather than individually. Notwithstanding Taiwan's gradual and economic involvement in the Strait, China continues to weaken its international position. For most Southeast Asia countries, however, Taiwan is an important trading partner, a productive source of investment, technology and tourism. In many economic circles the most recent suggestion is for the creation of a "Cross-Strait common market", to face political disagreements, nevertheless, some in a sceptical tone are referring to it as an idea for a "one China market".

New trends of an old issue

Although the last two chapters have attempted to clarify the main points of the Taiwan issue, it is important to note that both international relations schools provide us only with a partial part of the problem. Trying to understand the Strait issue under a realistic or liberal perspective could be completely deceitful because both are one-sided and well-known. For instance, the realist view doesn't give us a plausible explanation about the end of the Cold War without URSS and US direct military confrontation; while liberals become frustrated when they realize that open markets and trade tariffs reductions do not lead to peace. Yet, the introduction of new pieces to the Taiwan-Strait geopolitical puzzle, in which the GDP legislative and presidential of victories are evident, may allow us to fully understand the essence of the conflict, its contradictions, new issues and trends.

Firstly, from China comes its latest perspective towards Taiwan leaders which makes us believe that they have already understood the importance of not putting pressure on them. The most recent perspectives and speeches have revealed a much more under-toned language that may be interpreted as a sign of taking advantage of economic affairs without changing the *status quo*. Chen has intensified his politics of "Taiwanese identity", international prominence, especially in Latin America, promoting a new Constitution and the UN bid. Surprisingly, the provocative and populist language used just before the 17th

CCP National Congress was not received with the same aggressive rhetoric. On the contrary, Hu Jintao appealed for an unexpected “peace agreement” with Formosa as long as the island acknowledged the “one China” principle, which resembled the 1979 “Message to Compatriots of Taiwan” by Deng Xiaoping. Nevertheless, and without delay, Chen rejected the well-intentioned proposal saying it was a “treaty of surrender” (Taiwan Headlines, 17th September). In fact, we know the road to hell is paved with good intentions and we are not naive enough to interpret this speech as a very smart and practical strategy for getting social support in Taiwan and obtaining international recognition. The truth is that China finally understands that putting sour words into the speech only serves the island’s political interests. In part, DPP’s well succeeded elections were caused by mainland threats against Taipei. In 2000, Premier Zhu Rongji warned Taiwanese people against voting for candidate Chen Shui-bian, declaring it a decision for war. This is completely self-defeating because Beijing has always used harsh language and Taiwanese people have shown an immediate tendency to express anti-mainland attitudes and support independence. So, this is the smartest position towards the claim, unprecedented in respecting the political slogans of pacific arise and suitable maintenance of *mianzi* [face] in Asian arena and controlling social movements in Taiwan. It will be completely absurd to pick confrontation with the US and Taiwan risking economy performance, political stability and general international disapproval. Above all, it is trying to give the world an image of purity based on peace and stability of a well-positioned country. Higher Chinese political authorities have always reiterated that China’s path to the future will be founded on well defined, pacific rise (和平崛起 *heping jueqi*), changed to a new version of Pacific Development (和平发展 *heping fazhan*) or in a more recently one, scientific development (科学发展观 *kexue fazhan guan*), inscribed in Constitution on 17th NCCP (October, 2007).

Should the new Chinese posture of reiterated emphasis on peaceful slogans lead us to question the kind of peace behind all its discourse? The truth is that the number of missiles targeted at Taiwan seems to point out part of the answer. Suisheng Zhao (2006: 80) says that China has developed an unusual approach of conflict prevention characterized by *liangshou celue* (两手策略), which means a “two hand” strategy, like a kind of “stick and carrots” approach, involving an oscillating pattern of military coercion and peaceful investment. Basically, China is trying to take advantage of a more tolerant US by means of progressive erosion. Others see this strategy as an indicator of a

new *pax sinica* inflicting submission of other countries to Middle Kingdom hegemony. In fact, China made a lot of efforts to seek to obtain Japan, EU and US opposition to Taiwan referendum and maintain international isolation in order to submit it. Even economic relations are not considered by analysts as evidence that mainland China has adopted trade policies that will force Taipei to accept Beijing's political demands. On the contrary, while China inflicts an international political apartheid on Taiwan, economic dependence works as a "Trojan horse" in favour of Beijing, as it is referred to by Joseph S. Nye. In fact Chinese leaders fear that Taiwan authorities use the time around the Olympic Games to declare unilateral independence and stir up an explosive political and diplomatic international situation.

Another important new factor in the Taiwan issue is the evident cooperative diplomacy between Beijing and Washington, especially after 2004, when the GMD was unexpectedly defeated a second time by DPP. The US strongly opposes Chen's referendum proposal and fears it would increase tensions across the Taiwan Strait and change the *status quo*. The US policy towards Taiwan seemed less ambiguous, less intricate on Taiwan defence and more cooperative with the Beijing regime. The US used collect Taiwanese support in war against terrorism, trade liberalization, democratization, maritime security and an important mediation on the Korean peninsula and in North Korean nuclear program. For many years, Taiwan served as an important strategic platform against communist expansion and was an important buyer of American weaponry. Bilateral visits of both government members were common during this time and Bush administration paid particular attention to Taiwan's weaknesses and its international position. Most experts admitted US-Taiwan relations were recently at their worst point since 2000, from Chen's mandate to Lee Teng-hui's State to State formula. According to Kerry B. Dumbaugh from the US Foreign Affairs, the first Bush administration was quite different from previous Clinton presidency, and gave up the long-standing policy of "strategic ambiguity" on Taiwan by the alternative of "strategic clarity" that "placed more emphasis on Taiwan's interests and less on PRC concerns". This attitude could be confirmed by Presided George W. Bush words in a television interview when he said that the US would do "whatever it takes" to defend the island, "with the full force of the American military". The president also approved an ample sale of American weapons, including Kidd-class destroyers, 12 anti-submarine P-3C Orion warfare aircraft, 6 Patriot Advanced Capability-3 (PAC-3) missile defence batteries and 8 diesel-electric submarines. By that time, Washington and Taipei

had an intense diplomatic activity and put more effort on the international acknowledgement of Taiwan.

Within this scope, the US pressured Beijing to maintain speeches out of any type of conflict until Chen's successor came into office in March 2008. The free dynamics of economy and the gradual Taiwanese dependency would become *status quo*, a profitable solution while politics hardly won't achieve a reasonable way out. It's clear that the CCP survival depends on internal control of nationalism, which means the island will not have a political revival in the future. But at the same time commerce could be a decisive factor for the reduction of nationalist enthusiasm. On the one hand, Formosa remains a strategic pearl in the Asian security plan while it continues to challenge the US cooperation in agreeing to reduce political vulnerability caused by the Taiwan issue. George W. Bush confirmed complicity with China in the last APEC summit in Sydney when he publically refused to comment on the ROC bid to join the UN in spite of Chen's words saying that mainland China was strangling Taiwan with one hand and holding a gun to its head with another. The near future has some obscure rays in store for us while the majority of Taiwanese people seem more interested in peace stability, economic prosperity and a late politically decision, confirmed by Mainland Affairs Council (MAC) statistics. On the other, Ma Ying-Jeou seems to be more worried with economic growth than with political confrontation, especially in matters such as Taiwan's name and the promotion of Taiwanese membership into the UN. It is important not to forget that gradual economic liberalization, integration and the opening of new markets, especially after both become represented in the WTO, could also provoke political frictions because it allows Formosa to keep some international relations.

Another important element for understanding the new trends on the Strait issue is the "Russia factor". Beijing and Moscow are strengthening cooperation in economic and even military matters which represent the most remarkable approach between two countries since the ping pong diplomacy of the early 1970's. At that time, as we have seen, the Chinese political gravitation definitively and formally changed the US-Russia-China triangle from Moscow to Washington. But the latest developments in this game, however, show us that the stones could be changing again and this time with a more precise definition. China and Russia are cooperating in economic and military affairs and do not appreciate the American presence in Asia. Moreover, both are reluctant in imposing sanctions in Burma, Iran, Kosovo and Sudan, basically refusing Western imposition of sanctions on that conflict stages. A recent military joint

exercise in central Russia put together thousands of Russian Army and People's Liberation Army, showing they are closer now than ever, while Russian people witnessed, for the first time, a foreign army cross their isolated lands where no one had tried visiting before. Additionally, it intensified trade and cooperative work in the Shanghai Cooperation Organization (SCO). The western weapons embargo on China is partly working as an opportunity for Russia to approach China in business and politics. This new cooperative framework could bring new factors to Taiwan's position, especially by US worries of a new Sino-Russian axis recovery. The reason the US isolated China in 1989 was not only due to the near-collapse of the Soviet Union but also because Beijing was no longer strategically important for the US. China's isolation from the US happened because the Soviet Union was close to collapsing and the US no longer needed Beijing for its strategic plans.

Today the geopolitics puzzle is different and Washington needs Beijing's friendship. China and Russia, in the spirit of SCO, however, don't want the US presence in Central Asia and Middle East, especially after it used Afghanistan and Iraq wars to locate all important oil resources. In fact, the desperate search for energy sources is probably the hottest issue between China and US with a clear involvement of Taiwan. From Latin America, Africa and Middle East, China is developing a tentacular "Petro-Diplomacy" in order to supply its huge economic expands and maintain political stability. One of the most coveted regions of the world is the Persian Gulf where China is establishing control points that extend from there to the South China Sea. Taiwan should be the first check point on this scheme, crossing also the Strait of Malacca, the Indian Ocean up to the Arabian Gulf. This strategy, known as the "String of Pearls", is a manifestation of China's rising geopolitical influence through efforts to multiply access to ports and airfields, develop special diplomatic relationships, and modernize military forces.

Last considerations

Until recently, the Taiwan Strait was one of the world's most plausible scenarios for a war, which could involve hard weaponry including deadly nuclear missiles. The analysis of new trends of the cross Strait issue, however, suggests that though the conflict is stalemate and has reached its peak, it is on the way to a more cooperative framework based on economic interdependence. Our current perception is that military confrontation is a very remote

possibility, because it's the worst solution for all actors involved in this claim. Bush's administration, for instance, seems more connected to business and international influence of China and, especially after 11 September 2001, sees Beijing as a "strategic partner" while there is less frequent diplomatic relations with Taipei. Washington, more than ever, doesn't want PRC as an enemy, especially when Beijing leaders seem to be closer to Moscow in a renaissance of Sino-Russian axis, now under regional promotion of SCO. On the other hand, most Asian countries want trading relations with both parties of Strait, taking advantage of two significant markets and economies and are less involved in political disputes.

This entire new geopolitical puzzle only thickens the political isolation of Taiwan and puts the island on the trail of Beijing even more. Taipei is in an international inaccessible position that we consider to be an untenable and inequitable form of political isolation. China is using a profitable and desirable *status quo* hoping that time and money in a slow strategy of dependence will put the island over its geographic possessions, by softening its speeches in order not to destabilize Taiwanese public which would maintain DDP's party in power. On the other hand, the new president Ma Ying-jeou promises to pave a new path for these conflicting ties by reinstating the famous "1992 Consensus" and the resumption of semi-official talks that were interrupted in 1996. This implies the normalization of bilateral trade and economic ties and the removal of investment and commercial constraints. Immediate measures include promoting direct Cross-Strait charter flights, opening Taiwan to China's tourists, workers, Chinese products, as well as the mutual recognition of academic diplomas and exchange students.

During the last Boao Forum on the island of Hainan, vice-president elect of the KMT, Vicent Siew, in his capacity as chairman of the Cross-Strait Common Market Foundation, met with President Hu Jintao for historic talks that could open a new era of relations for the region. Basically, the meeting presented a new transversal blueprint for closer regional cooperation that could extend from the economic to social terrain. However, illusions should not be created around all this goodwill as this may well be another of Ma's strategies for falling into the grace of his voters, improving the economy and trying to soften the international *apartheid* provoked by Peking rather than a way of delimiting Formosa's sovereign power.

Contradictory attitudes are evident taking into account that Ma has always protested against China's democratic policies and publicly paid homage to Tiananmen victims. By means of a more intelligent approach and contrary

to Chen's conflicting posture, Ma prefers to use soft power to simultaneously reassure his population and reap important diplomatic dividends.

Internationally, Taiwan deserves another kind of solution, a more enlightened, courageous and well-defined American political diplomatic strategy which their involvement helped to create. Until recently Taipei followed all the tracks required by the US, created a democratic system, respected human rights and a market economy and in turn, it was treated with uncertainty and abandon. Taiwan has independent institutions, an independent government, an independent people, as some say, a specific identity system. At the same time, from the international law point of view, it's not clear that China has the right to the recover the island's sovereignty. The pressure on the ROC maintains while a more moderated rhetoric is being introduced into the speeches of the "bad wolf seducing little red riding hood".

In spite of Taiwan's fragile political position, we have a very liberal and optimistic point of view. We believe that a progressive opening of political and economic frontiers would be the most acceptable and advisable solution to the claim, even if it could cause greater dependence from the mainland. In fact, the gradual trend in business dynamics would introduce a more cooperative atmosphere and help the population to lose its fears. This doesn't mean that we are in favour of unification nor in favour of a *de jure* independence, we are in favour of a gradual cooperation between both sides, in such a way that war becomes the worst solution for the crises and allows Taiwanese people to rationally decide what they want.

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Poisoned Cooperation in Korea: Egoists, Nukes, and Reunifications's Zero-Sum Game

Nuno Santiago de Magalhães

Abstract

Inter-Korean cooperation is often considered a sustainable win-win situation, through which the ROK and the DPRK will be able to coexist peacefully in a stable peninsula, whether they remain two independent states or two autonomous regimes incorporated into a reunified Korean state. This article argues that inter-Korean cooperation is poisoned because it serves only as a selfish strategy to absorb or avoid absorption, and eventually it cannot be sustainable in equilibrium. Both Koreas are ultimately playing a zero-sum game and attach the highest utility to the outcome where one of them disappears through an absorption process that does not include prohibitive costs. Although the top preference of both Koreas is to absorb the other, given present constraints - limited material capabilities and the expected behavior of the United States and China - Seoul and Pyongyang are unable to achieve absorption in the short-run, so the optimal outcome in this strategic environment comes from cooperating and abandoning short-run absorption strategies, while keeping the peninsula peaceful and stable. The ROK and the DPRK are taking a calculated risk, each believing that the probabilities of achieving their goals are higher if they cooperate. Seoul has been cooperating with Pyongyang to prepare and

slowly stimulate a less costly and gradual absorption in the long-run. The DPRK's nuclear program did not destroy inter-Korean cooperation because the ROK still benefits from engagement, as long as the United States maintains the distribution of power favorable to the South. On the other hand, Pyongyang has been using cooperation to strengthen its economy, thus struggling against collapse and the consequent absorption by the South. In this context the inter-Korean cooperation process is likely to evolve in one of the following ways: it will break down when one actor perceives that cooperation cannot lead to or avoid absorption; or it will continue to be used as a strategy to achieve or avoid absorption, until eventually one polity disappears.

Introduction

Many South Koreans live unworried in an increasingly cosmopolitan country, looking with benevolence or indifference to the North and remaining genuinely convinced that inter-Korean conflict will not return. Moreover, they believe that both Koreas will maintain a cooperative win-win environment and consequently will keep the peninsula stable, whether they remain divided or ultimately reach a reunification solution that pleases everyone. Unfortunately, this seems to be a distorted vision. It is true that the Korean War of 1950-1953 was not followed by another military conflict between the Republic of Korea (ROK) in the South, and the Democratic People's Republic of Korea (DPRK), in the North, despite the occurrence of occasional clashes and the use of aggressive political rhetoric. It is also true that cooperation between both states has been increasing, despite the tension brought about by DPRK's nuclear program. However, the peninsula remains a focus of instability in Northeast Asia and the current cooperative relationship between both Koreas is not as healthy as it seems. This essay deals with the latter fact and states that cooperation between the ROK and the DPRK is a poisoned one, given that it is merely a strategy to achieve or avoid absorption and it is probably doomed.

The theoretical framework of this essay is that states are rational and egoist units that seek to maximize gains in an anarchical system, and their preferences concerning security have a higher utility attached to them than preferences concerning wealth, unless the probabilities of being destroyed by economic collapse become higher than the probabilities of being destroyed by a military attack (Magalhães, 2007: 7-12). Seoul and Pyongyang have been rationally adapting their behavior to the preferences of each other, in a

strategic cooperative engagement that has been responsible for a balance, whose outcomes have been satisfactory to the two actors. Even in the presence of sensitive issues such as nuclear weapons and reunification, both countries have been able to sustain a conciliatory approach. Such a cooperative environment has led to a widespread assumption in political discourse and public opinion that cooperation between the two countries can be sustained and improved, even leading to a non zero-sum Korean reunification, in which both regimes peacefully coexist in a confederate state. This belief seems misleading and, although inter-Korean cooperation has been and can continue being positive in the near future, such cooperation is endogenously poisoned.

Both Koreas are playing a zero-sum game in which both attach a highest utility to the disappearance of the other, in the sense that only one political regime can subsist in the peninsula. That zero-sum game is what makes inter-Korean cooperation eventually unsustainable: the top preference of each state concerning the peninsula is the disappearance of the other, so they actively prepare to fulfill that goal under favorable conditions and try to avoid that the other achieves it. In this context, both Koreas are cooperating because they cannot absorb the counterpart in the short-run, so they use cooperation as a strategy to achieve absorption in the long-run (ROK) or avoid being absorbed in the long-run (DPRK). Seoul and Pyongyang do not have benign intentions towards each other or seek to keep a cooperative coexistence indefinitely. Past and present behavior of the Koreas seems to be a consequence of such a competitive logic, so in the future inter-Korean cooperation is likely to break down when the expected utility of cooperating is surpassed by the expected utility of defection; or to continue serving as a strategy to absorb or avoid absorption until one polity finally disappears.

Inter-Korean Cooperation

The Korean peninsula is a focus of regional instability and major actors remain deeply involved in it (cf. Kihl and Hayes 1997; Hahn and Lee 1998; Park and Kim 2001; Kwak and Joo 2003; Kim 2006), particularly the United States and China. Formally the peninsula continues at war and is still divided by politico-ideological factors and not by ethno-national ones. Notwithstanding the obvious tension between them, the ROK and DPRK have been cooperating throughout the last decades, with different degrees of engagement. Cooperation requires that actors adapt to each others' preferences in an inharmonious

environment,¹ and the relationship between actors can vary: actors may be closer and less suspicious of one another or they may be detached and highly suspicious. Inter-Korean cooperation, from the dialogue of July 1972 to the recent summit in October 2007, has not evolved in a linear way because strong cooperative actions have been followed by non-cooperation or weaker cooperative ones. But the period of 1998-2007 is the one where cooperation has been stronger and better organized, basically due to the Southern engagement policies of Kim Dae Jung and Roh Moo Hyun. Although inter-Korean cooperation can often be seen as consequence of nationalism, it seems clear that selfish gains pursued under domestic and external constraints have been the driving force of the process, while idealist factors only played a marginal role.

One may argue that inter-Korean cooperation formally began on July 4th 1972, when both countries announced a joint declaration in which they pledged to promote peaceful reunification and the end of hostility in the peninsula. This was a breakthrough in the relation between two countries that had been marked by reciprocal open hostility and violent discourse. In spite of this dialogue, cooperation remained almost inexistent due to the lack of domestic and external incentives. In the case of Seoul, the regimes of Park Chung Hee (1961-1979) and Chun Doo Hwan (1980-1988) controlled popular desire for better relations with the North through “cosmetic gestures” such as the 1972 dialogue, while both presidents continued using the menacing image of the communist North as a way of consolidating their undemocratic regimes (Harrison, 2003: 70). Inter-Korean relations remained unstable and with no clear cooperation pattern, marked randomly by positive signaling such as the aid provide by the North to Southern victims of floods in 1984 and by negative ones such as Pyongyang’s terrorist actions against Seoul’s officials in Rangoon in 1983 and against a commercial airplane in 1987. Amid instability and tension, in 1988 President Roh Tae Woo put forth his Nordpolitik, which in terms of inter-Korean relations, defended bridging the differences with Pyongyang’s most important allies, the Soviet Union and China, as a way of isolating the North and eventually promote its openness and ease tensions in the peninsula. Despite feeling threatened by Seoul’s closeness with Moscow and Beijing, only after the Cold War would the DPRK feel forced to enter a new level of inter-Korean cooperation.

The end of the Cold War brought a transformation in inter-Korean cooperation, with the ROK emerging as potential reunification promoter

1 For a full concept of international cooperation see Axelrod and Keohane (1986: 226). For further introductory readings see Oye (1986) and Stein (1990).

and the DPRK defending itself and struggling to survive. If, until the 1970s, Pyongyang was considered the strongest state, Seoul's economic development and the silent defeat of communism marked an inversion. The United States was clearly the only superpower in East Asia, Russia was distant, and China was ambivalent, therefore Pyongyang's position was very delicate in terms of security and economic survival. It was under those new structural constraints that the Koreans entered a new period of cooperation. On December 13th 1991 the Agreement on Reconciliation, Nonaggression and Exchanges and Cooperation (Basic Agreement) was signed by the ROK and the DPRK, and on December 31st of the same year they signed the Declaration on the Denuclearization of the Korean Peninsula (Joint Declaration). Despite those agreements, the North Korean nuclear crisis of 1993-1994 brought back high instability, which was only defused by the Agreed Framework signed between the DPRK and the United States in October 1994. However, the North always kept its aggressive rhetoric because of its need to keep the antagonism alive, mainly to strengthen the regime at home after the death of Kim Il Sung. On Seoul's part, Kim Young Sam, successor of Roh Tae Woo and in office from 1993 to 1997, discretely sponsored policies that were part of a strategy to promote Pyongyang's collapse and a gradual and less costly absorption by the South. According to some he even hoped that his administration would witness the collapse of the DPRK (Harrison, 2003: 71-82). But Pyongyang did not collapse and, especially after the 1997 Asian financial crisis, Seoul became more cautious about the North's collapse and Korean reunification. The ROK had the upper hand in terms of relative power, due to its alliance with Washington, so it could carefully plan a long-run absorption that did not involve astronomical costs.

Kim Dae Jung, elected in 1998 and using an idealistic rhetoric, declared that regime change and absorption was not only undesirable but also impossible, arguing that if Seoul tried to push Pyongyang towards collapse, it would only make the latter more aggressive and reactive; hence the only solution was an engagement that could ultimately lead to peaceful coexistence and cooperation. The Sunshine Policy was born (See Moon and Steinberg 1999). Kim Dae Jung brought inter-Korean cooperation to a new level, defining clearly an engagement policy destined to strengthen the ties between Seoul and Pyongyang. His Sunshine Policy, also known as DJ Doctrine, was based upon three principles: non tolerance of military threat or provocation by the DPRK; abandonment of the idea of unification by absorption and other threatening measures that undermined Pyongyang's regime; and the promotion of exchanges and cooperation through the resumption of the Basic Agreement of 1991 (Moon, 1999:

38). More specifically, the Sunshine Policy was a “proactive policy”, driven by a “flexible dualism” that improved South-North dialogue by emphasizing the need to discuss easy issues and economics first and not follow a rigid defence of reciprocity in actions; it also emphasized the continuation of “military deterrence” based upon ROK-United States alliance, “domestic consensus” and the notion of “pseudo-unification”, by which Seoul recognized that formal reunification was a long and difficult goal and that the ROK should pursue a *de facto* unification through the exchange of personnel, goods and services and through confidence building and arms control (See Moon, 1999: 38-42).

Due to such engagement strategy, cooperation has obviously become deeper and more stable; projects such as Kumgangsan Tourist Region and Kae-song Industrial Park reflect such fact. The South has also been careful when it comes to controversial issues such as human rights, which have provoked negative reactions from Washington, mainly after George W. Bush came to power. The 13-15 June 2000 inter-Korean Summit in Pyongyang symbolized the new Korean cooperation, with vows of friendship being promoted and military, political and economic meetings taking place after the summit. However, the North acquiesced to such an event because it was paid off by the South and it was in its best interest to get closer to its wealthy Southern neighbours, willing to open their purses to have stability. Despite the Southern idealistic discourse, Pyongyang has certainly received ROK’s engagement policy with suspicion and was aware that Seoul had an undisclosed agenda (see Snyder 1999).

In office since 2003, Roh Moo Hyun has continued to defend the Sunshine Policy approach and has presented his own version of the engagement, the Policy for Peace and Prosperity, which in practice has kept Seoul’s cooperation strategy intact. This policy has two goals – peace in the Korean peninsula and pursuit of prosperity to both Koreas and Northeast Asia – and is based upon four principles: resolution of issues through dialogue; mutual trust and mutual-ity; international cooperation based upon the directly concerned parties; and public participation. For engagement supporters, unfortunately, Pyongyang’s nuclear policy surely put cooperation under pressure, with South Korean critics accusing the Blue House of giving too much without relevant returns and Washington showing signs of irritation. In effect, the relationship between the Blue House and the White House has not been perfect, especially due to Seoul’s sensitivity towards issues that can anger Pyongyang and to its lame response to the American strategy towards the nuclear DPRK.

In spite of the nuclear test of October 9th 2006, the ROK and DPRK ended up resuming their cooperation policy, even if the behavior of Pyongyang

in the Six Party Talks will be relevant to Seoul's future strategy. The Summit of 2-4 October 2007 was a recent demonstration of inter-Korean cooperation, in which Seoul and Pyongyang have not only continued to defend peaceful coexistence and unification, but also signed a peace declaration in which they supported the replacement of the Korean War armistice by a peace treaty. Along with other inter-Korean official meetings and events of different cooperative nature occurred throughout 2007, the latest defense ministers' meeting in November illustrates the present cooperative openness of both Koreas, although the conclusions were far from ideal and reflected competing strategic interests.

Present inter-Korean cooperation can be classified as a symmetrical process in which two units, with different economic and military capabilities but yet unable to exert a determining influence on the behavior of the other, use it as a strategy to absorb the other in the long-run (ROK) or avoid absorption in the long-run (DPRK), while obviously profiting from stability and peace in the peninsula. Peaceful coexistence is surely better than a hostile one, but it still is a second choice derived from the fact that none can achieve short-run absorption. Looking closer at the DPRK's nuclear policy and to the reunification conundrum, one can perceive why inter-Korean cooperation serves as a strategy to achieve or avoid absorption, and is not ultimately driven by idealistic preferences for peaceful coexistence.

The Nuclear Choice

Pyongyang has chosen to develop nuclear weapons in face of structural constraints, perceiving them as essential survival tools (Magalhães 2006).² DPRK's nuclear program constitutes an obstacle to inter-Korean cooperation but, until now, it has been unable to break cooperation down. Besides that, due to the fact that the ROK is a secondary participant in the denuclearization process and its options are limited, it is possible that cooperation does not break completely even if Pyongyang is able to maintain its nuclear capabilities.

Pyongyang has been trying to develop a nuclear program since the 1950s, as its contacts with Moscow indicate. Nuclear weapons would serve to reunify the Korean peninsula on its terms and guarantee the regime's survival. However, in the same way that the United States controlled Park Chung Hee when he threatened to develop nuclear weapons in the South, the Soviet Union

² See also Yoo (2003).

was also able to exert a crucial influence over the North. Pressured by Moscow, Pyongyang felt difficulties in developing its program in an independent manner but eventually it ended up commanding the process in the last years of the Cold War and avoiding strict international control. Although in 1985 the DPRK joined the Nuclear Non-Proliferation Treaty (NPT), it would only sign the safeguards agreement with the International Atomic Energy Agency (IAEA) in 1992, years after the Yongbyon nuclear reactor became operational.

The end of the Cold War led to more threatening United States, to the disappearance of the Soviet Union, and a dubious alliance with China. This context has made Pyongyang realize that the nukes were essential to increase its possibilities of survival. Even if he felt cornered, considering his fragile position when signing the 1991 agreements with Seoul and the referred 1992 safeguards agreement with the IAEA, Kim Il Sung put forth a bicephalous strategy through which he tried to approach Washington while simultaneously preparing to develop the ultimate deterrence factor. This obviously required economic policy trade-offs in the allocation of resources between civil and military sectors (Park 2004). The 1993-1994 nuclear crisis was solved by the Agreed Framework of 1994 but this agreement failed to put an end to Pyongyang's nuclear program. On the one hand, Bill Clinton seemed to hope that the death of Kim Il Sung in 1994 and the country's serious economic hardships would bring down Pyongyang's regime before he had to make any significant concessions, especially when the Republicans gained control of the Congress. On the other hand, Kim Jong Il knew that he had to hold on to the nuclear program as long as he could.

The inconclusive engagement with Washington lasted until George W. Bush arrived to the White House and altered the American policy towards Pyongyang in 2001. It was a more assertive policy which was later wrapped up in the 2002 «Axis of Evil» speech that put the pressure on North Korea, Iran and Iraq. The invasion of Iraq in 2003 and the aggressive «democratic peace» rhetoric of Washington – that actually was still less corrosive than Pyongyang's discourse – must have genuinely frightened Pyongyang. However, these factors also served as an international justification for Kim Jong Il's development of nuclear weapons. The Six Party Talks, the negotiations that since 2003 integrate the DPRK, United States, China, ROK, Japan, and Russia, in order to negotiate the end of Pyongyang's nuclear program, were ineffective in preventing the development of nuclear weapons by the North Koreans. Nukes gave Kim Jong Il deterrence against outside enemies, leverage in negotiations, and domestic prestige. In fact, although Bush's policy was obviously menacing, Pyongyang

was only looking for an excuse to develop such weapons and in February 2005 it officially acknowledged possessing them. The DPRK tried to make a demonstration of its nuclear capability to the world through the dubious nuclear test in October 2006, which seemed more a way of redeeming from the failed missile tests in July of that year and of getting an extra leverage in the Six Party Talks than a carefully planned test. To understand why Pyongyang has chosen to possess nuclear weapons and to assess to what extent it is willing to keep them, it is imperative to examine what goals have driven DPRK's nuclear policy.

States have preferences and they rationally design strategies to pursue them and achieve the outcome with the highest payoff possible. DPRK's nuclear strategy has goals that can be lined up throughout a continuum, from the small, immediate objective to the ultimate objective, including all sorts of intermediate goals. The small, immediate objective is to exchange the nuclear program for minimally acceptable political or economic benefits, while the maximum objective is to be considered a legitimate nuclear power, not only having the benefits of the nukes but also avoiding the costs of being an international pariah. Since DPRK's top preference is to absorb the South or at least, under constraining conditions, to avoid absorption, the best strategy is to be legitimized as a nuclear state. The fact that its nuclear policy is driven essentially by survival concerns is not only due to Washington's threat, considering that Pyongyang possesses a respectful conventional deterrent and the United States are not avid for a Korean reunification, but also by the fear of being gradually absorbed by Seoul. Nuclear weapons are not enough to prevent a regime from collapsing due to domestic constraints, but they would surely prevent the South from having excessive leverage over Pyongyang. North Koreans would be able to «legitimately» keep their nukes in case of: international or American recognition of its nuclear status; the end of the nuclear non-proliferation regime; or a nuclear race in Northeast Asia. But all three scenarios are unrealistic in the foreseeable future.

The first one is unrealistic because no major power, not even China, is currently interested in a nuclear DPRK. Washington and Beijing benefit from the NPT in traditional security terms by preventing other states from acquiring such power, with China particularly interested in keeping Japan out of the nuclear club. Moreover, the United States are concerned with the fact that too many nukes in the world increase the possibilities of a terrorist group getting their hands on one and use it in American soil. For Pyongyang it would be perfect to be internationally recognized as a nuclear power, but a bilateral acquiescence from Washington, similar to what was done in the case of New

Delhi, would certainly be enough. Both forms of recognition, international or American, seem out of the picture. The second scenario, even in the less probable case of the emergence of a nuclear Iran, seems unlikely because the nuclear non-proliferation regime will not be brought down in a short period of time. The third scenario, although probable in the long-run, is currently blocked by the American alliances with Japan, ROK and Taiwan, which currently prefer to stay under Washington's nuclear umbrella. Those three scenarios seem as improbable in the short-run as a scenario where the Chinese allies become the hegemonic power in Northeast Asia, inverting the power distribution in the Korean peninsula, granting legitimacy to Pyongyang's regime and dramatically reducing its need to possess nukes. In the present scenario and distant from more favorable ones, the DPRK needs the nukes, though keeping them implicates high costs. Yet, Kim Jong Il has been using Seoul's willingness to cooperate and Sino-American rivalry to hold on to the nuclear weapons without getting pressured so hard it collapses.

The United States and China still have interest in keeping alive the nuclear non-proliferation international regime, which limits the access to nukes and they are willing to cooperate to make them disappear from the DPRK, but they diverge in terms of how strongly should they pressure Kim Jong Il. Beijing has been essential in keeping Pyongyang's regime alive due to fuel and food aid. Despite occasionally stopping the fuel flow to pressure the North Koreans, the Chinese oppose any measure that can lead directly to the collapse of Pyongyang's regime, because they are not interested in having American troops in its borders, in receiving a massive flow of North Korean refugees, and in losing an ally in the region.

The United States have a bigger dilemma. The DPRK has been useful after the end of the Cold War in the sense that its menacing regime helped justifying the presence of American military in the ROK and Japan. That is the main reason why Washington has not pushed for Korean reunification beyond the formal official support. But since the DPRK has gone nuclear, new gains have been added to an outcome involving regime change and pro-Seoul reunification, since the disappearance of Kim Jong Il's regime would also make its nukes disappear along with the dangers of proliferation. In fact, a nuclear DPRK poses essentially a proliferation threat because its offensive capability can be contained by Washington. Such proliferation threat can be felt at state and sub-state levels: at state level the proliferation can be direct (state to state transfer of nuclear materials), or indirect (regional nuclear race in which states such as Japan or South Korea feel compelled to develop nukes); whereas at sub-

state level, the DPRK could sell nuclear material to actors working inside the state, such as terrorist groups (Magalhães, 2006: 95-96). If the Six Party Talks are not able to lead to Pyongyang's disarmament, Washington is facing the problem of having to choose if it is more profitable to keep Kim Jong Il's regime, because it is strategically useful in the region, to strangle harder the regime in order to bring it down, even if Washington has limited means to do so.

In practice, the DPRK has been able to maintain a nuclear program because economic sanctions are usually ineffective against a totalitarian state that controls its population, and also due to the fact that China refuses to pressure too hard. Even so, Pyongyang will incur in increasing costs to maintain those nukes and it is possible that a correct formula of pressure and incentives might lead to its disarmament. There are many opinions on how to make Pyongyang give up its nuclear ambitions (e.g. Kim and Harrison 1995; Sigal 1998; Albright and O'Neill 2000; Harrison 2003; Cha and Kang 2003; Hong 2003; O'Hanlon and Mochizuki 2003; Newnham 2005) but any solution must carefully take Pyongyang's preferences into consideration. If Pyongyang's higher preference is to be considered a legitimate nuclear power and if the longer it keeps the nukes the higher the leverage it can have in negotiations, what can make Kim Jong Il abandon his nuclear program? Pyongyang will only give up its maximum goal if it considers that the nukes are a present menace to the regime and such a menace can only disappear if the weapons are also gone. Presently, the DPRK considers that the costs of possessing nuclear weapons, international «isolation», sanctions, threats from Washington and Tokyo - are compensated by the gains – nuclear deterrence, negotiation leverage, and of course, the perspective of eventually being legitimized as a nuclear power.

Pyongyang will only give up its nukes to avoid a collapse of the regime in the short term directly provoked by them, in the sense that such threat becomes more dangerous than the long-run absorption by Seoul that those nukes ultimately seek to prevent. These assumptions may lead to conclusions that pressure alone can disarm Pyongyang.³ However, pressure alone can put Pyongyang in a situation where it only has damaging options, which can be hazardous. If abdicating from the nukes does not make the threat to the regime disappear, the DPRK might as well keep them and provoke a brinkmanship crisis. But an incentive policy alone is also a flawed approach because the maximum goal will still be possible, so incentives will not be enough to provoke a strategy change. The solution seems to lie on increasing the costs of keeping

3 John Bolton, former Ambassador of the United States at the United Nations defends such pressing strategies. See also Triplett (2004).

the nukes to a level of rupture but then, to prevent Pyongyang from opting for a risky brinkmanship strategy, incentives should be provided to assure the North Korean leadership that at least they will survive in the present. Washington is the only one capable of producing such pressure and providing such incentives. Throughout the last fifteen years, Clinton did not pressure enough and did not provide incentives efficiently, whereas Bush started with low incentives and high pressure but without means to enforce such aggressive policies. Presently, the Bush administration is willing to provide incentives and keeping Pyongyang under pressure, but the problem is that China, and to some extent the ROK, dilutes such a pressure.

The Six Party Talks are at a crucial point, in which the statement of February 13th 2007 is being implemented and apparently the DPRK is abandoning its nuclear program in exchange for political and economic benefits. Yongbyon has been shut down and the IAEA inspections have restarted. However, if Pyongyang is not desperate, it is likely that the process will have to face serious traps. North Koreans seem to be trying to obtain as much as they can without having to lose the nukes. Pyongyang can obtain incentives such as oil, food aid, the removal from the American list of terrorism-sponsoring states, a Korean War peace treaty, and the normalization of relations with the United States. The DPRK has already profited from fuel aid and the funds unfrozen from the Banco Delta Asia, and although Yongbyon was shut down, details about the nuclear program have not yet been disclosed and the weapons remain untouched. Some of the incentives can be obtained without letting go of the nukes and it is rationally predictable that the DPRK will try to do so. If it does not, it will likely mean that the regime is struggling economically and desperately needs to reach a bargaining solution, in which at least the minimal objective of its nuclear policy is achieved. Other explanations for a hypothetical situation in which Pyongyang abandons its nukes include justifying it as a miscalculation or an irrational decision, but these are obviously less probable. Hence, one should not take Pyongyang's disarmament for granted and should expect difficulties in the implementation of the denuclearization agreement. Pyongyang's violation of the 2007 deadline illustrates it.

If Pyongyang does not disarm, it is tempting to believe that inter-Korean cooperation will break down, but the fact is that it might not. The nuclear crisis has understandably shaken the inter-Korean relationship (see Kim 2004), but in essence Seoul continued opting for cooperation in spite of divisions within South Korean public, especially when Pyongyang announced the possession of nuclear weapons. Critics of engagement argue that positive incentives

from the South were not only inefficient but they were also used to subsidize Pyongyang's nuclear program. Supporters argue that despite its nuclear program the DPRK is more cooperative towards the ROK, and that this is a long term strategy that will eventually lead to peace and even reunification. With Lee Myung Bak and the Grand National Party (GNP) in power after the election in December 2007, it is normal to expect an initial aggressive reaction from Seoul if Pyongyang maintains its nuclear weapons, even including the immediate rejection of cooperative engagement. It is normal because the conservative GNP is home to many critics of the Sunshine Policy and its official position is that cooperation must depend on reciprocal gestures from Pyongyang, which have not been enough until now.

Despite that predictable initial behavior it is probable that Seoul will be tempted to go back to engagement, even if a conservative Blue House promotes a tougher policy than Kim Dae Jung and Roh Moo Hyun, pressing North Koreans over nuclear weapons and human rights. Consequently it is likely that cooperation continues, even behind a tough rhetoric. Why? Presently, Seoul does not play a relevant role in the DPRK nuclear issue, which means that its attitude will not significantly influence the behavior of Pyongyang in terms of keeping or abandoning its nukes. Hence, promoting discord with the North is less useful than continuing cooperation, given that the only gain coming from discord is a relative improvement in the relations with the United States and probable domestic support (although this one is volatile); whereas the losses would involve having Pyongyang return to an aggressive posture that destabilizes the peninsula and probably have a small quarrel with Washington (that would not jeopardize the alliance). Therefore, it will still be profitable for Seoul to cooperate with a nuclear DPRK if Washington keeps on guaranteeing its military protection and remains unwilling to punish the South Koreans for not fully supporting an American tougher policy against Pyongyang.

Though inter-Korean cooperation will probably continue, even in the extreme case of a GNP administration coexisting with a nuclear North, there are at least three scenarios - unrealistic in the foreseeable future - in which Seoul would not cooperate and could even go nuclear itself, regardless of the political party in power: if Pyongyang's behavior indicates that it can act offensively against the South; if the United States makes an ultimatum to the ROK in case Pyongyang goes too far (as it would happen if it smuggled nuclear materials); or if the alliance with the United States is severed. In those scenarios Seoul would certainly have more incentives to promote regime change and a costly economic absorption than to cooperate. But such scenarios are unlikely to oc-

cur so it is probable that a conservative Blue House will continue to cooperate with the North instead of using an ineffective strategy of promoting regime change, even if Pyongyang keeps its nuclear weapons. However, conceding that the nuclear issue might reveal insufficient to end inter-Korean cooperation, reunification appears as an inescapable process that will eventually make the Korean zero-sum game visible, either leading to cooperation falling through or to the absorption of one state.

Reunification's Conundrum

After the Korean War, Washington, Moscow and Beijing did not support further military reunification efforts by Seoul and Pyongyang. Syngman Rhee and Kim Il Sung had to give up their plans for a quick reunification under their regime. In 1972, South and North pledged to work together to achieve a peaceful reunification and this rhetoric is still dominant today, as if it was possible to sustain a reunified state where two different systems would subsist in parity and remain quasi-sovereign polities. The most widespread political project to the peninsula is a Korean confederation, in which the two regimes are legally recognized and coexistence becomes institutionalized. But there is no formal inter-Korean consensus about the political form of a reunified state and, in practice; both countries are not pursuing reunification in the short-run. Moreover, external actors play an important role in the peninsula and have been contributing to the postponement of Korean reunification.

Nowadays, it is common to talk about the collapse of the DPRK, gradual reunification under Seoul, or a confederation controlled by the South. However, throughout the first decades after the peninsula's division the North was considered the strongest and wealthiest half, so the ROK's military regimes from 1961 to 1987 feared being absorbed by the DPRK, which had stronger institutions, better economy, and domestic political stability (See Harrison, 2003: 70-71). Both countries' reunification policies and perspectives about a confederation have been changing according to their relative power and to international context.

Due to its superiority, Pyongyang nurtured the idea of a Korean unitary state, the confederation being a temporary stage in which both regimes would prepare to full blown political reunification. Kim Il Sung was convinced that Pyongyang could absorb Seoul in case they decided to advance towards peaceful reunification. This was DPRK's official position, but it started to change when

North Koreans realized that the South was becoming wealthy and stable, and mainly when they understood that the Cold War was going to end dramatically for the communists. From that point onwards, Pyongyang started to refer to the confederation as the final stage of unification and defending a loose system. Kim Il Sung's Ten-Point Program of Great National Unity of 1993 expresses the official policy of Pyongyang, with Kim Jong Il adding later that a Korean confederation would give their regimes more autonomy than China gives to Hong Kong under its «One Country, Two Systems» policy, since Beijing has practically absorbed Hong Kong (See Harrison, 2003: 76-77). Pyongyang knows that currently it will not be able to lead a unitary state or control a federation, so it defends a loose confederation, in which it can keep most of its sovereign powers. It also defends that Seoul should commit to such a project.

The ROK is in a stronger position so it currently avoids referring to specific reunification schemes, in an attempt to keep all options open. From Park Chun Hee's «small steps first» approach, through Kim Dae Jung's «three-stage» confederation project in the 1990s, Seoul has evolved towards a position in which the elaboration of formal schemes of political reunification is being avoided. Roh Moo Hyun's Policy for Peace and Prosperity is more concentrated on cooperation and peace regime than in establishing a concrete reunification solution in terms of state building projects.

Regardless of formal discussions about reunification schemes, presently Seoul and Pyongyang are not pursuing short-run reunification, which seems to contradict what has been written here about absorption preferences, especially in the ROK's case. The DPRK's position is simpler to understand: the regime is internationally considered anachronistic and its economy is bankrupt, so reunification would likely bring Southern absorption, as was the case of East Germany. On the contrary, the ROK is richer, has a larger population, its political regime is internationally respected and, obviously, it has the support of the most powerful state in the world. In an international order based upon values that the United States significantly influenced and expanded through its Cold War victory against the Soviet Union, Pyongyang's regime is the ideal candidate to be absorbed in case Koreans opt for reunification. What might seem puzzling is that, besides this favorable environment, after Kim Young Sam, the ROK stopped actively seeking regime change in the North and consequent short-run absorption.

An immediate and erroneous answer would be that idealist governments in the South justify it or that reunification costs are considered prohibitive by South Koreans, even if it would bring future benefits (see Noland *et al.* 1998).

This might lead to the conclusion that inter-Korean coexistence or economic stability rather than absorption constitutes Seoul's top preference. But such conclusions are incorrect. Then, why did Seoul stop seeking regime change and short-run absorption? First of all, Seoul was aware that Pyongyang would not collapse as a direct result of its action; secondly, if the DPRK survived the trouble period that came after Kim Il Sung's death in 1994, it could also survive many more years; thirdly, if Seoul sought confrontation and discord as a mean to bring the regime down under such conditions, it would prompt a hostile behavior from the North for an undetermined period. Therefore, if collapse of the regime cannot be achieved in the short-run and, in order to avoid future reunification from having the costs that present reunification would have if it occurred (much higher than in Germany), Seoul decided to cooperate and contribute to the development of Northern economy. If it was presently possible to peacefully absorb the North, it is highly probable that Seoul would prefer to do so, even with its astonishing costs, contrary to the widespread perception that the ROK could effectively promote regime change in the North and achieve absorption, but it does not do so because of the high socio-economic costs. Short-run reunification would have tremendous costs in terms of economy, social integration and public opinion, but eventually they could be politically managed by Seoul.

Given that short-run absorption cannot be achieved by Seoul itself, its engagement strategy is optimal because cooperation promotes stability in the peninsula (even if one may argue that part of those resources helped to build nukes) and because it bridges the economic gap between the countries. As far as the latter is concerned, it is possible to ask if promoting DPRK's wealth will not prolong its life, which would constitute a negative strategy for Seoul. It is not a negative strategy and there is a rational purpose behind it: if Seoul pushes for economic development, it will not only bring the economies closer but will also produce reforms in the North and social transformations in the hermit state. Such a process would decrease socio-economic distance and eventually lead to political reforms. The ROK is aware that Pyongyang's real problem is not an economic but a political one. The DPRK does not benefit from national consolidation to promote economic reforms and keep the political regime closed, such as China or Vietnam. Facing tremendous challenges in the post-Cold War (cf. Kim 2001; Eberstadt 2004), the dilemma of Pyongyang is that it urgently needs to reform its economy, but such an effort may dangerously lead to social and political openness: a danger, since Korean nationalism is still strong. Economic

reforms are required and attainable, but the DPRK is politically limited by the fact that Seoul can function as a destructive and absorbing magnet.

Finally, external actors also play a fundamental role in this process, especially the United States and China, but most continue reluctant to see a unified Korea emerge, although they officially support it. Korean reunification would have important consequences for the region and for its actors (see Eberstadt and Ellings 2001). As referred before, the DPRK served the strategic interest of the United States in Northeast Asia because it justifies the existence of troops in the ROK and Japan. However, its nuclear policy is making Washington redefine their strategy, adding up gains to a reunification scenario and costs to the present one. Another reason that prevents the United States from pursuing riskier policies is the awareness that a conflict in Northeast Asia would endanger Tokyo and Seoul, and probably be a fatal blow to the alliances with those countries. Still, if Pyongyang demonstrates that it will not disarm and behaves perilously, Washington can react more assertively and actively seek regime change. For China, pro-Seoul reunification would mean hostile troops in its borders, North Korean refugees, and the loss of a non-democratic ally. In this sense, reunification is only a positive scenario for Beijing in case Washington is out of Northeast Asia and the Chinese regime is not endangered by further democratization of its neighbors. For all those reasons, the United States has not been willing to push for reunification and China remains convinced that despite being unable to fully control Pyongyang, it is in the Chinese interest to keep that regime alive.

Korean reunification is presently a political conundrum to both Koreas and to external actors in the region, particularly the United States and China. The current situation is basically a deadlock, with the ROK unable to achieve short-run reunification because Pyongyang was able to avoid collapse and is supported by Beijing. Erroneously, reunification is sometimes perceived as a mirage in the future or as a win-win situation, in which a miraculous co-existence will be kept endlessly and both regimes will come out winning. As oil and water, incompatible political regimes cannot be mixed, so it seems unrealistic to believe that a confederation could function efficiently and guarantee the survival of both. Eventually, one regime would be absorbed, whether by gradual transformation or by a defection strategy of the dominant state. Aware of that reality, Seoul and Pyongyang maintain the rhetoric of peaceful reunification and coexistence but their ultimate goal is to emerge as the only polity in the peninsula: a zero-sum game.

Poisoned Cooperation

A zero-sum game refers to the interaction, in which the gain of an actor directly corresponds to the loss of the other one, whereas a non zero-sum game exists when the interaction between two actors can produce either negative or positive outcomes for each.⁴ Both Koreas have been cooperating and benefiting from it, which constitutes a non zero-sum game with positive aggregate gains. However, ultimately, the Korean game is indeed a zero-sum one because the ROK and the DPRK will end up trying to defeat and absorb the other when the opportunity presents itself. Four questions must be addressed in order to clearly expose the rationale of this argument: Why is it assumed here that Seoul and Pyongyang's top preference is absorbing the other? If they seek to destroy the other, why are the ROK and DPRK cooperating? Are egoism and preference for absorption inevitable, or can current social interaction transform the Koreas in a way that they develop unselfish identities or adopt benign top preferences, such as peaceful and cooperative coexistence with its neighbor or confederate partner? If identities and top preferences do not change and inter-Korean cooperation is indeed poisoned, what is the future of the current cooperative process?

States are rational actors with egoist identities that seek to maximize their gains and minimize losses, designing strategies to pursue their preferences within a strategic environment that constrains them. Preferences are aligned from the highest to the lowest, priority given to the former. If leaders from the ROK and DPRK act rationally to preserve their regimes, they will use their reunification policies to guarantee their political survival by seeking to absorb the other or trying to protect themselves from being absorbed. Absorption is obviously their best assurance of survival in an anarchical environment, given probabilistic considerations over the behavior of the other since, even if Seoul and Pyongyang coexist peacefully in a loose confederation for several years, the possibilities of defection and absorption attempts by the other are always higher than the null possibility of a dead regime doing so. In practice, Seoul and Pyongyang can even act irrationally or adopt strategies that seek to achieve common goals, but the backlash of such behavior will eventually be negative and bring high costs or even extinction. For instance, if Pyongyang decides to get rid of its nukes, liberalize its economy, open its political regime and give Seoul the control of a Korean confederation, i.e. lowering the costs of a reunification, one

4 For an introduction to game theory see Dixit and Skeath (1999).

should expect the ROK to push for short-run absorption. On the other hand, the ROK would also incur in damaging costs if its top preference became the peaceful coexistence with Pyongyang or if the Blue House designed its strategy under the idealistic assumption that the DPRK would not defect. Therefore, rational Korean governments from either side of the 38th parallel will obviously tend to prefer an outcome that guarantees their survival and future prosperity to one that, despite being able to offer conditions of peace and stability, inherently encompasses the possibility of defection and hostile absorption. To absorb the other without prohibitive costs will always be the optimal choice for rational and egoist governments in Seoul and Pyongyang. So question number two emerges: why are they cooperating?

Despite the absorption preferences, inter-Korean cooperation has grown stronger. Basically they prefer to embark on this symmetrical cooperation because they cannot make the other disappear in the short-run without incurring in prohibitive costs. Thus, if they have to temporarily live side by side, they profit more if they do so in a peaceful and stable environment. The prohibitive costs derive from two factors that constrain both Koreas and force them to opt for cooperation: limited material capabilities and the strategies of their strongest allies. As for the first one, it is obvious that neither Korean state has the ability to autonomously absorb the other, considering the other's own capabilities or those from allied countries. The second constraint refers to the fact that the United States and China are unwilling to support any military attempt of absorption by their Korean allies, and in addition, Chinese behavior and American reserves about reunification will likely keep Pyongyang's regime alive. Under these conditions, the ROK cooperates to pursue long-run absorption and the DPRK does so to avoid long-run absorption. In the ROK's case, it cannot bring down Pyongyang alone and it cannot put an end to the other's nuclear program. Hence, it is better to bribe the North, promote stability in the peninsula (which benefits its economy and pleases South Korean public), and strengthen DPRK's economy, hoping that such a development will end up bringing socio-political changes that eventually allow for a long-run, smoother and cheaper absorption. In the DPRK's case, it is obvious that to invade the ROK would bring an unbearable cost: its destruction by the United States. Thus, Pyongyang prefers to lower its aggressiveness towards the South and be able to profit from cooperation, obtaining aid, investment, and moderately «friendly» South Korean positions in international forums. Hence, Korean states are egoists with absorption preferences and they are constrained to cooperate, but

some may argue that such egoist identities and top preferences can be altered by benign social interaction within the international system. Is it plausible?

Notwithstanding varying levels of idealistic influence in the design of cooperation policies, that in the South can be seen if we compare the more pragmatic Roh Tae Woo's Nordpolitik with the more idealist discourse of Kim Dae Jung's Sunshine Policy, inter-Korean cooperation does not reflect the fact that the ROK and DPRK place the highest value on peaceful and stable coexistence.⁵ But could a benign cooperative interaction transform those states' identity and alter their highest preference into one where peaceful and stable coexistence between the two regimes became the goal? Rationalist authors would be skeptical about this transformative ability of the international social structure, whereas constructivists would support it. Rationalists such as neo-realists and neo-liberal institutionalists build their theories upon the common analytical assumptions that cooperation occurs between egoist units in an anarchical system and it does not affect the units themselves, with the theories diverging only when it comes to state preferences (driven, respectively, by concerns over relative and absolute gains) and the effects of international institutions on interstate cooperation (cf. Powell 1991; Baldwin 1993).⁶ Rationalist approaches that go beyond external factors, such as the strategic perspective, also keep the agent's egoist identity unaltered by systemic social interaction (see Lake and Powell 1999). Contrarily, constructivist authors support that social structures have a constitutive effect on actors' identities and preferences (e.g. Wendt 1999). For them it is possible that social structures at international level, built through social interaction, significantly influence states' identity and preferences. That is why some authors state that cooperation policies such as the Sunshine Policy are having a constitutive effect in the Korean peninsula (Son 2006). In spite of the more optimist constructivist framework, a rationalist one seems the most adequate because there is no empirical evidence that states relinquish their egoist identities and change their preferences due to a relevant influence of international social structures. If there was, it is probable that its effects would be meaningless when it comes to the socialization of the Korean states. Thus, in this case, it seems wiser to opt for a rationalist approach and assume that Korean egoist identities and reunification preferences are kept constant and immune to the influence of social structures. Since the third

5 For an analysis of Kim Dae Jung's idealism in the design of the Sunshine Policy see Moon (1999), pp.43-45.

6 For an example of a rationalist analysis of inter-Korean security cooperation using neo-liberalism and neo-realism, along with a prisoner's dilemma game, see Lee (2005).

question has been answered, it is time to ask the fourth and last one: under this rationalist framework and the assumption that cooperation is poisoned, what will happen to inter-Korean cooperation in the foreseeable future?

There are many factors whose evolution falls outside this rationalist analysis, as is the case of economic growth, social change, technological-military innovations, and irrational decisions that, although rare (in the sense of gain maximizing units trying to profit from their decisions), are still possible. However, it is more credible to predict the basic behavior of the ROK and DPRK if one assumes that both are rational egoists with predetermined preferences. In this context, two wishful thinking cooperation scenarios are promptly rejected: cooperation is kept permanently in a divided Korea and its independent states coexist peacefully; or cooperation leads to a reunification scheme with confederation characteristics, in which two regimes coexist permanently, peacefully and efficiently integrated in one country, with the integrity of both being guaranteed by means of institutional recognition. Those idyllic scenarios are unlikely to occur because both states are rational egoists constrained to adopt a cooperative behavior that constitutes a second choice. Considering that the probability of present constraints (material capability and allies' strategies) being altered is obviously higher than that of anarchy, identity or top preferences, cooperation seems poisoned and condemned to eventually disappear.

Therefore, it is probable that when present constraints – material capability and allies' strategies – suffer alterations, this will eventually trigger a shift in the ROK or the DPRK's strategies. In this context, possible scenarios emerge: cooperation will break down because one state considers that it no longer leads to or avoids absorption; or states continue cooperating until one collapses or until one reaches an asymmetrical position and is able to gradually absorb the other. The latter scenario is currently in play and the Koreans seem to keep believing that long-run absorption will be achieved (ROK) or long-run absorption will be avoided (DPRK) through that process. The ROK will probably keep a cooperative strategy and continue to pursue gradual long-run absorption, avoiding a reunification timetable until it reaches a dominant position. As for the DPRK, it is likely to continue promoting this symmetrical cooperation and try to avoid absorption, while struggling to maintain its nuclear weapons, revitalize its economy, orchestrate minor surgical reforms that do not jeopardize the regime, and keep its society uninfluenced by the South. Ultimately, the North hopes that the structure of power in Northeast Asia is altered in favor of China and that the Chinese political model becomes the regional reference.

This poisoned cooperation is risky, but both South and North continue to believe that they have better chances of achieving their goals this way and that the risks are manageable. Seoul is aware that cooperation may help strengthening Pyongyang's economy to an undesirable level or contribute to further military upgrade, while the DPRK is also aware that increased interaction with the South might unleash social and political transformations that may bring the regime down. Despite those risks, the ROK considers that cooperation will allow them to absorb Pyongyang's regime in the long-run, and the DPRK believes that cooperation may help to avoid its collapse and consequent absorption by Seoul.

Conclusion

Inter-Korean cooperation has become stronger throughout the last years and it has brought benefits to both states. Notwithstanding its positive results, this cooperative interaction is not based upon common goals, shared identities or unselfishness, but in egoism and strategic constraints. Moreover, given the zero-sum game played in the peninsula, cooperation is poisoned in the sense that the Koreans are cooperating to achieve or avoid long-run absorption, and not to pursue peaceful coexistence as ultimate objective, which will eventually make cooperative interaction unsustainable. The ROK and the DPRK are rational egoists in terms of inter-Korean relations, thus considering absorption of the other state as their ultimate goal, preferring this outcome to all others. Presently, due to the constraints (their material capabilities and allies' strategies), Seoul and Pyongyang are forced to cooperate and to relinquish absorption in the short-run. Under present constraints, the alternatives to cooperative coexistence would be destruction and chaos if they tried to invade the other or unstable coexistence marked by aggressive policies. These are clearly outcomes with lower payoffs than cooperation.

Within this context, the future of inter-Korean cooperation may be one of the following scenarios: its breakdown; or its sustainability until one actor collapses or is gradually absorbed. Given that benign interaction cannot alter the egoist identity and the top reunification preferences of ROK and DPRK, it seems that cooperation will be affected when material capabilities change or Washington and Beijing alter their strategies in the peninsula. Cooperation will break down if those constraints are altered in a way that Seoul or Pyongyang perceive cooperation as a worthless strategy to achieve or avoid

absorption; it will subsist until collapse if one state loses resources to survive; or it will subsist until gradual absorption if short-run absorption at acceptable costs becomes attainable. Given present constraints, it seems that Seoul will continue to opt for symmetrical cooperation as a strategy to pursue long-run absorption, trying to achieve a dominant role *vis-à-vis* a possible politically weakened and non-nuclear North. As for Pyongyang, it will also try to keep symmetrical cooperation alive, trying to strengthen its economy while keeping its political regime closed so as to avoid collapse or gradual absorption by Seoul. Inter-Korean cooperation seemed alive and kicking throughout the last ten years, but it is definitely poisoned by a reality that pushes the ROK and DPRK towards a zero-sum game.

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Sea Lines of Communication in East Asia

Antônio Emílio Sacchetti

There is no other coastal area in the world that is so long and also densely populated as that of the Pacific, extending from South Korea to Malacca Peninsula, in Southeast Asia.

On the other hand, next to this dense coast are located two of the largest archipelagic states (Indonesia and Philippines) and two of the most important insular industrial States (Japan and Taiwan, the latter is not internationally recognized as such).

If Japan is an economic giant that is highly industrialized but lacks raw-materials to fuel its powerful industry, further south, Australia with its almost continental dimension and scarce population, is one of the richest countries in terms of natural resources.

There is also New Zealand, an insular country that is bigger than the United Kingdom but smaller than Japan. All these countries are very similar in terms of geographic configuration; New Zealand is a member of the OCDE and until a few decades ago, it was the only one whose richness was based on agriculture, cattle raising and on a lower scale, fishing.

As result, the great population, the insular nature of the states, the industrial development and imbalances in terms of natural resources are factors which make trade exchanges by sea compulsory, using intense traffic and high-value sea navigation lines.

So, in order to discuss maritime trade and Sea Lines of Communication (SLOC's) in the Asia-Pacific region, we must also refer to:

- The geography of region, as a stable and conditioning factor for establishing the maritime routes;
- The economic development of riparian countries, namely in what concerns import and export levels as a factor which defines the interest of maritime routes and traffic intensity;
- Maritime security and the capacity of each country to protect its interests at sea, the fulfillment of the political and economic objectives which determine their maritime strategies.

1. The Pacific Region's Geography¹

The Pacific region is extraordinarily vast. The Pacific Ocean, the largest of all the oceans, has an enormous area of 166,243,000 square kilometers, 46% of the earth's liquid surface, and is four times larger than the largest continent – Asia. It is an ocean with a huge emptiness in the centre, connected to all of the other oceans by another enormous emptiness – the Antarctic Ocean.

The connection of the three oceans – the Atlantic, the Pacific and the Indian Ocean – are wide, with no strangulation serving to separate them, just as the southern limit, the border with the Antarctic Ocean, is merely a reference latitude, 60° S.

The coastal strip densely occupied by volcanoes surrounding the Pacific is called the ring of fire. The ring is interrupted in the southern region, which only has two small volcanic areas in the Antarctica (four volcanoes on the farthest end of the Antarctic Peninsula and three in Victoria Land).

The Pacific is a deep ocean. Alongside the ring of fire is another ring of great depth and long trenches. At sea, alongside the volcano-dense regions are the most important depths. In the south, only the abyssal plain (the Belling-shausen Plain) little more than 5,000 meters deep extends between the two volcanic masses of Antarctica mentioned above.

Most riparian countries have practically no continental shelves.

This is an important characteristic, both for economic and military reasons. Continental platforms have not yet been identified for oil exploration, other than those in the seas belonging to the Indonesian archipelago, including

1 Cf., Sacchetti, António E., *Geoestratégia do Pacífico*, *Anais*, ISNG, n.º 9, Novembro de 1995, pp. 21-43

the Timor Sea, and in the South China Sea; there are no extensive continental platforms for the fishing activity of the large fishing fleets of Russia, Japan, the United States, Peru, etc. On the other hand, there are significant quantities of polymetallic nodules in the deep seabed, waiting for technological development to make their extraction profitable and for international legislation to finally draw up more regulations on this maritime activity².

From the naval point of view, large extensions and great depths, namely when these are right outside the harbors, are the refuge or theatre of operations ideal for submarines. And, as stated above, the deep Pacific has ample access to the other oceans through the southern seas. A nuclear submarine that submerges right outside Petropavlovsk, in the Kamchatka, will only be discovered when it starts launching missiles or sinking ships in a given oceanic location of the globe.

The Mariana trench, with an extension of 11,033 meters, is the deepest in the world. However, the other trenches surrounding the Asian continent are also larger than those of any other ocean. We highlight the Aleutian, Kuril, Mariana, New Hebrides, Tonga, Peru-Chile, Middle America trenches, etc., all named after the adjacent territories.

One of the rare continental platforms of this region takes up the north-east half of the Bering Sea and the access to the Bering Strait, the only connection between the Pacific and the Arctic. The fact that this sea is not very deep and is frozen over for long periods during the year, associated to the facts that the strait is not very wide and that almost all of the islands in the region are North-American, significantly limits the strategic interest of this access to the Arctic Ocean, namely for Russia, which is the country that would want to use it most frequently.

The coastlines that limit the Pacific Ocean display an interesting geographical characteristic: the access to the American continent is totally open, while the access to the Asian continent is completely closed.

In the East Pacific, the American coastline is relatively regular, with no important islands, with no individualized sea and with only one peninsula – that of California. In the West Pacific, on the other hand, the eastern coasts of the

2 After a lengthy preparation process, the United Nations Convention on the Law of the Sea was finally drawn up on 10 December 1982. On this date, only 130 countries signed it. Its ratification was also a drawn-out process. On 16 November 1993, with the ratification by Guiana (60th country), the conditions were finally met for the Convention to come into force one year later, i.e. on 16 November 1994. On 7 August 2007, 155 countries and the European Union had ratified the Convention. The United States have still not ratified it. Portugal published the ratification on 14 October 1997, Government Gazette no. 238/97, Supplement, Series I-A, pp. 5496 (1) to 5486 (192).

Asian continent and of Australia have no direct access whatsoever to the large Ocean.

In the Asia-Pacific region several seas have been identified, some of which are limited by long chains of small islands, others by the greatest archipelagic states in the world (see Map 1). These seas are the Bering Sea, the Sea of Okhotsk, the Sea of Japan, the Yellow Sea, the East China Sea, the South China Sea, the Philippine Sea, the Coral Sea and the Tasman Sea. There are other smaller ones in *Australasia*: the Sulu Sea and the Celebes Sea between the Philippines and the Indonesia Islands; the Java Sea, the Banda Sea, and the Molluca Sea, in Indonesia; the Bismarck Sea and the Solomon Sea, between the archipelagos with the same name and the New Guinea (the second largest island in the world); the Timor Sea (where oil was recently discovered) and the Arafura Sea, between Indonesia and Australia.

Map 1. East Asia Most Important Straits



- | | | | |
|----------------------|---------------------|----------------------|-------------------|
| 1. La Perouse Strait | 4. Taiwan Strait | 7. Strait of Malacca | 10. Lombok Strait |
| 2. Tsugaru Strait | 5. Luzon Strait | 8. Makassar Strait | 11. Torres Strait |
| 3. Korea Strait | 6. Singapore Strait | 9. Sunda Strait | 12. Molucca Sea |

The Sea of Japan, where the Russian naval base of Vladivostok is located, is deep, if we take into account the fact that it is an inland sea. However, all of its exits are extraordinarily closed.

The Korea Strait or Tsushima Strait (divided by the Island of Tsushima in the Eastern Channel, between this island and the island of Kyushu, and the Western Channel between the same island and the Korean Peninsula) connects the Sea of Japan to another closed sea, the East China Sea. Located on Japanese territorial waters is also the Tsugaru Strait, between the Island of Honshu and the Island of Hokkaido, the two biggest islands of Japan, which is long, narrow and not very deep. The La Pérouse Strait or Soya Strait, between the Island of Hokkaido and the Russian island of Sakhalin, also has geographic limitations and connects the Sea of Japan to another closed sea, the Sea of Okhotsk.

The Sea of Okhotsk is completely surrounded by Russian territory (Kuril Islands, Kamchatka Peninsula, Asian continent and Sakhalin Island) except in the southernmost point, where the Japanese island of Hokkaido is situated.

In the negotiations initiated with the Soviet Union and which are now being pursued with Russia, Japan is asking for the restitution of what it calls the Northern Territories and which are, in fact, the Southern Kuril Islands, those closest to Japan: the Islands of Kunashir, Shikotan, Iturup and Urup. The Kuril Islands close the Sea of Okhotsk, between Japan and the Kamchatka Peninsula. The Soviet Union, during the time of Gorbachev, had agreed to return the first two but refused to return the last two. Japan did not ask for the restitution of the southern part of the Sakhalin, south of the 50° northern latitude, conquered by the Soviet Union along with the Kuril Islands in August 1945 because Japan, in turn, had conquered it from the Russians in the 1904 Russo-Japanese War³. The transfer of the sovereignty of the Northern Territories enabled the Japanese to increase their control over the access to the Sea of Okhotsk, which today belongs to and is of great interest to Russia.

Due to its importance, the Kamchatka Peninsula deserves further reference. With a length of 1,200 km, a width of 560 km and an area of 350,000 km², it separates the Sea of Okhotsk from the Bering Sea and from the Pacific Ocean. Halfway along its eastern coast to the west extends the long chain of Aleutian Islands and as from its southernmost point until Japan lie the Kuril Islands. Although the peninsula is blocked by ice during the long winter, the Soviet Union has started to develop some air bases in the area and in particular

3 The possession of the southern half of the Sakhalin by the Japanese had been confirmed by the Treaty of Portsmouth – New Hampshire, of September 1905, which marked the end of the 1904-05 Russo-Japanese War, also marking the emergence of the United States as a world power.

the Petropavlovsk naval base, which would grant its squadrons open access to any of the large oceans.

2. Navigation, demography and economic interests

The Pacific is an ocean of extensive rather than intensive navigation like the Atlantic or the Mediterranean Sea. It is therefore an ocean that separates rather than brings together the peoples who live along its margins.

Furthermore, the Pacific is huge and appropriate, as opposed to the Atlantic, which is smaller and has larger areas of high sea. This is a consequence of the scattering of thousands of islands with territorial sea and with the right to the definition of Economic Exclusive Zones (EEZ's).

On the American border, only the United States and the central isthmus have important land connections between the Pacific and the Atlantic, just as only the United States have extensive north-south land connections with Canada and Mexico.

On the Asian coast, noteworthy is the international communications network of China's large continental mass and Russia's difficult and very extensive east-west land connections, which have more of a strategic interest rather than an economic interest, at least before the full development of Siberia.

The societies and cultures that have developed along the Pacific coastline are extraordinarily varied and the interests shown by the 42 countries in the region are exceptionally diverse.

Four continents surround this ocean (America, Asia, Oceania and Antarctica). Its margins are bordered by four of the seven most populated countries in the world (China, United States, Indonesia e Russia) and by five of the six countries with the longest coastlines (Russia, Canada, China, United States e Australia); the borders of China with countries that belonged to the Soviet Union and that today are part of the Commonwealth of Independent States (CIS) are about 8,000 km long.

In the Pacific are six of the seven biggest insular countries: Australia, almost a continent in itself with 22,230 km of coast; Indonesia e as Philippines with about 13.677 and 7.100 islands respectively, are the two biggest archipelagic states; Papua New Guinea, Japan and New Zealand. Important not to forget that Australasia is used to refer to the group comprised of Australia, New Zealand e Insulindia, the latter made up of the archipelagos of Indonesia and Philippines. There is also the important territory of Taiwan, which is not

recognized as an independent state by the People's Republic of China or by the great majority part of the international community. There are a total of 21 insular countries besides a part of Malaysia which is insular.

Very few historical and cultural interests can unite the peoples of this enormous portion of the world, which is larger than one of the hemispheres (the Pacific extends from 104° East, in the Strait of Malacca, the border of the South China Sea, to 67° West of Cape Horn, in a total of 189°).

Only four of the developed countries, of a predominantly Anglo-Saxon culture (the United States, Canada, Australia and New Zealand), grouped into two pairs which are geographically very far apart and diametrically opposed, may have several common objectives of a political, cultural and strategic nature.

Recently, strategy has sought to devise extensive areas for the development of modern cultural, economic and ideological objectives. It was already like this during the time of Karl Haushofer and of the School of Munich, in the interval between the two world wars. However, even this School ignored the Central Pacific, considering only its peripheral regions integrated in the PAN-American and PAN-Asian regions.

Furthermore, the difficulty of achieving sufficient naval power to guarantee the accomplishment of common political objectives, should they exist, irrespective of the hostilities that could result, makes it very difficult for such large areas to constitute geo-strategic unity.

Notwithstanding the importance of the economies that have developed along its margins (very weak and unstable, in the case of the New Industrialized Countries - NICs⁴), the Pacific is too large to be the world's political centre of gravity or to be controlled by the superpower or by any of the most important riparian powers.

Many countries are rich in natural resources and the economic development of the Pacific Basin is remarkable. However, for better or for worse, the potential values of the region have not yet been exhaustively explored, as opposed to what happened in the Euro-American area.

In the rapid economic growth of the region, very much based on industrial and technological development, namely as from the sixties of the last century, certain aspects of interest to the study of the shipping routes may be highlighted.

4 NIC - New Industrialized Countries. These are South Korea, Taiwan, Hong-Kong and Singapore. In 1995, the re-elected Government of Malaysia stated that its country would soon become the 5th Small Asian Dragon.

- Japan is a large insular country, with no natural resources to fuel its industry and with no energy resources to sustain it. On the other hand, the manufactured products, including those of its heavy industry, are exported to the entire world. It is totally dependent on the sea, both for import and export purposes. If the main imports come from the south via the South China Sea (Persian Gulf, Australia and Indonesia), exports also use the trade sea routes of the Pacific directed at the western coast of the United States, at the Panama Canal and at South America. The route to Europe through the Pacific is longer but only has one choke point – that of the Panama Canal – while the Suez route passes through many areas of great instability, controlled by different countries.

- The NIC are States that do not have factors that contribute to the classical definition of national power and which achieved their wealth exclusively through an industry that is totally dependent on the capital of multinationals and imports. With a reduced population and limited domestic market, the sea trade of the import of raw materials and the export of manufactured products is the foundation of their economic wealth but also the reason behind their weakness. Only Taiwan and Singapore are insular.

- Australia has more diversified external trade relations. A great exporter of natural resources, it exports to the North, to the East-Asia region, namely to Japan. In this case, the more direct shipping routes avoid the South China and East China Seas. It has the further great advantage of being able to use the sea with no significant geographical constraints in all other directions: Suez Canal, Persian Gulf, west coast of the United States, Panama Canal, and South America.

- The great transformation of China started approximately two decades ago. Do to the extraordinary economic development, which will not be analyzed within the scope of this text, its wealth in raw materials is now insufficient. One needs only to recall that, as the world's foremost coal producer and the sixth oil producer (2005), it recently became a large importer of energy resources. It has sought to diversify its sources of oil supply, looking to African countries; however, irrespective of whether they use the Strait of Malacca or the Indonesian straits of Sunda or Lombok, the routes are the same as those used in the supply from the Persian Gulf. The construction of international pipelines through Asia, projected or under construction, may prove to be an important supply alternative, but will not do away with the need to use the shipping routes in view of the rapid rise in oil consumption.

Trade throughout the Pacific basin, which due to geographical imposition depends on the shipping connections, has become much more intense in the last decades. There are many examples that may be given: for the United States of America – economic power historically connected to Europe – the transpacific trade is approximately 30% greater than the transatlantic trade; Japan, the world's second economic power, is totally dependent on the import of minerals and oil, 80% of which comes from the Persian Gulf, through the South China Sea; more than 60% of the large volume of exports from Australia (minerals and agricultural products) are transported by sea to Asian countries. Both during peace and war, these maritime relations are intense and crucial.

Some of the important routes cross the Pacific, connecting Japan, Taiwan, China and Australia to the American coast, namely to California, to the Panama Canal and to the Strait of Magellan, in South America.

However, traffic is more intense along the entire coastal region of East-Asia, particularly in the region between Japan, in the north, and the huge archipelago of Indonesia, in the south. This is one of the world's most intense navigation regions. Vladivostok further north and the Australian continent to the south also contribute to this heavy traffic.

In this way, most of the traffic has to pass through approximately 32 straits, imposing some restrictions.

The most important is, no doubt, the Malacca Strait. Approximately 50,000 tankers pass through this strait every year, almost half of the number circulating around the world. Other important straits are the Sunda and Lombok Straits. But there are more, which are previous indicated on Map 1.

The Main Trade Sea Routes (see Map 2), are:

Indian Ocean (Europe, Africa, Persian Gulf, India) to/from Asia-Pacific

Ships with less than 200,000 tons can choose the shortest route passing through the Malacca Strait; if they have higher tonnage, they will have to sail further south, through the straits of Lombok or Sunda, in Indonesia.

Indian Ocean (Europe, Africa, Persian Gulf, India) to/from Australia, New Zealand and Americas

By avoiding the Straits of Indonesia, they may sail north of Australia, by the Torres Strait or circulate freely in the south of Australia.

Transpacific Routes

Those that start in New Zealand, Australia, Philippines, Taiwan and Japan are direct routes without any restrictions.

Those that leave from China will sail the waters of Taiwan.

Those that depart from North and South Korea will have to sail through the Sea of Japan or the East China Sea will have to pass the Korea Strait and sail through the Ryukyu Islands, in waters that are under Japanese jurisdiction.

Australia from/to Japan

The important route for Western Australia's exportation of minerals runs near Timor and Moluccas and extends to the Pacific, East of the Philippines.

From the western coast of Australia, it goes by the Coral Sea and without any restrictions continues to the Pacific, east of New Guinea and the Bismarck Archipelago.

Australia from/to R.P. China and Taiwan

As the ones mentioned above, but passing the West of the Philippines.

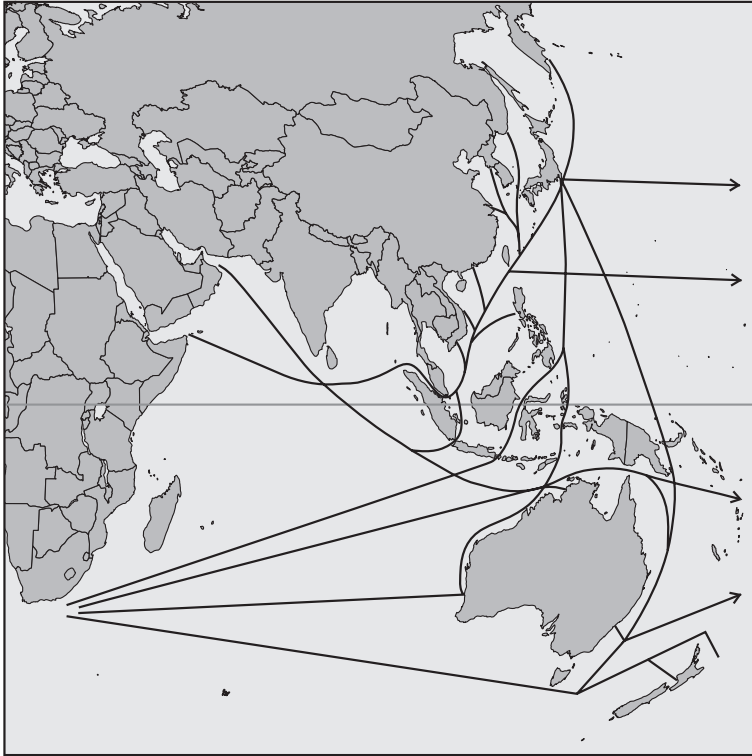
Coastal Routes

Almost all cross the South China Sea and then, depending on the destination, the Philippine Sea, or the East China Sea, The Yellow Sea and the Sea of Japan.

Northern Routes

Russia has important routes from Vladivostok to the Sea of Okhotsk passing the La Pérouse Strait, to Petropavlovsk in Kamchatka and to the Arctic, crossing the Bering Strait.

Map 2. Pacific and Indian Oceans: The Main Trade Sea Routes



3. Maritime security

95% of world trade is sea trade and 60% of oil exports are made by sea. The guarantee of security of sea routes is of world interest.

The problem of SLOC's security in the Asia Pacific announced by Professor Ji Guoxing, in 2000, in a very clear summary that has not lost its validity:

SLOC insecurities do exist, and the problems therein do not warrant optimistic views. Factors affect SLOC security include: the unstable political relationship among regional countries; different interpretation over the freedom of the seas principle; island's sovereignty disputes and overlapping maritime jurisdictional claims; the

*emerging naval build-up; and non-traditional threats such as pollution, piracy, drug-trafficking, etc.*⁵

Notwithstanding, East-Asia countries have been able to maintain questions of sovereignty between nations at a diplomatic dialogue level with noteworthy success. On the other hand, it is also recognized that the instability of the relations between great powers namely, Japan, Korea, China/Taiwan, and the United States, may represent a great threat to navigation security in the area.

However, the emerging naval build-up may be considered the result of the increase of non-traditional threats, the economic development of a greater number of countries with interests related to the use of the sea, the increase of merchant navies and regional sea traffic, all of which are deprived of the control of the two super-powers that lead the world bipolarization policy.

The security concerns that sea and industrialized western countries experienced during the Cold War in relation to navigation which at the time sustained their development are now being experienced by developing Asia-Pacific countries. And if western countries tried to organize a Three Ocean Alliance or All Oceans Alliance then, today, the Pacific is also trying to create and enhance a common security system that satisfies all the regional interests and needs. This process is underway and has already accomplished some useful achievements.

Therefore, greatest concerns right now include the non-traditional threats mentioned above, to which we may add maritime terrorism.

From remote times, the South China Sea, including the mouth of the Malacca Strait into the Indian Ocean, the South Borneo and the Philippines, has been an area with intense piracy activity.

This is always a complex problem because pirates are organized into very well armed and trained groups with information about the cargoes of their prey which are frequently obtained by contacts with corrupt portuary employees.

Moreover, these attacks have been under-reported by crews and owners wishing to avoid long delays in port for police investigations⁶ for a very long period of time.

Notwithstanding, 22 acts of piracy and armed robbery against ships in the Malacca Strait and 66 of such acts in the South China Sea were registered in 2006. The countries of the region do not have the tradition of establishing

5 Guoxing, professor Ji, **SLOC Security in the Asia Pacific**, Asia-Pacific Center for Security Studies, Honolulu, Hawaii, February 2000.

6 Gibson, Helen, *A Plague of Pirates*, **Time**, August 18, 1997, p. 44.

formal and permanent alliances. However, all of them recognize that maritime defense cooperation is an essential common interest, as a guarantee of regional security and prosperity.

Although no summary is ever complete, we may conclude that: the United States are still interested in remaining in the region, maintaining a high capacity of power projection; this American presence is only welcome by countries such as Japan, South Korea and by the smaller States of Southeast Asia; the great regional powers are developing naval capacity able of fulfilling their national defense objectives and the protection of the sea lines of communication right up to the Indian Ocean; although the small countries of southeastern Asia and insular countries may want the presence of the United States in their seas as mentioned previously, they wish to organize a system of autonomous maritime defense in order to solve security problems related to their constantly increasing maritime interests.

Human Security in East Asia: Rocks, Scissors, Papers

Diana Santiago de Magalhães

Abstract

Human security is an increasingly important concept in international politics but its effects still depend on states' interests. Evidence indicates that state policies and international cooperation concerning human security are positively enhanced if democracies and international regimes are involved. States in East Asia have shown an increasing concern with human security issues, but the fact that most of them are not democracies seems to lead to policies that are inefficient and limited in scope, especially when it comes to human rights. Moreover, regional cooperation is limited by the non-democratic nature of the majority of states and by the relative weakness of regional institutions. Therefore, although further democratization of the region is apparently menaced, more democracies and robust regional institutions in East Asia would probably promote stronger human security policies and cooperation.

Introduction

The end of the Cold War led to significant changes within the international system. Globalization and the consequent growing interdependence

between international actors are a reality. Conflicts have changed from interstate to intrastate and threats to security are no longer exclusively military. Issues such as environmental degradation, health pandemics, organized crime, economic deprivation, and human rights violation are viewed as threats to international stability. All these threatening factors have been incorporated into the loose concept of human security.

Since there is a link between national and international stability, threats to the constitutive elements of human security in one state can jeopardize an entire region. Therefore, state security and human security should not be divided but reinforce one another. Nonetheless, political leaders tend to adapt the concept of human security to their own power preservation strategies. States promote national policies to deal with those threats within a selfish point of view. In terms of international cooperation, understood as the process through which “actors adjust their behavior to the actual or anticipated preferences of others” (Axelrod and Keohane, 1986: 226), an utilitarian reasoning would make us believe that states would work together to eliminate such threats, but the reality is quite different. Unfortunately, international anarchy and state selfishness do not make a tasteful recipe. Therefore, human security in some ways remains an idealist concept that is still far from constraining the behavior of states and affects them in different ways.

The theoretical framework behind this analysis is based upon the work of neo-liberal institutionalists and democratic peace theorists. The first assumption, taken from neo-liberal institutionalism (Keohane 1984) is that international regimes are the most suitable tool to promote cooperation between selfish states that seek to solve human security problems in an anarchical environment. Most of those issues would certainly be correctly addressed if international institutions were put in place, notwithstanding the limitations of such institutions in a world controlled by states. The second assumption is that democracies can pursue more efficient domestic policies and promote stronger cooperation processes, an assessment of the domestic and international effects of democracy which is an adaptation from the work of authors such as Rudolph Rummel (1997) and Bruce Russett (1994). It is a fact that even democracies fail to have a perfect domestic and international record, as made evident by the United States’ failure in dealing with issues such as the death penalty and the Kyoto Protocol. However, democratic institutions seem to make a difference when it comes to policies and cooperation concerning many human security issues, due to their domestic accountability and international benign signaling ability. Like the children’s game, *rocks* (human security threats) can threaten *scissors* (states) and

be nullified by *papers* (domestic and international institutions), but the latter are ultimately dependent of the will of *scissors*.

This essay aims at examining the main human security problems in East Asia and focusing on how local states have been dealing with them, whether in terms of state policy or international cooperation. In East Asia there are states promoting broad national policies and international agendas, such as democratic Japan, and states, such as North Korea, that remain virtually indifferent to human security. Undemocratic regimes and weak regional institutionalization concerning human security still jeopardize efficient policies and cooperation, although states in the region are becoming increasingly aware of the negative impact that human security threats can cause. In the future, democratization and more robust regional institutions seem crucial in the promotion of better policies and stronger cooperation.

Human Security

Insecurity derives from several threats that are no longer necessarily linked to interstate wars. The world is changing rapidly and it is becoming smaller. There are no borders to stop the impact of civil conflicts, extreme poverty and famine, natural disasters, or diseases. Terrorist threats are no longer territorially limited and have become increasingly unpredictable. Crime is being organized transnationally, disregarding the Westphalian boundaries. Human rights violations continue worldwide. These are the issues we should acknowledge as threats; threats that may begin by being perpetrated against individuals but that ultimately go beyond states and may even jeopardize entire regions or the globe as a whole. The concept of Human Security was born from the necessity of tackling those insecurity issues. Its aims may seem broad but of extreme importance to global stability. In 1994, the United Nations Development Program (UNDP) introduced a new concept of human security; a concept that emphasized the importance of key issues related to *people* and *development* (UNDP 1994).

In 2003, the Commission on Human Rights gave the world a description of the elements that constitute the core of human security.

Human security means protecting fundamental freedoms — freedoms that are the essence of life. It means protecting people from critical (severe) and pervasive (widespread) threats

and situations. It means using processes that build on people's strengths and aspirations. It means creating political, social, environmental, economic, military and cultural systems that together give people the building blocks of survival, livelihood and dignity. (Commission on Human Security, 2003:4)

The concept *per se* is not easy to define since it refers to issues like «fundamental freedoms», that are extremely likely to undergo different interpretations. For instance, conceptions of fundamental freedoms are different in Confucian Asia than in the so called «West», or the Islamic world. For that reason we can also find several definitions for the term human security; however, the concept is indeed often associated with the UNDP Report of 1994, which set the guarantees of freedom from want and freedom from fear. In my perspective these two dimensions are better accessed when dealt together. Peter Wallensteen and Birger Heldt explained the two categories of the concept, and stressed the importance of their complementarity: “freedom from “wants” (such as poverty, malnutrition, disease and hunger), that is, what we often regard as underdevelopment, as well as freedom from “fear” (violence and physical unsafety), that is to be secure from violent conflict and oppression.” (2004:19) Thus, “human security complements state security, enhances human rights and strengthens human development” (Commission on Human Security, 2003:2). According to Rizal Sukmas' assessment of the economic crisis that led to social disorder and therefore to the collapse of Suharto's regime in Indonesia, 1996-1997, “human security and economic-political stability are mutually reinforcing; the former cannot be achieved without the latter, while the latter might not be sustainable without the fulfillment of the former in its comprehensive manner”.¹ Human security is more than a moral issue; it is a fundamental key to dictate the instability or stability of a region.

The same reports indicated and explained seven crucial areas where human security threats can be best viewed (UNDP 1994); let us take a look at those issues in a global perspective. First of all, economic security requires a regular guaranteed income, whether originated from a paid work or finance safety nets. The threat to economic security is not exclusive to less developed countries. If we take a look at the GDP growth in developed countries we notice that is parallel to an increase of unemployment rates. Moreover, projections of the World Bank indicate that developing economies to “expand by 7

1 Quoted in Anwar (2003: 542)

percent for the year as a whole, more than twice as fast as high income countries (3.1 percent), with all developing regions growing by close to or more than 5 percent” (World Bank, 2007a: 1). Nonetheless, both developed and developing countries are facing the problem of decaying or undeveloped social security systems, a fact that contributes to the increasing of poverty.

Secondly, we can relate food security to the access to food, whether that is physical or economical access. The main issue related to the access to food is its uneven distribution and therefore, the low quantity in some areas; the quantity of food available can be enough, but if the distribution channels are inefficient, there will be people who cannot have access to it. Besides, these issues are related to economic power; people who live below the poverty line, even if they have physical access to food, they do not have the buying power. Another contributor to famine are environmental problems; in regions much dependent on rural production, the scarcity of water and the climate change contribute to a decrease in production and therefore, to the lack of access to food. **Let us not forget** that not only the quantity of food available contributes to the well nourishment of people but also that the quality of the food is important in terms of nutrition.

Though the case is more serious in rural areas where nutritional, environmental and economical problems prevail, the reality is that health security threats are present in both developing and developed countries. Not only these threats assume different forms – such as epidemics and infectious diseases, environmental degradation or natural disasters – but they also may affect every individual. It is therefore in the global community’s best interest to tackle these issues urgently. Health issues are not isolated; they are deeply connected to issues related to poverty, nutrition and environment. The major gap in terms of North/South numbers is seen when comparing both regions in terms of child and maternal mortality and respiratory and infectious diseases, such as HIV/Aids.

Fourthly, the need for environmental security has been strongly felt and evident not only for the scientific community or environmentalist groups, but also for political chancelleries and the general public, as demonstrated by the results reached in the United Nations Climate Change Conference in Bali and the recent award of the Nobel Peace Prize to Al Gore. The causes of threats to environment security can be seen in both developed and developing countries. If developing countries are facing difficulties in the access to water, developed countries are facing pollution problems. The effects of deforestation, greenhouse gases and pollution are global problems that affect the world as a

whole. Therefore, the aim of environmental security is to protect people from both short-term and chronic environmental threats, whether they are natural or human-made. These threats are changing the world as we know it, as far as environmental landscape and as fostering conflicts shaped by nature and demography are concerned. The tensions and conflicts over land and water access are increasing dramatically and the demographic movements are leading people into living in areas considered prone to natural disasters.

Fifthly, personal security is related to the prevention of physical violence. Individuals are targets to different types of violence, regardless of their region of origin. Terrorism, proliferation of weapons of mass destruction (WMD), repressive state policies are all examples of threats to personal security. Threats to personal security can occur at a state level, an intrastate level or even a household one. The threats to personal security at a state level can derive both from actions perpetrated by states against their own population, as well as consequences of conflicts between states. In case of intrastate level, individuals can feel threatened by other groups, by the threat of crime or by several types of established discrimination. The easiest targets to violence are usually women and children, and especially for those the threats can also occur at a household level. According to Amnesty International, around seventy percent of casualties in conflicts have been civilians, mainly women and children, and at least one in three women around the world has suffered some kind of violence in her lifetime (Amnesty International 2007b). Finally, household threats are also perceived as contributions to personal insecurity, and are related to the consumption of drugs and suicide.

Community security, in my perspective, can be seen as an extension of personal security but, in this case, threats are addressed as derived and directed towards a specific group. As in personal security, the threat can come from the state, other groups or can derive from the individual's own group. The targets can be ethnic, sexual or religious minorities or socially discriminated groups within a state or an intrastate group, for instance.

Lastly, political security is concerned with the degree to which human rights are respected within a society. The waves of democratization contributed to empowering civilians; nonetheless, in the name of fighting terrorism or for the sake of economic development, states are still neglecting its citizens' basic human rights. According to Amnesty International, there are many issues threatening human rights worldwide. Let us look at some numbers: 69 countries around the world still have the death penalty; in 2006 around 1544 people were executed in 25 countries and at least 3861 people were sentenced to death in

55 countries (Amnesty International 2007a:314). Prisoners of conscience were reportedly kept in 57 countries (Amnesty International 2007b). Despite the fact that the Convention against Torture and Other Cruel, Inhuman or Degrading Treatment or Punishment has been ratified by 144 states, cases of abuse by state authorities were reported in 102 countries (Amnesty International 2007b).

The concept of human security calls for a multidisciplinary approach, since many dimensions and agents are involved when promoting human security, such as government policy makers, non-governmental organizations and independent analysts. At the Millennium Summit of 2000, the United Nations Secretary-General Kofi Annan declared the need to promote human security recognizing that “individual sovereignty takes precedence over state sovereignty”.² Therefore nation-states should promote human security, not obstruct it. But the reality is that selfishness ultimately prevails in the concerns of states and competing interests are not usually compatible. In these situations, states feel reluctant to bind themselves to treaties and perceive them as limiting instruments in the international arena. Moreover, if states do bind themselves to treaties, many do not feel obliged to comply. When they act this way, states function as impediments to achieving cooperation in human security. Instead of cutting properly the paper to produce an international regime that tackles threats, states behaving that are simply scissors cutting through and destroying the paper that could wrap up the threatening rock.

Rocks in East Asia

Globally, human security still plays the role of the secondary character in the international politics movie and in East Asia is no exception. Previously we examined the seven areas identified by the UNDP report of 1994 as being crucial to access human security threats; considering those categories, let us now look at the situation in **the** region. Nonetheless it is important to keep in mind that the division between human security issues is just conceptual, essential in terms of analytical clarity; the majority of the issues is intertwined and therefore should be viewed from a holistic perspective, such as East Asian problems illustrate.

In the 1990s, and with the exception of Cambodia, Laos, Myanmar and North Korea, the whole of Asia was experiencing economic success and relative

2 Quoted by Lee (2004:11).

political stability (Kim, 2000:290). However, the 1997 Asian financial crisis had a negative impact on the political and social cohesion of key Asian states, which aggravated human security transgressions – for instance involuntary migration, xenophobia and racism increased (Kim, 2000:290). The financial crisis contributed to the neglect of solving human security issues in the sense that budgetary priorities were related to economic recovery. In periods of economic distress, societies become more vulnerable to other threats to human security, such as organized crime, aggravation in human trafficking and illegal immigration, famine, poverty, and even terrorism. Although since the 1990s the region as a whole has progressed in terms of human security, some countries still lack political will to promote efficient policies and the region still lacks institutionalized cooperation.

In terms of economic security, East Asia region as a whole has been showing a strong GDP growth, mainly due to high productivity and exports that consequently improved living standards for the populations. Nonetheless, according to the Asian Development Bank (ADB), inequalities – measured by income and expenditure – have also risen. According to an ADB report, three dimensions are involved when explaining that fact (ADB 2007). There have been growth differences, firstly at sub-national levels, secondly at sector level and finally, at household level. Increasing inequality in the region is not that related to the rich getting richer and the poor getting poorer, but “the rich getting richer *faster* than the poor” (ADB 2007: 33). According to the ADB, in countries like China, Cambodia and Laos, the “Gini coefficient has grown by an average of more than 1% a year over the years covered by the data” (ADB 2007: 54). According to Amnesty International, the numbers of 2006 for that country showed there was an enormous (four times) disparity between earnings in towns and in rural areas. Consequently, life expectancy in China’s urban areas was reportedly between 10 and 15 years longer than that for rural areas.

Food security is another issue menacing East Asia, as pointed by the ADB, although official numbers show a general improvement. The number of people living in East Asia with less than 1 dollar a day, between the years of 1987 and 1998, has decreased from 420 million to 280 million (Amerasinghe 2002) and the numbers for undernourishment in the past decade have decreased around 3 percent a year (World Bank, 2007b:94). Nonetheless, as wealth distribution is not even, economic and physical access to food in some areas of East Asia remains harsh. For that reason, migratory movements are increasing, both from rural areas to urban areas as well as to areas considered inadequate to live in. This situation is increasing deforestation processes in many

areas, which contributes to increasing levels of pollution as well as constitutes a danger to the local ecosystems. One of the most flagrant cases of famine in the region is seen in North Korea, where the UN Special *Rapporteur* on the right to food advanced that severe hunger affects 12 percent of the country's population (Amnesty International 2007a: 159). Also Human Rights Watch had estimated that in 2002 malnourishment affected more than a half of the country's population. This specific case has not only political nuances but, since the country is frequently affected by severe floods, also environmental ones.

The main threats to health security in East Asia are related to the spread of HIV/Aids and respiratory diseases. According to UNAIDS, the highest national infection levels of the HIV/Aids in Asia continue to be found in Southeast Asia, mainly as a result of the use of injection drugs without sterile injecting equipment as well as unprotected sex. The case of Vietnam is an example of rates of HIV/Aids continuing to increase each year and has even more than doubled between the years of 2000 and 2005 (UNAIDS 2007: 23). Nonetheless, thanks to the role of international organizations, non-governmental organizations (NGOs) and the regulating intervention from governments, the number of infected people has decreased in countries such as the Philippines and Cambodia. In the latter, the prevalence of the virus had decreased from 2% in 1998 to 0.9% in 2006 (UNAIDS/WHO 2007: 24). The efficiency in dealing with this problems will be much dependent on how the states deal with issues related to transnational organized crime, namely in the areas of drug trafficking and sexual slavery. As for possible pandemic diseases, it seems that governments already forgot the lessons of the frightening spectrum of an uncontrolled outbreak of SARS in the region. Sloppy policies and deficient regional cooperation are still the rule. One of the difficulties in dealing with SARS was the lack of transparency some governments might have showed when reporting numbers. The reasons were related to the attempt to protect the region's economic development³ - related both to tourism and consumption of regional products - and to prevent international interference in internal affairs. According to the World Health Organization, "SARS did not become endemic in humans or gradually fade away. Its spread was halted less than four months after it was first recognized as an international threat – an unprecedented achievement for public health on a global scale" (WHO 2007:40). Now the region is facing the latent threat of the H5N1 avian influenza virus, which has

3 In the outbreak of the SARS epidemic, the World Bank predicted that the impact of the disease could affect the region's GDP by reducing its growth 0.4 to 0.5 percent.

been increasingly affecting humans. Hence, despite some efforts⁴, domestic interests and suspicion among regional states has been blocking the coordination of policies necessary to tackle the issue.

Environmental security is also a much discussed topic in East Asia in terms of domestic policies and regional cooperation. As for the former, the behavior of certain countries is harmful not only to their own population and environment, but also to their regional neighbors. China emerges as the paramount example, with its government privileging high economic growth rates and neglecting the environmental toll. High industrial production and economic competitiveness in an emerging economy such as the Chinese often constitute obstacles to the establishment and enforcement of environment protection regulations. Such regulations tend to decrease production rates and increase production costs. The result is environmental degradation in China and unwanted externalities that affect other countries. One of those externalities is the so called «yellow dust» that affects neighboring countries such as South Korea, which is a dust storm that has become increasingly harmful due to the intense desertification in China and air pollution from Chinese industry. Regional cooperation concerning this problem is obviously hindered by Chinese economic priorities, but other issues could and can be addressed in a cooperative mode. For example, the effects of the December 26th 2004 tsunami, devastating for countries such as Indonesia, Thailand or Myanmar, could have been reduced if adequate prevention and coordinating regional networks were established.

Finally, it is hard to talk about personal security, community security and political security in the region in isolated terms; these threats are extremely complex and highly intertwined. The primary case pointed here is the North Korean. The region of Pyongyang represents the greatest threat to regional stability. Besides being an obvious threat in terms of nuclear proliferation and even an environmental threat due to its nuclear activities, North Korea also threatens regional stability due to its refugees, whose estimated numbers in neighbor countries goes around 400,000. The reasons people fled from North Korea vary: there are those who try to escape hunger and those who do it for political or religious reasons. Some neighboring countries, especially China – where around 100,000 North Korean refugees are estimated to hide (Amnesty International 2007a:87) –, prefer to maintain friendly ties with Pyongyang while attempting to avoid massive waves of North Koreans from getting into

4 According to WHO's Health Report 2007, ASEAN "have created international stockpiles of oseltamivir, the antiviral drug that potentially could stop transmission in an early focus of human-to-human transmission." (2007: 51)

the country. For that reason the status of refugee is not easy to get, and many people are sent back to North Korea. Once they are back they receive the proper punishment for their behavior. It is not unusual for punishment to be extended to family members in order to prevent new or repeated escapes (DLA Piper/USCHRNK 2006). If the reasons for escaping were related to poverty and famine, those people are sent to correction camps. As for individuals who fled for political reasons – e.g. asylum seekers or defectors – the punishment is more severe, as they are subject to “indefinite terms of imprisonment and forced labor, confiscation of property, or death” (Haggard and Noland, 2006: 18). North Koreans who manage to stay illegally in other countries face the permanent fear of being sent back.

Myanmar represents another example of a state that, due to its repressive policies towards ethnic or political groups non compliant with the governing elite, not only threatens its own citizens but also disturbs the neighboring countries. For example, children – considering those less than eighteen years old – are being recruited by the National Army and forced to fight ethnic minorities and pro-democracy supporters. According to the Human Rights Watch, recruited children go through intensive physical work and are kept in deplorable conditions; if they fail in their tasks they are also submitted to severe punishments (Human Rights Watch 2007:8). This situation is spreading its scope and having an effect in its neighbor, Thailand, since this country is receiving *Tatmadaw* child deserters. Several reports point to the difficulties for these children to go to a refugee camp, since they fear the reactions of the refugee population, mainly from a different ethnicity and that already suffered *Tatmadaw* abuses; for that reason many choose to live illegally in Thailand. The Amnesty International Report 2007 shows that around 150,000 refugees have remained on the border between Myanmar and Thailand and that there are around 16,000 displaced people in Myanmar’s more populated Karen province (Amnesty International 2007a:28).

Due to their dimension and complexity, these are all issues whose effects states cannot face alone. But unfortunately states alone can worsen their effects and block their resolution. Therefore, it is obvious that human security problems remain entangled, not only in terms of social interconnectedness but also in terms of regional interdependence, a reality that makes it urgent for regional cooperation and, preferably, institutionalization. The problem is that the political regimes of the majority of East Asian countries appear to negatively affect their domestic policies and regional cooperation.

States, Democracy and Asian Values

It seems that in East Asia one can confirm that democratic states not only produce better policies but also tend to better cooperate. Democracies are institutionally predisposed to include issues such as human rights in their political agenda, so their policies become broader, whereas non democracies do the contrary, with leaders seeking to stay in power at the expense of the populations' political and civic rights. Additionally, when one compares democracies with non democracies in the effectiveness of policies that do not concern political-civic issues, such as environment or health, democracies have political accountability mechanisms usually forcing leaders to pursue more effective policies. Unfortunately free countries do not abound and democratization is threatened by cultural manipulations engineered politically by leaders who intend to hold on to their undemocratic chairs.

According to the Freedom House, in 2007 there are only five free countries in East Asia (Japan, South Korea, Taiwan, Mongolia, and Indonesia). The partially free (e.g. Singapore, Malaysia, Philippines) and not free countries (e.g. China, North Korea, Vietnam, Myanmar) are the majority in the region (Freedom House 2007). That classification does not correspond strictly to a democracy index, but it is useful in the sense that goes beyond the formality of regime designation or institutional design that often does not match praxis. As far as promoting human security is concerned, a democratic Japan leads the way since it is part of its foreign policy. Akiko Fukushima (2004) asserts that although formally defending a broad concept of human security, Japan focuses on freedom from want, is shy when it comes to human rights and tries to avoid humanitarian intervention. But despite not being the perfect champion of human security, Japan is surely in the leading group and is demonstrating how a democratic country acts differently amid a majority of non democratic ones, when it comes to human security.

Contrarily to Japan, China shows how an undemocratic state typically behaves when it comes to human security. The difference between discursive make-up and concrete policy is striking. For example, Beijing promotes domestic policies that gravely violate human rights, although it has signed international human rights treaties such as the International Covenant on Economic, Social and Cultural Rights, the Convention on the Elimination of All Forms of Discrimination against Women, the Convention on the Rights of the Child, International Convention on the Elimination of All Forms of Racial Discrimination, Convention against Torture and Other Cruel, Inhuman or

Degrading Treatment or Punishment, the Convention and Protocol relating to the Status of Refugees. Pro-democracy groups, human rights activists, religious groups, women, ethnic minorities, they all face contention by the Chinese officials that seek to keep the regime politically closed while economic openness is promoted. Democracies like Japan, South Korea and Taiwan clearly have a more positive human security record than non democracies like China, North Korea or Myanmar. Even in cases that are not directly related to human rights, countries like China demonstrate less efficient policies, as demonstrated by Chinese environmental and health policies.

As Lee Shin-wha notes, “[i]n democracies, state interests normally reflect the interests and welfare of resident individuals and groups, as well as promoting military defense, the organizational stability of the government and national economic development” (2004: 17). But there are obviously limitations, in the sense that “state interests do not always represent the interests of people and society as a whole, but rather the interests of power holders within the state” (Lee, 2004: 17). If this can happen in a democracy, it is almost endemic in non-democratic regimes.

Democracies produce broader and more effective policies concerning human security. However, the road to democratization in the region has been made difficult not only due to the examples of difficult transitions in Philippines and Indonesia (Acharya 2004), but also due to the Chinese model, which shows undemocratic leaders in the region that political freedom and economic growth do not run side by side, and reinforces the fabricated idea that democracies are not compatible with «Asian values». East Asia should be seen as a vast territory that encompasses many different peoples and cultures but there has been an attempt from several leaders to build a homogeneous region, namely through the concept of Asian values. Claiming the region’s hierarchical legacy – nearly three millennia of Confucianism and Asian values – it is tempting to consider the concepts of social contract and the primacy of the individual as impositions from the West (Tow and Trood 2000). Such interpretations obviously destroy a broad and encompassing concept of human security that includes issues such as human rights. But is that broad interpretation of human security really exclusive to Westerners or are Asians really inherently adverse to such an interpretation?

Asian values were a concept made fashionable by some influential Asian leaders in the early 1990s. Backed by the successful economic development, these leaders defended the idea that there were specific values based on cultural and historical characteristics, which were exclusive to Asia and consequently

much more adequate to Asian societies than the ones imposed by the West. The former prime minister of Singapore, Lee Kuan Yew was one of the most enthusiastic leaders' activists against what they considered to be Western values. Asian values – based upon a set of premises that include above all the respect for community and authority – helped to enforce the idea of the legality of some authoritarian regimes and practices that, to Western eyes, are illiberal (Kim, 2000:294). Thus, it seems easier to link these values to a political effort rather than to a natural reflection of a homogeneous identity.

There are values that should be seen as intrinsic and inalienable to individuals, regardless of their ethnicity, culture, or political regime they live in, such as the freedom from want and freedom from fear. These values are not Western values but universal ones. In response to Lee Kuan Yew's claims of "Asian values", Kim Dae-jung (2001) argues that since culture is not immutable and does not determine the evolution of a society, democratic values can develop within any society and culture. Leaders like Lee use cultural incompatibilities as an excuse to keep their power and limit the democratization of the country. In Asia, such leaders are the main obstacle to the flourishing and strengthening of democratic regimes and the upholding of human rights. Democracy does not need to be seen as an exclusive principle of the «West». As defended by Kim Dae-jung, Asia can be the birthplace of a new democracy based upon its "democracy-oriented philosophies and traditions" (Kim, 2001:98), which can contribute to the overall evolution of global democracy.

According to Aurel Croissant (2004), the Asian continent appears last in terms of democratization. Despite the increasing number of democracies after the third wave of democratization, the fact is that the future of democracy is uncertain and many regimes remain defective – illiberal or semi-liberal democracies that abide to formal procedures of electoral democracies but maintain autocratic features. Between 1972 and 2002, Croissant underlines, the percentage of liberal democracies increased but also the percentage of illiberal democracies (2004).

There are two barriers when dealing with universal principles and distinct cultures: a philosophical one and a material one. In philosophical terms, the difficulty falls mainly on the framework of conception and evolution, i.e. how an agreement about a value can be reached and how to legitimize its subsequent changes. For instance, nowadays we verify that human rights, even the most consensual ones, fail to gather unanimity in their interpretation. Secondly, in material terms, it is very difficult to politically impose the respect for such rights due to the conflict with other principles, such as sovereignty. Even if

a consensus was reached, governments would have the tendency to continue blocking international interferences in their realm. So is there a solution? Based on some of the main ideas of Xiaorong Li (1999), I believe that the solution lies in slowly continuing to promote inter-cultural dialogue in a voluntary quest for a common basis of values and against ethnocentric tendencies or political usage of those values. It is a slow path but the only one available at the moment. Cultural identity must be preserved but it can never be used against the evolution of universal benign values such as human rights, even if reaching unanimity about what is universal and benign encompasses terrible difficulties. Importing democracy from the «West» to East Asia, as it already happened in Japan or South Korea, must be a phenomenon generated internally and must not be considered a neo-colonial phenomenon imposed externally by force (despite the Japanese *sui generis* case), in an evolution towards that form of government that not only offers the best record of domestic respect for human security issues, but is also able to produce more benign outcomes in terms of interstate peace and cooperation.

Culture is definitely important in analyzing political history and institutions, but not endogenously incompatible with specific political principles. It is important to repeat that cultures cannot be considered immutable and absolute values. Even if nowadays certain countries are not culturally open to what is considered a full blown democracy in terms of political and civic rights, there is nothing preventing those countries from eventually embracing such political institutions in the future. It is a question of adaptation.⁵ But one should not forget the warning of Kim Dae-jung, noting that some leaders produce and perpetuate such incompatibilities in order to protect their political power. Culture is essential to sustain democratic institutions, but the leaders must not forget that cultural evolution and political adaptation can be nourished by them, instead of blocked by certain discourses and policies; leaders can positively or negatively influence the path of cultural development. Singapore is an example of blocking, where leaders produce a justificatory narrative in which a strong government in order to prevent chaos and fulfill the expectations of its people's preferences, in accordance to its culture. For them, such a culture (Asian) produces fixed preferences that are not adaptable to westernized democratic values. Lee used Asian values to justify his own governance in Singapore.

Concerning China, its evolution will be essential to determine the evolution of democracy in Asia. If China does not democratize, there is the danger

5 Zakaria's book about illiberal democracies (*The Future of Freedom: Illiberal Democracy at Home and Abroad*) also deals with such aspects of cultural preparation to absorb democratic institutions.

of Beijing promoting the export of its regime, of arguing that the conciliation between an authoritarian regime and a free economy is an alternative to liberal democracy. The appeal of such a regime is obvious to the leaders who want to accumulate power or to those who criticize the social problems or destabilization faced by certain liberal democracies. On the other hand, if the country fully democratizes and evolves towards liberal democracy, it will likely influence other countries in the same direction.

It should be noted that being in favor of democratic values becoming universal does not mean that they should be imposed, since each culture flows in different speeds and depths. Democracies can gradually spread around the globe, but voluntary evolution must be the way. Once again, countries such as the South Korea, Japan and Taiwan can serve as positive examples of Asian countries which have evolved towards liberal democracy, even if some dimensions of these particular political systems still need to be improved. Democratization would improve human security strategies, including those orchestrated through regional cooperation.

Cooperation in East Asia

At this point we can easily affirm that to effectively fight global threats states should cooperate multilaterally – regularly and institutionally. This idea is also defended by Withaya Sucharitanarugse, who declares that “these types of multidimensional problems require multilateral collaboration to generate sufficiently creative and comprehensive solutions” (2000:50-51).

The perception that, in order to fight common threats, it is much more effective to act accordingly and as a group rather than to do it alone can be an important step to an institutionalized regional cooperation. States are still very concerned about their selfish interests but if they conclude that the only way to solve global problems – environmental and health issues for instance – is to cooperate, in the end they will do so. Moreover, the Asian financial crisis of 1997 raised a problem to the region as a whole and raised the awareness that the region needed multilateral mechanisms to deal effectively with such threats (see Kim, 2000). But there are still factors blocking cooperation even in non-political issues. East Asia encompasses states with huge differences that may seem decisive when cooperation is at stake – historical grievances, different regimes, nationalism and lack of shared identity, antagonist ideologies and

religions. Northeast Asia is particularly affected by such obstacles to cooperation (e.g. see Kim 2004).

East Asia regional institutional arrangements such as ASEAN, ASEAN+3 or ARF seem merely a way to maintain a friendly environment between member states and not effective political or security coordination instruments. Furthermore, these arrangements lack any relation to human security issues in their normative and doctrine foundation. (Lee 2003). Nonetheless, East Asian states have been punctually coordinating efforts to deal with specific issues, for instance ASEAN leaders signed joint declarations in weapons matters and the organization has a working group for an ASEAN human rights' mechanism. Several East Asia countries have signed the UN Convention against Transnational Organized Crime and also a Protocol that supplemented it. In order to deal with health issues, specifically SARS, 10 ASEAN members met in Cambodia in June 2003 in order to coordinate efforts to fight the epidemic. But more importantly was the signature of an ASEAN Charter, in November of 2007, that if ratified will provide the organization with what is expected to be its legal and institutional framework and also for the establishment of a regional human rights body. Hopefully this can be a turning point for the region's future cooperation and institutionalization, especially concerning human security issues.

As the concept "human security" is, *per se*, very complex and encompasses several issues that are interconnected, inter-regional epistemic communities can be important to determine political coordination— for instance the Council for Security Cooperation in the Asia Pacific – as they work as interlinkages between issues and also between different perspectives (see Kim 2000). In the 2005 APEC Human Security Seminar, in Japan, it was pointed out that the APEC activities on human security "should complement and support the economic agenda", as well as "avoid negative effects against trade and investment liberalization" through the building capacity on human security.⁶ To conclude, the meeting members states agreed on the importance of include "Human Security" as a "prominent feature of the APEC agenda" complementing and supporting the economic agenda; of developing a common approach and joint programs related to implementing human security; of the agreement on several "human security" areas becoming cooperation areas – Avian influenza, human trafficking and the impact of terrorism on economies; and finally the

6 See MOFA, Japanese Ministry of Foreign Affairs, *APEC Human Security Seminar* www.mofa.go.jp/policy/economy/apec/semminar0510-2.html .

coordination amongst international organizations and avoid duplication⁷. In conclusion, “human security should continue to be recognized as a key APEC component”⁸.

There are issues that remain almost untackled in East Asia, mainly those related to human rights. Unfortunately the lack of regional agreements concerning human rights is notorious. That harsh reality symbolizes how some of the states deal with human rights, the death penalty being an obvious example; and even if the domestic policy is not directly linked to non democracies, as the striking Japanese case proves (Amnesty International 2007a: 153), these regimes surely use it for political purposes. Countries like the Philippines (abolished death penalty in June 2007) and South Korea (has a moratorium concerning it while considering to abolish it) are undoubtedly successes, but one cannot ignore the reality in other states in the region, such as China, Japan, Malaysia, North Korea, Singapore, Thailand and Vietnam. Apparently, to deal with such human rights’ issues under present political conditions will imply small steps towards an increased trust between regional states in order to attain a basis for understanding. Such small steps can derive from the interaction within international institutions, as well as Track I, Track II and Track III encounters (cf. Lee, 2004: 336-337).

In 2006 several East Asian states, such as China, Indonesia, Japan, Malaysia, the Philippines and South Korea became members of the UN Human Rights Council (UNHRC). Although one is tempted to look at the presence of some those states with skepticism, especially China, such institutional interaction can lead to a decrease in mutual regional distrust and boost new forms of regional cooperation. Although Track I inter-governmental encounters in organizations such as ASEAN or APEC are not expected to produce strong cooperation or coordination policies on human rights, the fact that some countries include them in their agenda can at least «institutionalize» a habit of dialogue. Track II encounters, defined by Louise Diamond and John McDonald as diplomatic contacts outside the formal government system⁹, held in academic or semi-official meetings, can also be relevant (see Lee 2003). The East Asia Vision Group was an example of own interaction dynamics can be promoted through these processes. Finally, Track III contacts, involving non-governmental organizations (e.g. Amnesty International, Citizens’ Alliance for North Korean Human Rights), might produce not only a dialogue tradition between different

7 *Ibidem.*

8 *Ibidem.*

9 Quoted by Lee (2003: 337).

actors but also increase the accountability of undemocratic states, even if it does so in an almost imperceptible way.

The fact that regional cooperation in human rights is stalled and, in present political conditions, dependent on a gradual and subtle evolution, the resolution of political crisis as the one affecting Myanmar is obviously hindered. As Amnesty International points out, although the Myanmar issue was on the UN Security Council table, the situation remains unaltered (Amnesty International 2007a:29). It seems that only strong regional institutions could influence these kinds of processes. Could ASEAN play a role in this situation? How about the humanitarian situation in North-Korea, who could address it better if external influence, is seen as according to Lee Shin-wha, a new form of imperialism (2003)? A regional organization would surely be better received by states that are suspicious of «Western» countries or «Westernized» international organizations whose political values they want to export. Undemocratic regimes clearly fear such external interference and would be more open to regional organizations, but the problem is that such regimes are not prone to openness if it might bring their downfall and if they do help to create an organization, they will try to control its actions as they do with internal institutions.

It seems that the ideal scenario would be one in which regional states became democracies and promoted strong regional institutions, or at least a scenario in which a majority of democracies would be able to strengthen existing institutions or create new ones, including in the minority of non democratic states. Both scenarios, especially the former, would not only promote peace in the region (Pevehouse and Russett 2006), but they would also promote cooperation in human security. Due to the democratic peace effect, issues such as WMD proliferation could be better tackled, and given the fact that democracies have broader and more efficient human security policies, cooperation would be strengthened. Ramesh Thakur (2000) correctly observes that human security issues are closely connected to peace, so one can argue that if democracy promotes human security's protection and peace, the democratization of East Asia would be highly desirable.

Conclusion

Human security is an increasingly relevant concept, with the potential to promote a better existence for human beings, but it still lacks the ability to shape the domestic and international behavior of states. States are still the most important political actors, with the highest capacity to influence the lives of populations and regional or global outcomes, so their policies towards their own populations and other states are still the most important mechanisms to tackle human security issues. Although states are governed by leaders with priorities that often clash with several dimension of human security, which explains why so many states fail to protect its citizens internally and to promote international cooperation, the fact is that democracies and international regimes seem to offer the best available solution to the promotion of human security in national and international agendas. Democracies have a broader perception of the concept of human security, their policies tend to be more effective, and international cooperation between democracies can be stronger because of their credibility, whereas international regimes provide conditions for enduring cooperation. Democracies are not perfect promoters of human security and the impact of international regimes is still limited by states' interests, but presently it is as good as it gets.

Following a global trend, states in East Asia have become increasingly aware of human security issues and have shown interest in signing diverse international agreements, mainly global ones. However, state policies are still far from an ideal performance and global agreements face bigger enforcement problems. State policies in the region seem to corroborate the assumption that democracies promote broader and more effective policies, with Japan leading the way and South Korea coming right behind. At the opposite end of the spectrum, North Korea continues its poor performance and even the economic security of its population, so theoretically defended by the communists, is outrageously threatened. East Asia has few strong democracies and is populated with non free and partially free countries, which explains the negative performances of countries such as North Korea, China, Myanmar or Vietnam. On the other hand, regional cooperation has been increasing under institutions such as ASEAN, but the commitment of states continues limited, especially when it comes to political and civic liberties issues. Democratization in the region is still threatened by certain interpretations of Asian values and by the Chinese model, but the solution for promoting broader and more efficient national policies, as well as cooperation, seems to lie in democracy and international regimes.

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