A Tale of Two Asias

In the battle for Asia’s soul, which side will win -- security or economics?

BY EVAN A. FEIGENBAUM, ROBERT A. MANNING | OCTOBER 31, 2012

Whatever happened to the "Asian Century?" In recent months, two Asias, wholly incompatible, have emerged in stark relief.

There is "Economic Asia," the Dr. Jekyll — a dynamic, integrated Asia with 53 percent of its trade now being conducted within the region itself, and a $19 trillion regional economy that has become an engine of global growth.

And then there is "Security Asia," the veritable Mr. Hyde — a dysfunctional region of mistrustful powers, prone to nationalism and irredentism, escalating their territorial disputes over tiny rocks and shoals, and arming for conflict.

In today’s Asia, economics and security no longer run in parallel lines. In fact, they are almost completely in collision.

In the one domain, Asian economies have come in recent years to depend increasingly on China — and one another — for trade, investment, and markets. And this trend toward regional economic integration has been reinforced over the last four years by austerity in Europe and slow growth in the United States. But these same economies now trade nationalist barbs, build navies, and acquire new arms and power projection capabilities. With the exception of China, all major Asian states, though their economies are increasingly integrated within Asia, are tacking hard across the Pacific toward the United States for their security.

So much for the new East Asian community of which many in Asia have dreamed.
What explains the change? Put bluntly, Economic Asia and Security Asia have become increasingly irreconcilable. But where Economic Asia was winning the contest in the decade and a half after the Asian financial crisis of 1997-98, Security Asia has begun to overwhelm those recent trends.

Indeed, so powerful was the rise of Economic Asia that it had challenged even the longstanding American role in the region. Intra-Asian trade and investment took off fast with the end of the Cold War, but Asia’s growing web of economic and political connections was particularly reinforced by the 1997-98 financial crisis, which hit hardest in places like Indonesia and Thailand. Across the region, elites came to view the United States as arrogant and aloof, and groped for their own solutions to regional economic challenges. The United States, which bailed out Mexico in 1994, refused to bail out Thailand just three years later, fueling perceptions that it neglected Southeast Asia. To many in Asia, Washington appeared to be dictating clichéd solutions. And, in the ensuing years, preferential trade agreements, regionally based regulations and standards, and institutions created without American involvement advanced. These have threatened to marginalize the United States over time.

But after two years of nationalistic rhetoric over rocks and islets in the East and South China Seas, Security Asia has roared back. Rampant and competing 19th and 20th-century nationalisms have moved again to the fore as pathologies that seemed frozen in time raise the specter of renewed conflict. A recent study from the Center for Strategic and International Studies reports that defense spending in China, Japan, India, South Korea, and Taiwan has doubled in the past decade, reaching $224 billion last year. Asians have worked for decades to develop a pan-Asian identity and enhance their collective clout in the global system. But economic integration has thus far yielded no basis for collective or cooperative security in the Pacific. Instead, the world’s new center of economic gravity looks fragile and conflicted.

**Politics Unbound?**

Could Security Asia actually overwhelm, or even destroy, the economic gains that were beginning to pull the region away from its debilitating past? Some have argued that this is a temporary phenomenon — a cynical ploy by Asia’s politicians to build support at a time of domestic weakness.
But it is too easy to write off these recent developments as the product of domestic politics. Yes, China, Japan, South Korea, and Vietnam, among others, are focused on internal economic or political developments. Seoul, for example, is in the midst of a presidential campaign. Japan’s governing party faces a stiff test, and probable defeat, at the hands of a resurgent Liberal Democratic Party next year. China is in the midst of a once-in-a-decade political succession, and, what is more, Beijing has hit the upper limit of its existing growth model, which is delivering diminishing returns and threatens to become a major political vulnerability for the government. Vietnam and others in Southeast Asia face domestic pressures to supercharge their economies and reinvigorate reforms.

Yet while it is true that popular chauvinism is a useful tactic for Asia’s beleaguered politicians, such tactics will yield significant costs and enduring damage. Nor are such passions easily turned on and off. Economic and political nationalism is deeply rooted in all Asian countries. It will survive and thrive even after these various political transitions are complete.

Just take the Vietnam-China relationship. Nayan Chanda wrote in his classic history of Indochina, *Brother Enemy*, that events after the fall of Saigon demonstrated that "Instead of being the cutting edge of Chinese Communist expansion in Asia that U.S. planners had anticipated, Vietnam proved to be China’s most bitter rival and foe."

"History and nationalism, not ideology," he noted, powerfully shape Asia’s future.

Just as these nationalisms threatened ideologies of Communist solidarity in the late 1970s, so do they now threaten ideologies of pan-Asian integration. Economic Asia is increasingly at risk.

Look, for example, at the recent events in China: As protestors took to the streets this fall in dozens of Chinese cities, Japanese businesses were attacked, thousands of China-Japan flights were canceled, and Honda, Toyota, Panasonic, and other popular Japanese brands closed factories. Sales of Japanese cars in China fell nearly 30 percent in September. The Chinese government, which aspires to a prominent role in international institutions, allowed nationalist passions to overwhelm expansive global ambitions: Beijing scaled back its participation in the 2012 Annual Meetings of the International Monetary Fund and World Bank simply because they were held in Japan.
The ghosts of history are visible elsewhere too. South Korea and Japan have traded nationalist recriminations over even tinier rocky islets. The result is that America’s Northeast Asian allies, despite a robust trade relationship and a powerful shared interest in countering North Korean threats, could not sign even a straightforward intelligence-sharing agreement to enhance cooperation in the face of a common threat from Pyongyang.

**Asia’s Schizophrenia**

Such developments belie much of what has been written about Asia’s recent evolution. Many have argued, for instance, that Japanese strategy is now motivated principally by *realpolitik* instincts — specifically a desire to balance rising Chinese power. But if this is true, then it is difficult to understand Tokyo’s festering spat with South Korea.

What is more, Tokyo has long been an exemplar of Economic Asia and a motive force behind the quest for greater regional economic integration. Postwar Japan, a strong U.S. ally with a powerful sense of trans-Pacific identity, has incubated a variety of pan-Asian regional ideas and ideologies, especially with respect to Asian monetary integration. It was Japanese officials who in 1997 proposed the establishment of an Asian Monetary Fund, which helped give rise to today’s Chiang Mai Initiative of bilateral swaps among ASEAN Plus Three countries (the ten Southeast Asian members of ASEAN, plus China, Japan, and South Korea). And it was Junichiro Koizumi, a prime minister with especially robust ties to the United States, who helped to push forward a China-Japan-South Korea trilateral mechanism and, with a competitive eye on China, other trade arrangements on the basis of ASEAN Plus Three.
Amazingly, even amid this autumn's high geopolitical drama over contested islets, talks among Beijing, Tokyo, and Seoul for a trilateral free trade agreement rolled along. The same phenomenon can be seen in Southeast Asia. As fears of confrontation rose last summer, ASEAN Plus Three, which includes the South China Sea’s three most vocal antagonists (China, Vietnam, and the Philippines), announced a strengthening of the Chiang Mai initiative through pledges that double the arrangement’s size to $240 billion in the event of another financial crisis and the establishment of an implementation office. In November, ASEAN and six partners (Australia, China, India, Japan, New Zealand, and South Korea) launched negotiations for a Regional Comprehensive Economic Partnership that could be worth $17 trillion in trade and will be a counterpoint to Washington’s preferred pact, the Trans-Pacific Partnership (TPP).

**Strategic Dilemmas**

It is difficult to avoid analogies to Europe in 1914. Norman Angell’s 1910 bestseller, *The Great Illusion*, argued that war would prove impossible because Western economies were so interdependent as to make conflict suicidal. But Thucydides’ rationales why men go to war — interest, honor, and fear — have tended to prevail in international history.

The current push and pull between Economic Asia and Security Asia thus raises a number of powerful questions.

For one, Asia’s major multilateral institutions have proved to be almost irrelevant to practical problem-solving. Is it, therefore, time to rethink these experiments in regional architecture?

Pan-Asian regionalism has failed to quell Asia’s nationalist demons, and existing institutions, including those that involve the United States, have been largely missing in action throughout the turmoil of recent years. Last summer, ASEAN cohesion collapsed at a meeting in Phnom Penh, with the Cambodian chair at loggerheads with Vietnam and the Philippines over how sharply to confront Beijing. The new East Asia Summit (EAS) has done nothing to consolidate an agenda in between its annual meetings. And the ASEAN Regional Forum (ARF) has, similarly, become an arena for accusations and counterclaims. Indeed, the ARF is perhaps the most pregnant example of institutional failure. ARF is Asia’s leading security forum, yet all of the major sources of prospective conflict — Korea, Asian maritime claims, China-Taiwan, and India-Pakistan — are largely off the table.
Revisiting Asia’s regional institutions could help to fashion mechanisms better able to address the real problems while buttressing the U.S. position. Inertia and "process-centered" rituals continue to predominate at regional meetings. Diplomats rack up frequent flyer miles but little else.

Certainly, it can be useful for heads of state to meet regularly. But it would be wise for a group of like-minded countries, including the United States, to think through a modest but substantive operational agenda for the next EAS meeting to decide priority issues. Then, depending on the issue, leaders could ask that ARF or the Asia Pacific Economic Cooperation (APEC) forum, or another relevant body, follow up with practical actions. This would begin to inject greater relevance into regional institutions and more connectivity among them.

**Whither Washington?**

A second question concerns the American role in Asia.

The U.S. role as Asia's security provider has been reinforced even as the region's economy has become increasingly pan-Asian, with the U.S. role shrinking in relative terms. This begs the question of whether the U.S. security role is sustainable without a significantly increased American economic profile in Asia, not to mention substantially greater leadership from Washington in driving regional trade and investment arrangements.

At present, Washington faces two strategic dilemmas:

First, the triumph of Security Asia would benefit the United States by assuring its centrality. After all, Washington is Asia's essential strategic balancer and is becoming more so against the backdrop of growing Chinese naval power and projection capabilities. The dilemma, then, is that a security-dominant Asia will, at the same time, be a vastly more volatile region. And such volatility and instability are precisely what the United States has worked for two decades to avoid.
Washington could find itself navigating uncomfortably between competing territorial claimants. It will find it difficult to avoid choosing sides not just on matters of principle, such as freedom of navigation, but also on this or that specific sovereignty claim — for example, in the South China Sea between China and the Southeast Asian countries whom it has courted (some of whom have disputed claims with one another). An American president could ultimately find himself pulled into a military conflict over tiny shoals to which the United States has no claim.

A second dilemma is that Americans seek a stable, dynamic Pacific Rim for the long term and, in that sense, need Economic Asia to prevail. But economically, Asia is increasingly pan-Asian, meaning that American centrality could actually shrink as trade and investment patterns come to further reflect intra-Asian economic and financial integration.

U.S. economic involvement in Asia is growing in absolute terms but receding in relative terms. Trade with the United States comprises a diminishing share of nearly every East Asian country’s total trade. Yet the U.S. response has been deeply inadequate. Thus far, Washington has focused mainly on security "rebalancing" to the exclusion of economic rebalancing. Asians are providing ever more economic public goods to one another, while the U.S. role in this sphere has ebbed.

If present trends persist, America will only continue to recede. Thus the United States needs to raise its economic game in the region. And that will require revitalizing the U.S. economy and fiscal fundamentals. More than any factor, these could make a difference in demonstrating that the United States has staying power in Asia for the long term.

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If history is any guide, it may take a crisis or game-changing shift for Asia to move more fully onto the positive path of Dr. Jekyll. Greater American involvement with Economic Asia will help. But there are few scenarios likely to produce a more dramatic shift through which Economic Asia could overwhelm Security Asia.
If China stumbles in its efforts to rebalance its economy, concerns will mount that China is falling into the middle-income trap, potentially risking its political stability. That could bring Asians together through a shared interest in avoiding a downward spiral in China. Similarly, a sudden collapse of North Korea could threaten all of Asia, precipitating a sobering crisis and leading nervous Northeast Asians to work together to manage the transition to a reunified Korea.

But Dr. Jekyll faces a very uphill battle. Even under such dramatic scenarios, nationalistic responses could ensue, leading Mr. Hyde to prevail.
Different in Asia?
Developmental states, trade, and international conflict onset and escalation

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Abstract

In this article, I ask what might be the effect of international trade on interstate conflict in Asia and the Pacific. Overall, the associations of trade interdependence and trade volume in the region appear similar to those globally: interdependence is accompanied by a reduction in the chance of militarized conflict onset, whereas the volume of trade appears to reduce the chance of conflict escalation to deadly international violence. I suggest a partial exception for East Asia, implying weaker associations between trade and pacific outcomes. I argue that the regionally common ‘developmental state’ model allows such states to more freely, but less credibly, use trade as a foreign policy tool, reducing trade’s constraint upon East Asian states in security affairs. Analyses of East Asian dyads and of developmental states in data from all regions of the globe support my contention that trade...
interdependence has weaker pacific effects in these contexts, although some other expectations are not supported.

In this article, I apply a framework for thinking about the relationship between international trade and interstate conflict onset and escalation that incorporates distinct roles for trade volume and trade interdependence. I focus on the implications of such an approach for understanding trade–conflict dynamics in the broad Asia and Pacific region. The region, especially East Asia, is interesting to study from this perspective for at least two reasons. First, the amount of intraregional trade has expanded greatly since about 1980 (Wu, 2007; Asian Development Bank, 2009), roughly coinciding with the changes introduced by Deng Xiaoping to Chinese domestic and international economic relations beginning in 1979. This corresponds with a regional drop in interstate war and deadly conflict in the region (Tønnesson, 2009). Second, Asian states, especially those in Northeast and Southeast Asia, are often considered to have a distinctive trade-based recipe for development, based on export-led growth with a large role for the strategic choices of the state, usually called the ‘developmental state’ model (Johnson, 1982; Amsden, 1989). I do find some difference in the trade–conflict dynamics in East Asia, and one motivation for this study is to identify a variable that explains this difference and may be substituted for the proper name ‘East Asia’ (Przeworski and Teune, 1970, p. 8). The developmental state model appears to be such a variable.¹

In the rest of the article, I first briefly discuss the concepts of interdependence and volume as aspects of trade that might be considered distinct in their relationship with international conflict. I pay special attention to how the developmental state model might interact with these two aspects of trade. I next discuss measures and methods, and then present results for a series of probit selection models that examine my propositions. I summarize conclusions in the final section of the article.

1 Trade interdependence and trade volume²

This section draws on bargaining models of war (Fearon, 1995; Reiter, 2003) to consider how trade volume and interdependence might relate to

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¹ Replication files for the statistical analysis are available here: http.
² Parts of sections discussing general hypotheses and methodological choices are based on Goldsmith (2013).
international conflict. Trade volume is defined as the total amount of exports and imports between any pair of countries (or ‘dyad’). Trade dependence is the relative importance of that trade for each country, based on its share of the country’s gross domestic product (GDP). Interdependence refers to the degree of mutual dependence on the trade relationship for each country in a dyad – when levels of dependence for both states are relatively high, interdependence is also high.

Bargaining models understand interstate conflict as a process of strategic interaction. Two crucial points in this process are (i) the initial challenge leading to a dispute, and (ii) the subsequent choice for escalating or defusing the crisis, usually considered as leading to war, or peace, between the states involved. A central insight is the idea that, given full information and certainty, war is irrational. Fearon (1995) provides a seminal example of such models, considering the implications of private information and uncertainty. If states are able to credibly signal their levels of capability and resolve to fight, then through bargaining they can reach a mutually acceptable agreement while avoiding the extra costs of war. However, because states have incentives to bluff and exaggerate, credible and effective communication is problematic. War ensues due to uncertainty over its likely outcome, and is only resolved once the side that is likely to lose clearly recognizes its position (Reiter, 2003).

Thinking about the role of international trade in this process should therefore focus on how it might affect leaders’ perceptions of the costs of war, and how it might affect the communication process regarding uncertainty over intentions and resolve.

1.1 Interdependence

As both a signaling tool and a representation of state-level opportunity costs, trade interdependence has qualities that might reduce the likelihood of conflict onset. This is so because putting trade at risk implies that leaders have the resolve to suffer the domestic costs incurred if that trade is actually lost in conflict with the trading partner. The likelihood of significant domestic political costs makes the trade-based signal credible (Fearon, 1995, 1997). Regarding conflict onset, Crescenzi (2003) considers how contentious interchanges over trade before a militarized crisis might be consistent with a negative (pacific) effect of interdependence on the subsequent emergence of a militarized dispute, because they
facilitate communication about resolve. As Gartzke et al. (2001, p. 400) put it ‘interdependence makes it easier to substitute nonviolent contests for militarized disputes in signalling resolve.’

At the stage of escalation to serious violent conflict, bargaining theories may point to the further ability of interdependent states to credibly signal their resolve during a crisis through placing trade at risk (Morrow, 1999, p. 487). However, I argue that this does not fully consider the selection dynamics of the conflict onset stage (see also Goldsmith, 2013). Trade-based economic interdependence for the state and its adversary are likely to be observable at the conflict onset stage, and thus fully considered by each state. Interdependence should not play a major role in the escalation stage, because the potential costs to oneself and the adversary of risking that trade have already been ‘priced in’ to the calculations of each side. The signals have already been sent. These arguments lead to two hypotheses.

General hypotheses about trade interdependence:

Hypothesis 1: higher dyadic trade interdependence will have a negative effect on interstate conflict onset.

Hypothesis 2: higher dyadic trade interdependence will have no effect on interstate conflict escalation to more serious violence.

1.2 Volume

Another way of measuring dyadic trade is to consider the value of trade flows in absolute terms, rather than proportional to the overall economy of each state. I suggest that more trade may increase the chance of conflict onset, even if resolve for escalation to war is low. For example, trade volume, even if not implying high dependence, is especially attractive for signaling at low levels of conflict because it has qualities that are appealing for leaders looking for ‘bargaining chips’ which are not obvious as such to opponents. It often represents interests that are valuable enough not to be dismissed as cheap talk or bluff by an opponent, but also not vital enough to defend at all costs. A trade-related issue might also arise

3 But see also Morrow (1999, p. 485) who argues that the overall effect of interdependence on conflict onset is ‘indeterminate.’

4 In the hypotheses and analysis, I use language-implying causation because of the strength of theory and evidence cumulated in the literature I cite (and in this article), although I acknowledge the caveat that ‘effects’ are never certain in observational data.
based on the interests of the sub-state actors involved, such as firms, even though national leaders are unwilling to actually go to war over the issues. Controlling for the degree of state-level dependence, more traded goods or higher values of goods could provide more points of potential conflict. Realist thinkers in international relations, such as Gilpin (1987, p. 172) and Waltz (1979, p. 138), highlight that trade among states may serve both as a conduit for signaling dissatisfaction on other issue areas, and as a set of issues which might themselves lead to conflict.

But the absolute volume of trade could also be relevant for bargaining to avert escalation to violent conflict. As suggested, it might often be the case that the degree of the state’s overall interdependence was factored into the decision when the state selected itself into the conflict onset stage (either by initiating the conflict, or by not conceding the issue at stake before the disagreement became militarized). In such circumstances, interdependence would not play a significant role in further decisions about escalation. Trade issues leading to disputes will also have already been raised, by definition. But dramatic bargaining gestures involving large amounts of trade, or specific goods perceived to be of special importance, either as concessions or as further threats to signal a higher level of resolve than previously perceived, could help defuse the crisis. Because signals regarding interdependence levels will have already been perceived at the conflict onset stage, high-volume trade relationships might provide further signaling tools using valuable, dramatic gestures regarding high-profile aspects of the trade relationship: the more and larger the trade issues available to each state for signaling, the more likely that states can effectively communicate their preferences to avoid war, or signal their resolve to fight. Perceptual factors can be important in international conflict dynamics, over and above the actual economic value of a good or set of goods to the overall economy (Jervis, 1976). Such tools should be more available when the overall amount of trade is high, and scarce if the overall amount of trade is low.5

5 This argument might be usefully expanded to consider specific types of goods (Dorussen 2006), or the degree to which firms are globalized (Brooks 2005), but my argument does not hinge on them. If they exist, my empirical analyses would tend to underestimate the effect of relevant firms or states, given that irrelevant firms’/states’ trade is included in the general trade data.
General hypotheses regarding trade volume:
Hypothesis 3: higher dyadic trade volume will have a positive effect on the onset of interstate conflict.
Hypothesis 4: higher dyadic trade volume will have a negative effect on the chance of interstate conflict escalation to more serious violence.

1.3 East Asian states and trade signaling
My expectations regarding East Asia are based on the centrality of trade, especially exports, to the developmental state model, and on the close connections between political and economic elites in states adopting the model. The model’s core tenets originate with Johnson (1982) and are summarized well by Leftwich (1995), Önis (1991), and Woo-Cummings (1999). Leftwich (1995, p. 405) lists the ‘six major components’ of the concept: ‘(i) a determined developmental elite; (ii) relative [state] autonomy; (iii) a powerful, competent, and insulated economic bureaucracy; (iv) a weak and subordinated civil society; (v) the effective management of non-state economic interests; [and] (vi) repression, legitimacy, and performance.’

I argue that such a political-economic system would lead to the expectation that, other things equal, trade will be less potent as a signaling device for East Asian developmental states. Signaling logic depends on the existence of domestic constituencies able to impose costs on foreign policy decision makers. However, East Asian developmental states have constituencies with weaker abilities to impose costs. Civil society is especially weak, and business elites are not truly autonomous from the political and bureaucratic decision makers; rather there are ‘extraordinary degrees of elite unity’ (Önis, 1991, p. 115), whereas the state is relatively autonomous from sub-national pressure.

In such circumstances, signaling based on risking the loss of trade for the state would be seen by adversary states as incurring relatively fewer domestic costs, and more likely to be a bargaining tactic. Business elites will probably go along with, and may be complicit in, the overall conflict strategy if trade has come into the bargaining process. This will tend to reduce the pacific effect on conflict onset of overall economic interdependence, because the lower-cost signals sent will seem less credible. Thailand and Cambodia, for example, have experienced a series of
militarized disputes since 2008, over the contested status of a temple on their border, in spite of their relatively high trade interdependence.

However, the amount of trade between two countries might further increase the chance of a dispute arising. While less able to use trade to credibly signal resolve, relatively autonomous East Asian developmental states will be freer to raise high-profile or high-value trade issues in the conflict bargaining process, regardless of whether firms or other societal actors (e.g., labor unions) find such behavior in their interests. They will therefore be free to link them to other contentious issues in relations with other states. Thus, relative to other states, specific amounts of trade, or traded goods, will be somewhat more likely to be sources of dispute onsets for East Asian states. In the context of ongoing territorial disagreements in 2002, for example, Singapore refused to pay a higher price for Malaysian water than their contract required. Malaysia’s Prime Minister Mahathir then stated publicly ‘according to the agreement, we must supply them with water – unless we go to war with them’ (BBC 6 August 2002).

But high trade volume may also be somewhat less likely to provide useful tools for avoiding conflict escalation to violence because of the lower domestic political costs. Developmental states will have easier access to trade issues during conflict, but these trade issues will be relatively less credible as signals which might help avert conflict escalation. Returning to the example of the Thai–Cambodian border dispute, in spite of relatively high trade volumes ($1 billion in 2008, and a reported further $900 million in unofficial trade along border areas) and attempts from the Thai side especially to use cross-border flows and trade-related loans to defuse tensions, it has escalated to a shooting conflict involving soldiers’ deaths (although never approaching the 250-death threshold used in the analyses in this article) several times (The Bangkok Post, 16 October 2008, 31 January 2009, 11 June 2009).

In the empirical analysis that follows, I test the hypotheses that stem from these arguments on two types of dyads: those including two East Asian states, and those including at least one developmental state in any region. This is appropriate because, while my logic hinges on the characteristics of developmental states, there may be states in East Asia that adopt many of its important aspects, but are not categorized as fully fitting the model. For example, neither Vietnam, Cambodia, nor the Philippines is categorized as developmental for any period (see below).
Cross-regional analysis is potentially useful when different models of political economy have been adopted by diffusion or other processes (e.g., ‘flying geese’ or more nuanced processes, e.g., Bernard and Ravenhill, 1995) in different regions. On the other hand, some countries outside of East Asia, such as Botswana and Finland, have been categorized as developmental states for parts of their history. My expectations should therefore be tested against their patterns of conflict behavior, so I also present analysis for intraregional dyads including at least one developmental state in any region of the world. Hypotheses finding support in analysis with both types of dyad will deserve greater confidence.

East Asia/developmental state hypotheses:

Hypothesis 5: for East Asian dyads (developmental states), higher dyadic trade interdependence will have a pacific effect on interstate conflict onset, but of less magnitude than for other types of dyads.

Hypothesis 6: for East Asian dyads (developmental states), higher dyadic trade interdependence will have no effect on interstate conflict escalation to more serious violence (the same as hypothesis 2).

Hypothesis 7: for East Asian dyads (developmental states), higher dyadic trade volume will have a positive effect on the onset of interstate conflict, but of greater magnitude than for other types of dyads.

Hypothesis 8: for East Asian dyads (developmental states), higher dyadic trade volume will have a pacific effect on the chance of interstate conflict escalation to more serious violence, but of less magnitude than for other types of dyads.

2 Measures and methods

In this section, I discuss measures and statistical methods used to test the hypotheses. Pooled dyadic annual time-series data are used (notation omits time indicators for clarity). Some variables are further described in the appendix.

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6 Models similar to 4 and 7 using an indicator of dyads of two developmental states fail to produce valid results due to the small number of such dyads. However, my hypotheses do not require that both states in a dyad be developmental.
2.1 Measures of trade and conflict

GDP share is the proportion of country $i$'s GDP that is represented by trade with a particular country $j$.

$$\text{GDPshare}_{ij} = \frac{\text{imports}_{ij} + \text{exports}_{ij}}{\text{GDP}_i}.$$ 

Once this is calculated, for each dyad $ij$, the lower of the two values of GDPshare is chosen, using the weak-link logic (Dixon, 1994) that the least dependent state (largest GDP) represents the effective level of interdependence (GDPshare$_{\text{lower}ij}$).

The volume of trade is simply the sum of imports and exports within a dyad for a given year, in constant inflation-adjusted dollars.

$$\text{Trade volume}_{ij} = \text{imports}_{ij} + \text{exports}_{ij}.$$ 

It is important to note that there is not a high degree of empirical correlation between trade volume and interdependence ($r = 0.293$ for Trade volume$_{(ln)}$ and GDPshare$_{\text{lower}}$). This is so because weak-link interdependence is proportional and hinges on the size of the larger state in the dyad, whereas trade volume is a function of both economies in the dyad, and not proportional.

My operationalization of international conflict involves measuring both the onset of a militarized dispute, and the escalation of some disputes to levels of serious interstate violence. I use all militarized interstate disputes (MIDs) in the correlates of war (COW) dataset, for the years 1951–2001 (1961–2001 for some analyses), coding all years in which a MID was initiated within a dyad as 1 (MID data end in 2001). A MID involves a threat, show, or use of force by one state, directed at the other. Dyad-years of MID continuation are dropped, and all other non-MID dyad-years are coded 0. I create an indicator for MIDs which escalate, eventually incurring over 250 battle-related deaths, coding an escalation variable 1 for dyad-years involving the onset of such a MID, all subsequent years for those MIDs are dropped, and all years with no such serious MID are coded 0.

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7 All intraregional dyads, 1950–2000. Without the logarithmic transformation for Trade volume, this is 0.344.
Descriptive statistics for all such MIDs in the Asia–Pacific, as well as GDP share and trade volume are presented in Table A1, for dyad-years experiencing ‘fatal’ MID onsets which incur at least one battle death, along with counts for fatal MIDs with over 250 battle deaths, and MIDs incurring 1000 or more deaths. The analyses rely only on the escalation threshold of over 250 deaths, because available MID incident data, 1992–2001, indicate that no MIDs begin with an incident involving that many deaths. This reinforces the assumed escalation process reflected in the statistical models, while providing the greatest possible variation in the dependent variable. The conflict indicators are measured 1951–2001, one year after the independent variables (1950–2000) to support causal inference. Given my focus on the bargaining process of MID onset and escalation, I drop ‘joiners’ – states that were not involved on day one of the MID onset – from the analysis.

I also include a number of control variables likely to be associated with both trade and conflict. Alliances are one such factor. I use Signorino and Ritter’s (1999) alliance portfolio similarity statistic, $S$ (alliance ties ‘$S$’), weighted by global share of military capabilities. This is also an important control because it helps account for the role of extra-regional great powers, such as the United States or the Soviet Union for Asia, in conflict dynamics among intraregional dyads.

Xiang et al. (2007) show that omission of a variable accounting for power (states’ military capabilities) has the potential to bias trade and conflict models. The military capabilities of each state (as measured by COW’s composite index of national capabilities) is an important control for this study because it is related to economic size, and thus to the potential trade volume of states. I create a dyadic indicator by adding them, then taking the natural log.

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8 See Goldsmith (2013) for detailed discussion based on data from Ghosn et al. (2004), and robustness checks.

9 South Vietnam is coded as a joiner for the MID with North Vietnam beginning in 1964, and thus this conflict is not included in the results presented here. This dyad did have a fatal MID in 1960 (see Table A1). In the MID data, the primary parties to the Vietnam War are the United States and North Vietnam. However, if the north–south dyad is re-coded as a primary party with a MID onset in 1964 that escalates to war, then the results presented here are not substantively affected. The only change in statistical significance for the trade variables is that the negative association with MID escalation of the interaction term for Tradevolume and East Asia becomes significant at the 90% level in model 3.

10 I add a very small number, 0.000001, to the sum of dyadic CINC scores to avoid zero values before taking the natural log.
Regime type and geographic distance are also important controls. In the conflict onset stage, I use two indicators of dyadic regime type, measuring the degree of joint democracy in the dyad and the existence of a jointly authoritarian dyad as separate factors (Goldsmith et al., 2008). I include distance (natural log of miles between capitals) and contiguity. I also include a cubic polynomial for peace years (number of years since the dyad’s last MID) to account for temporal dependence (Carter and Signorino, 2010).

To identify the escalation stage, variables included are trade volume and trade interdependence – the focus of this study – and also total dyadic power capabilities and joint autocracy. Dyadic power is included again to guard against the overestimation of the effect of trade volume at this stage. Joint autocracy is included because, whereas there is little theory to guide expectations, it is possible that autocratic leaders are less constrained by audience costs or other factors than leaders in less centralized regimes. Given that conflict among autocracies is less likely, those that do experience it might be especially resolved to pursue the issues at stake, and thus especially likely to escalate. Such high resolve and low constraint might not be observed by adversaries at the conflict onset stage, even though they are aware of the regime type of the state, due to the closed nature of fully autocratic states’ decision making.

Dyads in East Asia, Asia and the Pacific, and other regions are coded using dichotomous (dummy) indicators. I limit the regional analyses to the period 1961–2001, because prior to this, there were relatively few states categorized as developmental in East Asia. I also use several indicators to assess the robustness of my findings to alternative hypotheses. These include territorial conflicts, dyads with free-trade practices, dyads sharing membership in regional integration arrangements (RIAs), and dyads sharing memberships in all types of international governmental organizations (IGOs).

As noted, I also create an indicator for dyads including at least one developmental state based on the literature on this topic. This is appropriate because not all East Asian states, even after 1960, can be considered ‘developmental,’ and there are a number of states outside of East Asia.

11 Including distance and contiguity is important because capital cities might be quite far, although two states share a border. For example, China and Vietnam border each other, although their capitals are over 2,000 miles apart.
Asia categorized in the existing literature as developmental. In fact, according to my coding detailed below, while 67% of 5,497 East Asian dyad years, 1950–2000, \(^{12}\) include at least one developmental state, these represent only 33% of all 11,262 dyad years containing at least one developmental state in intraregional data for that period. The remaining 7,574 developmental state dyad years include 4,632 (41%) comprising one East Asian and one other Asia–Pacific state, and 2,942 (26%) comprising states outside of the Asia and Pacific region altogether.

I define Asia and the Pacific as the wide region, including Oceania/Australasia, South, Central, Southeast, and Northeast Asia. I define East Asia as Southeast and Northeast Asia. Specifically, Cambodia, China, Indonesia, Japan, Laos, Malaysia, Myanmar, North Korea, Philippines, Republic of Vietnam, Singapore, South Korea, Taiwan, Thailand, and Vietnam (Socialist Republic of Vietnam). Thus, East Asia is a sub-region of Asia and the Pacific. In the analyses, I compare East Asian dyads (for which both states are in East Asia) with dyads in other parts of Asia and the Pacific (not including East Asia). I also compare both groups with all other intraregional dyads globally. The other regions for which dyads are pooled in these analyses are Latin America, the West (Europe and North America), Sub-Saharan Africa, and the Middle East and Northern Africa. Interregional dyads (e.g., Bolivia and Laos, or the United States and Vietnam) are excluded from the analysis because they are less appropriate for comparison with East Asian dyads or other sets of intraregional dyads: they take considerably lower values for trade and all other variables in the models (except, of course, distance), and they have a much lower likelihood of conflict.

Based on the developmental state literature, I coded the following states as ‘developmental’ for the periods indicated: Japan (1925–), Taiwan (1949–), France (1945–85), Austria (1950–79), Finland (1950–79), Malaysia (1957–), Thailand (1958–), South Korea (1960–), Singapore (1965–), Botswana (1966–), Indonesia (1966–), People’s Republic of China (1979–). Sources are noted in the appendix.\(^ {13}\) I now turn to a discussion of the choice of econometric method for assessing support for my hypotheses.

\(^{12}\) This rises to 72% of 4,725 for the period 1960–2000.

\(^{13}\) I also acknowledge the useful study of Kivimäki and Kivimäki (2011), but do not fully concur with its coding of developmental states.
2.2 Econometric models

The analysis relies on a Heckman (1976) selection estimator for probit models, because the conflict escalation process might be vulnerable to selection bias. This occurs when there is a relationship between the factors causing a case to enter a sample, and the factors associated with the outcome to be studied.

A key insight of bargaining models of war is that international conflict analysis can suffer from selection bias. For example, both resolve and military capabilities are important for conflict onset as well as escalation. As Fearon (2002, pp. 6–7) writes ‘Rational challengers select themselves into crises according to their prior beliefs about the defender’s willingness to resist with force. To the extent that this occurs, the crises in which defenders’ immediate deterrent threats are most credible will tend to be crises in which the challenging states are relatively strongly motivated to change the status quo, and thus willing to accept an appreciable risk of conflict. Hence despite their credibility compared to immediate deterrent threats in other cases, defender threats in this subset are less likely to succeed.’ Other studies using selection models to examine escalation using MID data include Bennett and Stam (2004, pp. 30, 117, 219) and Braithwaite and Lemke (2011).

Huth and Allee (2002, pp. 35–36) raise another relevant issue. In dyadic time-series studies of international conflict, the possibility for theoretically irrelevant but statistically significant findings exists due to the rarity of conflict, and lack of much basis for conflict within many dyads. However, to assess the effects of international trade, it is preferable to include all dyads, because even smaller non-contiguous states often trade with each other. Including relevant control variables is one approach suggested by Huth and Allee, and these are included in the models. The regional approach of this article further helps focus analysis on proximate, relevant dyads. A selection model also provides a check: in the second stage of the process, states that have selected themselves into militarized conflict represent a small and relevant subset, and the possibility of escalation is logically strong.

In the analyses that follow, I first present models including all intraregional data, and using interaction terms for Asia and Pacific (excluding East Asia) dyads, East Asian dyads, and dyads containing at least one developmental state, to assess whether there is a difference in the
trade–conflict relationship between these groups and all other intraregional dyads in the world. I then proceed to models including only dyads for each group. I also discuss a number of robustness checks. Finally, I present estimates of the substantive impact of trade volume and interdependence on the chance of conflict onset and escalation in East Asia and among dyads with a developmental state, compared with all other intraregional dyads.

3 Results

I include all intraregional dyads in the models in Table 1. Interaction terms are used to assess whether there is a statistically significant difference in the trade–conflict associations of dyads comprising the groups of interest in the hypotheses, and all other intraregional dyads. Model 1 presents baseline results for all intraregional dyads in the period when the developmental state model began to be widespread in East Asia (from 1960). Model 2 contrasts the effects of the trade variables intra-regionally with their effects in Asia and the Pacific, excluding East Asian dyads. Model 3 considers the difference in the effects of trade for East Asian dyads. Model 4 has a longer temporal domain, and considers the difference between intraregional dyads without a developmental state and those including at least one developmental state, with independent variables measured 1950–2000 (and the corresponding dependent variables measured 1951–2001).

The results suggest that trade interdependence (GDPshare) has a pacific effect on the onset of MIDs intra-regionally, and no significant association with MID escalation to over 250 battle deaths. This supports general hypotheses 1 and 2. Trade volume appears to have no significant association with MID onset, although the coefficients are positive as expected, and a negative and significant association with MID escalation. Thus, general hypothesis 3 finds little support, but hypothesis 4 is supported.

These patterns are clear in model 1, but also consistent in models 2–4, for the GDP share and trade volume terms (when Asia–Pacific/East Asia/Developmental state dummy = 0). The interaction terms in these models also show that there are statistical differences in the association of interdependence and MID onset for each of the groups indicated (when dummy = 1). Thus, in model 2, the interaction term for Asia–Pacific dyads excluding East Asian states and lower dyadic GDP
<table>
<thead>
<tr>
<th>Table 1 Intraregional models with interactions</th>
<th>Model 1</th>
<th>Model 2</th>
<th>Model 3</th>
<th>Model 4</th>
</tr>
</thead>
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<tr>
<td>All Intraregional Dyads, 1961–2001</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Escalation to over 250 Deaths</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tradevolume(_{(ln)})</td>
<td>-0.04</td>
<td>0.01</td>
<td>0.00</td>
<td></td>
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<td>Tradevolume(_{(ln)}) \times \text{[AP, EA, or Dev State dyads]}</td>
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<td>14.13</td>
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</tr>
<tr>
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<td>1337.52</td>
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</tr>
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<td>-1.28</td>
</tr>
<tr>
<td>Selection into MID</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Tradevolume(_{(ln)})</td>
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</tr>
<tr>
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<td>0.19</td>
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</table>

Continued
Table 1 Continued

<table>
<thead>
<tr>
<th></th>
<th>Model 1</th>
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<th>Model 3</th>
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</thead>
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<td>0.48</td>
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<td>0.00</td>
<td>0.48</td>
</tr>
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<td>0.07</td>
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<td>0.03</td>
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<td>0.00</td>
<td>−0.03</td>
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<td>0.00</td>
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<td>0.00</td>
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<td>Distance(ln)</td>
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<td>0.00</td>
<td>−0.26</td>
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<td>0.00</td>
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</tr>
<tr>
<td>Peaceyears$^2$</td>
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<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Peaceyears$^3$</td>
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<td>0.00</td>
</tr>
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</tr>
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<td>0.03</td>
<td>−0.28</td>
</tr>
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<td></td>
<td></td>
<td>78,211</td>
</tr>
<tr>
<td>Uncensored observations</td>
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<td>Wald chi-squared (4, 7 df)</td>
<td>15.37</td>
<td>0.00</td>
<td>17.93</td>
<td>0.01</td>
</tr>
</tbody>
</table>

Probit selection models. Dependent variable measured at year $t + 1$ (1951–2001), independent variables at year $t$ (1950–2000); statistically significant coefficients at 0.10 level or better indicated with bold; Significance of $\rho$ based on the likelihood ratio test for independence of equations. All significance tests are two-tailed.
share is negative and significant (at the 90\% level), suggesting a stronger pacific effect for interdependence in this part of Asia than among other intraregional dyads. But the opposite is the case for East Asian dyads and dyads including a developmental state. In models 3 and 4, the corresponding interaction terms are positive and significant, although the magnitude (absolute values of the coefficients) is not quite as large as the negative coefficient for GDP share. This suggests a weaker, although still pacific, effect for interdependence for East Asia and for developmental states in general. This is consistent with hypothesis 5. There is also no significant effect indicated for interdependence in the MID escalation stage in models 3 and 4, which is consistent with hypothesis 6.

However, hypotheses 7 and 8 regarding trade volume do not find support: there is no indication in models 3 or 4 of any significant difference for East Asia or developmental states in the association of trade volume with MID onset or escalation, when compared with other intraregional dyads.

These patterns and conclusions are further supported by models 5 through 8 in Table 2. While interaction terms in probit models are useful for assessing whether there is a statistical difference between one set of observations and another, their interpretation is not straightforward (Kam and Franzese, 2007). I therefore present models using only the sets of dyads of interest in Table 2, as well as two sets of marginal effect plots in Figures 1 and 2.

Regarding the choice of selection models, the rho-statistics in models 1 through 5 are highly significant, indicating a strong likelihood of selection bias. However, the results are substantively unchanged if separate probit models are used.

When all intraregional dyads excluding East Asia\(^\text{14}\) are examined in model 5, there are significant pacific relationships between trade interdependence and MID onset and trade volume and MID escalation, but no significant association between interdependence and escalation, again supporting general hypotheses 1, 2, and 4. When only East Asian dyads are considered in model 6, the same relationships hold, but the magnitude of the coefficient for interdependence in stage 1 of the model appears to be much smaller, suggesting support for hypothesis 5 (probit coefficients

\(^\text{14}\) A model using only Asia and Pacific dyads excluding East Asian states fails to converge.
<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Escalation to more serious conflict</td>
<td>Selection into MID</td>
<td></td>
</tr>
<tr>
<td>Tradevolume(ln)</td>
<td>−0.03</td>
<td>0.01</td>
<td>0.01</td>
</tr>
<tr>
<td>GDPshareLower</td>
<td>17.05</td>
<td>21.73</td>
<td>0.43</td>
</tr>
<tr>
<td>PowerAB(ln)</td>
<td>−0.05</td>
<td>0.06</td>
<td>0.64</td>
</tr>
<tr>
<td>Joint autocracy</td>
<td>0.16</td>
<td>0.21</td>
<td>0.43</td>
</tr>
<tr>
<td>Constant</td>
<td>−0.93</td>
<td>0.42</td>
<td>0.03</td>
</tr>
<tr>
<td>Tradewealth(ln)</td>
<td>−0.00</td>
<td>0.00</td>
<td>0.93</td>
</tr>
<tr>
<td>GDPshareLower</td>
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<tr>
<td>Parity</td>
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<td>0.00</td>
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<td>PowerAB(ln)</td>
<td>0.22</td>
<td>0.02</td>
<td>0.00</td>
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<tr>
<td>Alliance ties ‘S’</td>
<td>0.08</td>
<td>0.07</td>
<td>0.25</td>
</tr>
<tr>
<td>Joint democracy</td>
<td>−0.03</td>
<td>0.01</td>
<td>0.00</td>
</tr>
<tr>
<td>Joint autocracy</td>
<td>−0.37</td>
<td>0.06</td>
<td>0.00</td>
</tr>
<tr>
<td>Contiguity</td>
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<td>0.00</td>
</tr>
<tr>
<td>Distance(ln)</td>
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<td>0.02</td>
<td>0.00</td>
</tr>
<tr>
<td>Peaceyears</td>
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</tr>
<tr>
<td>Peaceyears²</td>
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</tr>
<tr>
<td>Peaceyears³</td>
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<tr>
<td>Constant</td>
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<td>rho</td>
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<td>0.01</td>
</tr>
<tr>
<td>Number of observations</td>
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<td>9808</td>
</tr>
<tr>
<td>Uncensored observations</td>
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<td>164</td>
<td>186</td>
</tr>
<tr>
<td>Wald chi-squared (4 df)</td>
<td>8.44</td>
<td>0.08</td>
<td>8.95</td>
</tr>
</tbody>
</table>

Probit selection models. Dependent variable measured at year \( t + 1 \) (1951–2001), independent variables at year \( t \) (1950–2000); statistically significant coefficients at 0.10 level or better indicated with bold font; significance of rho based on the likelihood ratio test for independence of equations. All significance tests are two-tailed.
cannot be clearly interpreted without considering the values taken by other variables in the model, therefore estimates in Figs 1 and 2 are better indicators). The negative interdependence–MID onset relationship in model 7, when dyads containing at least one developmental state are considered, becomes insignificant. This is also consistent with hypothesis 5.
Before further assessing the hypotheses by considering marginal effects, presented in Figs 1 and 2, I first discuss the robustness of the findings so far.

3.1 Robustness checks

The dyads involved in deadly MIDs (Table A1 in the appendix) give an indication that Asia–Pacific MIDs often involve states with competing
territorial claims. If trade and territorial issues are correlated, then the apparent effects of interdependence and volume on conflict might be spurious. To assess whether territorial disputes might account for the distinctions found for East Asian or developmental states, I include a control for them in each stage of models otherwise specified as in Table 1. The Territorial claim indicator is coded 1 for all dyad-years with an active territorial claim, 0 otherwise, based on data for 1950–95 from Huth and Allee (2003). The results indicate that territorial claims are strongly associated with MID onset, but are not more likely to escalate than MIDs with no territorial issue. But inclusion of these variables does not change the sign or significance of the trade–conflict relationships of interest.

Recent literature on trade and conflict has suggested that trade conducted with fewer tariff or non-tariff barriers is most conducive to peace, whereas non-free trade is less so (McDonald, 2004). Because developmental states tend to manage trade strategically, this argument might explain the findings. Another argument focuses on the role of RIAs in facilitating conflict avoidance or resolution (Haftel, 2007). Because East Asia has relatively few of these (only two of the 25 Haftel identifies), this may also provide an explanation for my results. Similarly, I also test whether lower joint IGO memberships of any sort explain my findings.

In order to assess each of these hypotheses, I ran models similar to models 3 and 4 in Table 1, also including in each stage indicators of joint GATT or WTO membership (for free trade), joint RIA membership, or joint IGO membership, and interacting these terms with the trade variables at each stage. If these variables provide alternative explanations, they should cause the trade interaction terms with East Asian and developmental state dyads to become insignificant. If the trade interaction terms’ coefficients retain the same patterns of sign and statistical significance as in models 3 and 4, the results for East Asia and developmental states can be considered robust to these factors.

15 My RIA coding is admittedly less nuanced than Haftel’s, because it does not code the scope of economic activity covered by RIAs, nor the frequency of leader meetings. However, interacting RIAs with trade volume is a reasonable substitute for economic scope. This has considerably greater substantive effect on conflict than leader meetings (Haftel 2007, p. 230).
The findings in Table 2 prove highly robust in these sensitivity tests. In all cases, the trade variables and their interactions with East Asian and developmental state dyads retained comparable sign and significance, whereas in some instances, the new dummy and interaction terms also produced significant results (not discussed, to save space).

### 3.2 Estimating substantive effects

The results discussed so far indicate that the effects of trade interdependence on the onset of interstate conflict in East Asia and among dyads with a developmental state appear to be smaller than in other intraregional dyads, as anticipated by hypothesis 5. Hypothesis 6 has also been supported because there is no indication of a difference between the null effects of interdependence on escalation in general and among East Asian or developmental state dyads. However, hypotheses 7 and 8 have not found support.

In order to further assess hypotheses 5–8, a clearer indication of the relative substantive effects on the likelihood of interstate conflict onset and escalation is given in Figs 1 and 2. They present the marginal effects (and 95% confidence intervals) on predicted probabilities of MID onset and escalation, based on models 6 (Fig. 1) and 7 (Fig. 2). The figures are based on estimated effects\(^{16}\) for the trade variables while all other variables in the model are held at values that represent dyads at plausible risk of conflict. Given that interstate conflict is quite rare (MID onset occurs in just 0.9% of intraregional dyad years, 1951–2001, whereas MID escalation to over 250 battle deaths occurs in just 5% of those onsets), it is important to simulate scenarios in which the role of trade in preventing conflict can be meaningful. I therefore set the values of all other variables in the model at their 80th percentile ‘dangerous’ values (i.e., the 80th percentile low value for distance and the 80th percentile high value for parity). I then allow the relevant trade variable (GDPshare or Trade volume) being estimated to vary from the minimum

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\(^{16}\) Specifically, they are based on simulations using 10,000 sample draws from the multivariate normal distribution, similar to simulations produced by Clarify software (King et al., 2000) or suggested by Brambor et al. (2010). For the simulations, separate probit models are used for each stage for the sake of computational simplicity, with the second stage run on data only for dyads with MID onsets (a conditional model). The probit results are very similar to those for models 5 and 6.
to maximum value it actually takes in intraregional data when the other trade variable is set at its 80th percentile dangerous value.\textsuperscript{17} This provides realistic scenarios based on the actual cross-national variation in the key variables. These values are calculated for all intraregional dyads, 1960–2000, such that the same values are used for all scenarios in Figs 1 and 2. They allow comparability across scenarios for typical dyads at some plausible risk of conflict, rather than the average intraregional dyad, which has a very low \textit{a priori} risk of conflict.

Comparison of these marginal effects strongly supports the conclusions already suggested. The pacific effects of trade interdependence on the chances of conflict onset are smaller and weaker in East Asia and among dyads including a developmental state, as is evident when the lower left panels of each figure are compared with the lower right panels. This is consistent with the logic laid out regarding the use of trade interdependence to signal intentions and resolve in the initiation stage of conflict for developmental states. If they can more freely, but less credibly, use trade as a signaling tool, I have argued that this weaker effect is indeed what would be observed. Also consistent with my expectations, interdependence has little apparent effect on escalation for any type of dyad – which I argue would be the case if it had been sufficiently factored in to actors’ calculations at the conflict onset stage. The middle upper panels in both figures indicate this; the slopes are almost perfectly flat for East Asian and developmental dyads, and although there are slightly inclining slopes for other intraregional dyads, they are small and the confidence intervals are quite wide across the entire range of values.

While the slope of the marginal effect of trade volume on the chance of MID onset in East Asia is slightly positive (Fig. 1, middle lower left panel), this is too small to count as substantial support for hypothesis 7. There is no corresponding conflict-exacerbating effect evident for the dyads including a developmental state (Fig. 2, same panel location). The corresponding positive coefficients in models 3 and 6 are also not statistically significant. Neither is there evidence that trade volume has less of a pacific effect in East Asia or among dyads with a developmental state.

\textsuperscript{17} I use the range of the 95\% confidence interval of the 80th percentile value as calculated by Stata 11 software.
than in other intraregional dyads. The left and right upper graphs in each figure are very similar. Thus, while trade volume, rather than interdependence, is associated with pacific outcomes at the escalation stage, as anticipated by my general hypothesis 4, this effect is not of any less magnitude in East Asia or among developmental states, and hypothesis 8 is not supported. This would, for example, support an interpretation of the already-mentioned Thai–Cambodian dispute that points to trade as a possible factor inhibiting the conflict from escalating to higher levels. The weaker pacific effect of trade on MID onset, but not on MID escalation, among East Asian and developmental dyads is an area for further consideration and analysis. Perhaps it points to different perceptual dynamics due to different levels of decision maker attention at each conflict stage, for example.

4 Conclusions

This article has presented statistical tests regarding the trade–conflict relationship, with special attention to East Asia and to developmental states. The findings support the expectation that different aspects of trade can have different effects at different stages of the conflict bargaining process. While the expansion of intraregional trade flows in East Asia may have coincided with a drop in the escalation of militarized disputes, I find that the link between trade interdependence and peace is actually somewhat weaker in East Asia than in other regions. I provide evidence that this effect is attributable to the developmental state model. However, a broader conclusion of this article is that differences in the trade–conflict relationship across regions, and across different political-economic systems, appear to be differences of degree, rather than of kind. Contrary to my expectations, the impact of the developmental state model is not so strong that trade volume is associated with a greater frequency of MID onset, or with a weaker pacific impact on MID escalation. In East Asia, as in other regions, high volumes of trade appear to provide useful signaling tools that states involved in militarized disputes can deploy to help avoid escalation to large-scale interstate violence and war. The region’s increased trade flows may thus help explain the relative lack of conflict escalation in recent decades.
Acknowledgements

I am grateful to Vinod Aggarwal, Ajin Choi, Thomas Christensen, Anders Engvall, Natasha Hamilton-Hart, Stuart Harris, Alastair Iain Johnston, Isak Svensson, Andrew McIntyre, Erik Melander, Chung In Moon, Helen Nesadurai, Andrew Phillips, John Ravenhill, and Liz Thurbon for important comments that improved the article. Support from East Asia Peace Programme, Uppsala University, the ANU-MacArthur Asia Security Initiative (ASI) and from the Australian Research Council (DP1093625) is gratefully acknowledged.

Appendix

Further notes on the data and sources


Conflict. COW Project dyadic MID data (Ghosh and Bennett, 2007).

Developmental states. The coding relies on some often cited and/or empirically focused studies of developmental states, including chapters by Woo-Cummings, Johnson, Pempel, Vartiainen, and Loriaux in Woo-Cummings (1999), Leftwich (1995), and Wong (2004). Regarding some borderline cases, Masina (2010) argues that Vietnam does not fit the model due to its lack of industrial strategy, Pempel (1999, pp. 155, 164) argues that the Philippines has political and socio-economic differences due to its colonial legacy. A number of studies also point out that Chile has been too focused on free-markets internally and in its trade policies to fit the model.

Regime type. Polity IV dataset (Marshall and Jaggers, 2007). The commonly used polity index ranging from −10 (fully authoritarian) to +10
(fully democratic) is used to create two indicators, joint democracy and fully authoritarian dyads, as described in Goldsmith et al. (2008).

**Power, contiguity, distance, and peace years.** As provided by EUGene software version 3.1 (Bennett and Stam, 2000). Contiguity coded ‘1’ if a land border is shared or if there is 24 miles or less of water between borders, otherwise ‘0.’

**IGOs.** Data for this variable, and also RIAs and Free Trade, are from the COW IGO database (Pevehouse et al. 2004). The variable measures the number of IGOs in which both states in a dyad are members in a given year. It ranges from 0 to 107.

**RIAs.** Based on Haftel’s (2007, pp. 234–235) list of 25 such organizations. The only one not found in the COW IGO data was the Bangkok Agreement (now named the Asia–Pacific Trade Agreement), so a new variable was created and included in the final tally, based on the organization’s website: http://www.unescap.org/tid/apta.asp. The variable counts annual dyadic joint memberships and ranges from 0 to 3.

**Free trade.** I do not use McDonald’s (2004) measure based on residuals from regressions on trade levels. Not only is this complicated to implement, but it relies heavily on the assumption that one can correctly specify such a model. Because trade volume itself is a key independent variable in my study, and determinants of trade may vary over time and by region, I prefer to use an institutional indicator of free trade. Thus, I code free-trade dyads as ‘1’ for those in which each state is a member of the GATT (1950–1994) or its successor the WTO, ‘0’ otherwise.
### Table A1: Asia and Pacific dyads with fatal MIDs, 1951–2001

<table>
<thead>
<tr>
<th>State A</th>
<th>State B</th>
<th>MIDs w 1000+ deaths</th>
<th>MIDs w over 250 deaths</th>
<th>All Fatal MIDs</th>
<th>GDPShareA</th>
<th>GDPShareB</th>
<th>Tradevolume ($ millions)</th>
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<td>India</td>
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<td>5</td>
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<td>0.0044</td>
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<td>5</td>
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<td>0.0015</td>
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</table>

Values for GDPShare and trade volume are averages for all years $t$ with fatal MIDs in year $t + 1$; only states involved on day one of the dispute are included (‘joiners’ coming later to the MID are dropped from the analysis).
References


East Asia has experienced more than three decades of peace and prosperity, a sharp contrast with the recurrent wars and lagging development that plagued much of the region during earlier eras. The last major military conflict, the Sino-Vietnamese War, ended in 1979. Although skirmishes between the antagonists were not completely extinguished until the 1980s, the year 1979 marked the beginning of a clear secular decline in militarized conflict that has continued through the present (see Figures 1.1 and 1.2). That year also marked the start of sweeping economic reforms initiated under Deng Xiaoping's leadership in China. China's reforms, however, were only the most widely publicized among various efforts at economic liberalization throughout the region since the late twentieth century. These policy shifts have enabled many East Asian countries to share in a newfound prosperity that had previously taken root in Japan and in the so-called four tigers. Yet this era of peace and growth has been punctuated by periodic reminders of enduring security problems in the region. Do these security problems pose a threat to East Asia's record of economic success? Or do economic success and the greater levels of international economic cooperation that have accompanied it provide a foundation for political cooperation and the management of security problems? The contributors to this volume shed new light on these important questions.

Three broad approaches to thinking about economics and security in East Asia can be identified. One approach views the region's growing economic
prosperity as a result of the peace that has prevailed. In an international setting fraught with fewer political tensions, nations could focus resources on domestic development and enjoy the fruits of international trade and investment with countries whose prosperity they no longer viewed through the prism of military rivalry. In this approach, what needs to be explained is the peaceful context that has provided the opportunity for economic activity to thrive. Explanations for this peace often point to the power and leadership of the United States. As the Soviet Union declined and then collapsed, the United States stood as the sole superpower. American preponderance not only mutes potential security rivalries among its allies but also serves as a hedge against future uncertainty over new military threats that might emerge. Consequently, East Asian countries can refrain from deploying the kinds of forces that they might otherwise need to cope with the possibility of conflicts with a resurgent Russia or an increasingly powerful China.

America's relationship with China has also contributed to peace in the region. During the 1980s, Sino-American cooperation rested on a common
interest in counterbalancing the Soviet Union's assertive foreign policy. But even following the collapse of the Soviet Union, and despite the outbreak of some serious political and economic disagreements between China and the United States, the latter two countries managed to sustain a largely cooperative working relationship. Absent a common adversary, their overlapping interests in coping with problems of proliferation, terrorism, and the dangers of instability on the Korean Peninsula helped prolong a constructive U.S.-China relationship initiated during the closing decades of the Cold War. Although some analysts suggested that China's rise would undermine Sino-American cooperation and perhaps jeopardize regional peace, the yawning disparity between Chinese and U.S. capabilities minimized concerns about the countries' shifting power and enabled both states to focus mainly on the absolute, rather than the relative, gains they derived from bilateral cooperation. In short, one approach is to suggest that American power and the ability of the United States and China to avoid an adversarial relationship have sustained a peaceful international context conducive to regional economic prosperity.
A second approach views peace as stemming from regional prosperity, or more accurately, from the economic activity that generates prosperity. The logic is discussed further below, but centers on the claim that interdependence between trade partners establishes benefits that would be scuttled in the event of military conflict. Participation in international economic institutions reinforces this constraint by clarifying these benefits and the associated opportunity costs of military conflict. Institutional participation also socializes elites to embrace transnational perspectives; in national policy debates, parochial perspectives are then less likely to prevail, thus facilitating the compromises that are necessary to sustain international cooperation and to prevent conflicts from escalating to the use of force. Aside from participation in international institutions, overseas commerce itself creates and sustains common interests between economic partners and encourages a more cosmopolitan perspective conducive to the peaceful adjudication of international disputes. Finally, economic exchange reshapes the domestic political landscape of the participating countries, thereby empowering those segments of society whose interests are served by a foreign policy that avoids disruptive military conflict.

A third approach is skeptical that peace in East Asia is linked to economic activity. As has often been noted, extensive economic interdependence and strong elite ties across the major European states in the early twentieth century failed to halt the slide to World War I. Other skeptics go further still and consider East Asia’s current period of peace and prosperity a brief respite from the normal pattern of interstate rivalry or perhaps even a mirage misleading analysts who fail to appreciate the looming dangers of military conflict and economic disruption. Such views typically draw on the Western, mainly European, historical experience and suggest that Asia’s future may well be Europe’s bloody past.

Even analysts who had become optimistic about Europe’s peaceful future in the immediate aftermath of the Cold War argued that the basis for such optimism was absent in East Asia. Multilateral institutions that evolved in Europe over the era since World War II had provided a trellis first for economic and then for security cooperation that had no parallel in East Asia. In the early 1990s, Aaron Friedberg (1993–1994: 22) famously drew a sharp contrast between the “rich ‘alphabet soup’” of regional organizations in Europe and the “thin gruel” of such organizations in Asia. Moreover, Europe had forthrightly addressed many troubling historical legacies that had
repeatedly generated conflict on the continent, as well as more recent sources of antagonism. By contrast, East Asia seemed a region still rife with such problems—competing territorial claims, divided states, and lingering historical grievances (especially toward Japan), all fueled by the heated nationalist sentiment of newly emerging, newly independent, or recently reviving states. For those subscribing to this dark vision, East Asia’s story of economic prosperity was not just about rising living standards; it was equally about the accumulation of national resources that would sooner or later fuel military capabilities harnessed to competing national interests.

Such concerns notwithstanding, East Asia’s peace and prosperity endures. If the existing evidence remains inconsistent with the pessimists’ expectations, is that because their theories about the links between economics and security on which they base their predictions are flawed? Are there assessments of East Asia that are more solidly grounded in theories that identify connections between economics and security? More generally, how useful is the existing tool kit of international relations theories for explaining East Asia’s recent peace and prosperity?

Any particular theory explains only a slice of reality by setting aside many of the details and some of the causes that produce observable outcomes. A more comprehensive understanding of historical or contemporary events requires tapping various theories and the partial insight that each offers. Consequently, when the authors of the chapters in this volume examine the nexus of economic and security relations in East Asia, they usefully draw on a rich variety of theoretical approaches that can illuminate important questions about a region whose significance for students of both international political economy and international security has grown dramatically over the past thirty years. Their work suggests, in various ways, that the interaction of economic and security concerns defies simply categorizing either as the independent variable (cause) and the other as the dependent variable (effect). To grasp the reasons for, and evaluate the durability of, East Asia’s recent peace and prosperity, both economic and security fundamentals matter; the chapters here explore how they matter and, where possible, the extent to which existing theories explain why.

The remainder of this introduction provides some general background for the more focused chapters that follow. First, we set forth evidence that demonstrates the growth of economic regionalism in East Asia, comparing the current era with the recent past in the region and drawing some limited
comparisons with evidence from the European experience. Second, we clarify the security issues whose links with regional economic developments our authors examine. Third, we briefly discuss leading theories that claim to offer explanations for the connection between economic and security affairs in international politics. Fourth, we discuss the prominence of China in many of the chapters, even as the volume addresses East Asia as a region. We conclude by describing the organization of the volume and by offering a preview of the perspectives in the chapters that follow.

The Growth of Economic Activity in East Asia

Over the course of the past thirty years, there has been a substantial rise in the amount of cross-border economic activity in East Asia. To illustrate this growth, we present some data drawn from the economies in East Asia: the ten Association of Southeast Asian Nations (ASEAN) states (Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam), China, Hong Kong, Japan, South Korea, and Taiwan. Figure 1.3 shows the ratio of international trade among these countries to the total trade that they conducted for each year from 1979, when economic reform started gaining traction throughout the region, until 2009. In 1979, roughly one-third of the trade these states conducted was intraregional, a value that spiked to about one-half by 2009. China has played a leading role in this rise. In 1979, about 10 percent of intra-East Asian trade stemmed from foreign commerce involving China; by 2009, the value exceeded 30 percent.

Figure 1.3 also reports the annual flow of trade from East Asian countries to the United States, the European Union, and Latin America, respectively, as a percentage of the total overseas commerce conducted by East Asian states. Clearly, the surge in intra-East Asian trade is not matched by East Asian trade with other key partners. States in the region have experienced no noticeable change in the amount of foreign commerce with the European Union and Latin America. Over the past decade, they have experienced a rather pronounced dip in trade with the United States.

In addition to trade, foreign direct investment (FDI) within East Asia has risen precipitously. Figure 1.4 shows the yearly stock of FDI emanating from East Asian home countries and located in host countries in the region as a percentage of total outward FDI by East Asian states. There is ample evidence that, over the past three decades, these states have located an increasing
amount of their foreign investment within East Asia. Indeed, the percentage of total outward East Asian FDI located in the region tripled, rising from about 20 percent in 1980 to roughly 60 percent by 2005.

Over the past thirty years, there has also been a dramatic increase in the number of economic institutions designed to promote and regulate trade, investment, and finance in East Asia. Only a few such institutions existed in 1980; currently, there are a few dozen. Moreover, plans are afoot to launch even more. China, Japan, and South Korea have each explored the possibility of forming a free-trade area (FTA) with members of ASEAN, the region’s most important institution. Various East Asian countries have expressed interest in concluding a regionwide free-trade zone that would encompass not only China, Japan, South Korea, and ASEAN, but also Hong Kong, and Taiwan. More generally, policy makers throughout East Asia have commented on the desirability of forming additional economic institutions in the region. In 2005, for example, Indonesian Finance Minister Jusuf Anwar commented that
East Asian integration should be promoted by "weaving a web of bilateral and multilateral FTAs" (Nikkei Weekly 2005).

The growth in economic activity within East Asia is impressive, even when compared to Western Europe, which sets the standard for regional economic integration. As shown in Table 1.1, both East Asia and the European Community (EC/EU) doubled the amount of intraregional trade as a percentage of total trade between 1960 and 2009.¹ To be sure, in any given year, the ratio of intraregional trade to total trade was anywhere from 10 percent to 60 percent greater for the Western European countries than for the East Asian states. Moreover, the value of total trade and intraregional trade conducted by EC/EU members far outstrips that conducted by East Asian states. Nonetheless, trade within East Asian has grown very rapidly in recent decades. There has also been a rise in investment; efforts at financial cooperation; and the establishment of institutions designed to promote economic cooperation in the region, a trend vividly illustrated in the chapter by Wu Xinbo.

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¹ The data for EC/EU is from the European Commission, while the data for East Asia is from various sources including the UN Conference on Trade and Development and the Organisation for Economic Co-operation and Development.
TABLE 1.1 Intraregional trade as a percentage of total trade in East Asia and Western Europe, 1960–2009

<table>
<thead>
<tr>
<th>Year</th>
<th>ASEAN+4</th>
<th>EC/EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960</td>
<td>25.66</td>
<td>32.65</td>
</tr>
<tr>
<td>1970</td>
<td>30.30</td>
<td>46.36</td>
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<tr>
<td>1980</td>
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<td>42.73</td>
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<tr>
<td>1990</td>
<td>40.14</td>
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<tr>
<td>2000</td>
<td>48.12</td>
<td>53.35</td>
</tr>
<tr>
<td>2009</td>
<td>49.99</td>
<td>60.47</td>
</tr>
</tbody>
</table>

Source: International Monetary Fund's Direction of Trade Statistics.

Note: ASEAN+4 = ASEAN, China, Korea, Japan, and Hong Kong. These figures do not include Taiwan because it is not possible to obtain reliable data on Taiwanese trade before 1990.

Security Issues

Over the past thirty years, East Asia has experienced rapid growth in intraregional economic activity. It has also experienced a marked reduction in political-military conflict. No regional wars have broken out since 1979, and although isolated incidents have occurred, until the early 2011 border clashes between Thailand and Cambodia, there had been a complete absence of serious interstate military conflicts since 1988. Figure 1.1 shows the frequency of wars and conflicts in the region since 1946, based on data collected by the Peace Research Institute Oslo (PRIO). Following PRIO, we define wars as interstate and extrasystemic hostilities (i.e., disputes between a nation-state and a nonstate actor located outside of the nation-state) that generate at least one thousand battle deaths annually. Conflicts are defined as interstate and extrasystemic disputes that yield between 25 and 999 fatalities per year. Both wars and conflicts have steadily declined over the post-World War II era. And, as is shown in Figure 1.2, battle deaths in the region declined precipitously once the Sino-Vietnamese War concluded in 1979. Indeed, for nearly a quarter of a century, no one had perished in formal military combat.

Is the recent expansion of economic activity in East Asia causally related to the reduction in political-military hostilities, or is this relationship spurious? Alternative explanations are readily available. Perhaps disputes in the region have simply failed to rise to the level of intensity that prompts states to choose war over diplomacy. Perhaps the robustness of military capabilities
(including the ominous presence of nuclear weapons) and alliances that tie the U.S. military to key states in East Asia have discouraged recourse to the large-scale use of force. In short, other causes may account for the durability of the East Asian peace or may reinforce the pacifying effects of economic causes. The chapters in this volume begin to sort out the relevance of economics for regional security. They also touch on related questions. To the extent that economic causes have been a force for peace, how likely is it that this salutary effect will continue? Do current economic developments in the region, separately or in combination with other trends, provide grounds for optimism about an enduring peace? Or do those trends provide reasons for concern that the economic foundation for the thirty-year peace is weakening or that economic problems may even emerge instead as a source of conflict that could increase the likelihood of war in the future?

Although East Asia has been free of major war since 1979, it has not been free of interstate disputes, including conflicts marked by the use of military force. Peace, in other words, has not meant absolute security for the countries in the region, despite the remarkable diminution in the frequency and intensity of military conflict and crises. Most notably, although the Korean armistice has held, small-scale military incidents on the peninsula and in the nearby seas have occurred both before and after 1979. These, along with the tensions triggered by North Korea's nuclear weapons program since 1993, serve as reminders of the continuing potential for larger military conflict. The troubling security concerns on the Korean Peninsula, however, are not closely linked to the changes that have characterized the rest of East Asia over the past three decades. Pyongyang has stubbornly resisted suggestions that it follow the example of China and others to reform and open up its economy; in many ways it stands as a singular exception to the broader pattern. Perhaps most telling, security concerns on the Korean Peninsula have not served as a wedge in exacerbating conflicts of interest among the other East Asian states. On the contrary, the shared interest in preserving the peaceful regional environment conducive to international economic activity has led others to focus on containing instability in Korea and to work hard to minimize the risk of escalation to military action.⁵

Beyond Korea, however, there are other signs of continuing international insecurity, even as peace prevails and economic interactions deepen. One of the most prominent features of the region's security landscape is the presence of ongoing disputes about sovereignty claims, a topic addressed in the chapter
by Zhang Tuosheng. Although most of the land-based territorial disputes in East Asia have been resolved, significant disagreements remain about a wide variety of maritime claims and claims to territories that lie across the sea from the principals. These disputes are not just about historical sovereignty but also about contemporary economic interests. China and Japan contest energy-rich patches of the East China Sea. Japan and Korea have not yet resolved their occasionally heated dispute about the islands known as Dokdo in Korea and Takeshima in Japan, which has implications for economic resource rights. Indonesia, Vietnam, Malaysia, Brunei, the Philippines, Taiwan, and China disagree about overlapping claims to territory, waters, and resource rights in the South China Sea, where some expect to find significant energy reserves. And because the United States is allied with Japan, Korea, and the Philippines, and has been cultivating a closer relationship with Vietnam, conflicts rooted in most of these East Asian maritime disputes carry the potential for escalation and for drawing in the world’s most powerful states. Thus far, the parties to these disputes have managed to contain the potential for military conflict by delaying the resolution of sovereignty claims and focusing instead on ways to permit ongoing economic activity.

The continuing tensions between China and Taiwan represent another East Asian conflict that has linked economic and security dimensions as well as the potential to involve the United States. China upholds a long-standing claim to sovereignty over Taiwan and the smaller islands administered by the government of the Republic of China (ROC) in Taipei. Although the United States no longer has a security treaty with (or even recognizes) the ROC, in 1979 the U.S. Congress passed the Taiwan Relations Act (TRA). The act asserted a continuing American interest in the island’s fate, indicated that the United States might intervene in the event of military conflict in the Taiwan Strait, and established the basis for subsequent decisions to sell defensive weapons to the authorities in Taipei. Although the TRA’s original assertion of a continuing American interest in Taiwan’s fate reflected the history of political ties between Washington and the ruling party in Taipei, as Taiwan’s economy soared after 1979, it became an important economic partner for the United States and its allies in East Asia. Perhaps more intriguing in light of this volume’s theme, the interplay of economic and security interests has increasingly been reflected in the relationship between China and Taiwan. Despite their ongoing dispute about sovereignty and continued preparation for the possibility of military conflict in the strait separating them, Taiwan
and China have experienced a boom in their economic relationship. The extensiveness and deepening of these ties has led them to sign the Economic Cooperation Framework Agreement, which institutionalizes their thickening network of economic relations and is likely to simplify Taiwan’s ability manage economic activity, not only with the Chinese mainland but also with the vast majority of countries that no longer formally recognize the ROC government in Taipei (Richburg 2010).7

Intertwined with the varied territorial claims noted above are significant disagreements about the maritime rights defined by the international law of the sea. Most notably, China’s decision to define its national security interests as extending to areas that other countries view as zones in which contiguous states have exclusive economic rights but not the right to exclude other countries’ ships or aircraft has generated conflicts between China and the United States (Dutton 2010). Thus far, incidents growing out of these conflicts, especially disputes about the right of innocent passage by vessels that may be undertaking surveillance activities, have been contained. But the fundamentally different perspectives in Beijing and Washington make clear that, short of war, a crisis that develops from each side’s insistence on its principled position and testing of the other party’s resolve risks dangerous military escalation.8

Clearly, maritime disputes loom large in thinking about the way in which economics and security in East Asia condition each other. Economic interests in sustaining a peaceful regional context for development may dampen territorial and sovereignty disputes at sea before they escalate to the use of military force. Is it possible, however, that the economic costs of war fighting for the major states in East Asia are so high that some will believe that it is safe to press their maritime claims without fear of escalation? If so, then a corollary to the East Asian peace may be that it does not preclude the possibility of crises and perhaps even limited conflicts in which military power remains relevant.9

East Asian states have certainly demonstrated a keen interest in maintaining the military capabilities necessary to protect their political and economic interests. Some of these capabilities are familiar sorts of weapons systems necessary for power projection on, under, and above the seas to ensure national interests and territorial claims against potential threats. The ability of states in the region to invest in such military capabilities has grown along with the size and sophistication of the economies from which governments draw their revenues. But some military capabilities pursued in East Asia reflect new wrin-
kles in modern warfare that have resulted from the advance of, and reliance on, high technology. To the extent that such innovations alter the effectiveness of weapons systems, mastering new technologies and marrying them to military operations (or devising novel ways to disrupt the adversary's military operations dependent on such technology) assume an unprecedented significance. Because many of the relevant technologies are rooted in advances in electronics and computer systems that have civilian applications, and because the East Asian economies are home to some of the leaders in these fields, the increasing importance of high technology for military power indicates yet another way in which economic developments interact with the security environment and shape the prospects for conflict in East Asia—a consideration explored at length in Michael Horowitz’s chapter.

A different connection between economic developments and political-military relations in East Asia pertains not to military capabilities but to strategy. As Taylor Fravel indicates in his chapter, aside from thinking about maritime disputes and the way these demand changes in the thinking of a military long focused on ground operations to defend China’s borders, the People’s Liberation Army (PLA) has begun to develop new strategies along with new capabilities to address nontraditional security concerns, especially disaster relief, counterterrorism, and peacekeeping operations. Though certainly not supplanting its ambitious program of military modernization designed to deal with the traditional contingency of interstate conflict, as China’s economic involvements well beyond the mainland have increased, and as the regime has become more concerned about internal threats to the domestic stability necessary for economic progress, the PLA and especially its navy have begun to address the need to prepare for military operations other than war.

Although economic interests influence military-security relations, military-security interests also influence the region’s economic relations. Concerns about vulnerability and domination inform the design of economic institutions and the choice of institutional venues for addressing economic problems, with enduring political considerations limiting their role and effectiveness, as the chapters by Miles Kahler and Benjamin Cohen make clear. Security concerns also condition the extent to which economic interests shape patterns of trade and investment in goods and services that may have military externalities, particularly technologies and systems for employing them that can affect the relative power that states can bring to bear in conflict. As the chapter by Horowitz indicates, this consideration can extend beyond the
hardware and software to the education and training of personnel from which new technologies emerge and on which their military applications ultimately depend.

Yet security concerns can sometimes encourage the institutionalization of economic ties. To allay fears about its growing clout, during the mid-1990s China turned to multilateral economic institutions as part of an effort to cultivate its image as a responsible international actor rather than a potential threat. These efforts—including participation in regional financial arrangements; the conclusion of a free-trade agreement with ASEAN; and exploration of greater economic coordination among China, Japan, and South Korea—have had mixed results and have been tested by the strains of the global recession of 2008-2009. But from the perspective of our examination of the nexus of economics and security in East Asia, the point is that economic developments not only shape but also are shaped by security concerns.

Theoretical Perspectives on the Political Economy of National Security

Various theoretical perspectives exist on the relationship between international economic relations and security relations. One view is advanced by liberals, who argue that extensive economic interdependence discourages interstate conflict and reduces the likelihood that those disputes that do occur will escalate (Stein 1993; Doyle 1997; Mansfield and Pollins 2001). In advancing this claim, liberals have emphasized several causal mechanisms that could explain political-military relations in East Asia. For example, liberals frequently argue that economic exchange promotes greater contact and communication between governments and between private actors located in different countries, thereby fostering cooperative political relations (Doyle 1997: chap. 8; Hirschman 1977: 61; Stein 1993; Viner 1951: 261). Indeed, there is ample reason to believe that heightened economic activity in the region has increased such contact, although it is far less clear whether this has made any substantial contribution to political cooperation.

Furthermore, liberals stress that open international trade and FDI generate efficiency gains that contribute to growth and prosperity. Both individuals and firms benefit from these gains. As openness rises, private actors become increasingly dependent on foreign markets. Military conflict risks undermining openness and rupturing economic relations among the antagonists,
thereby scuttling the gains from overseas economic exchange. Consequently, private actors have reason to press their governments to avoid becoming embroiled in hostilities with key economic partners. Government officials, in turn, have reason to attend to these societal pressures because they depend for political support on groups that would be adversely affected by conflict. As Montesquieu famously put it centuries ago, "the natural effect of commerce is to lead to peace. Two nations that trade together become mutually dependent: if one has an interest in buying, the other has an interest in selling; and all unions are based on mutual needs" (quoted in Hirschman 1977: 80).

However, liberal arguments about the political economy of national security have faced criticism. First, various observers have charged that open trade relations and extensive economic interdependence can adversely affect a state's security, as the efficiency gains from trade often do not accrue to states proportionately and the distribution of those gains can influence interstate power relations (Hirschman [1945] 1980; Gilpin 1981). In a particularly influential study, Albert Hirschman ([1945] 1980) concludes that trade relations can foster political dependence and domination. He argues that open trade affects power relations by generating efficiency gains that enhance the military capacity of the participating states and by increasing the costs associated with any disruption in the commercial relationship. States that would have trouble replacing economic exchange with a given trade partner are dependent on that partner. The more costly it is to shift trade from this partner to other markets, the greater this trade partner's influence. Consequently, states can use foreign trade to bolster their power by shifting trade to smaller and poorer partners, which have a particular need for commerce and the income that it yields. One source of concern in East Asia is that the rapid rise of China's trade with other countries in the region has increased their dependence on Beijing, thus providing it with leverage that could adversely affect their national security.

Second, some studies charge that liberals are insufficiently attentive to the institutional context in which trade is conducted. Robert Keohane (1990), for example, argues that economic openness can inhibit interstate conflict, but only if international institutions exist to promote openness and ensure that it will not falter in the future. Edward Mansfield and Jon Pevehouse (2000) make a related argument. They focus attention on preferential trading arrangements (PTAs), which are a set of interstate institutions that grant each member country preferential access to the market of every other participant.
Most states enter PTAs expecting to derive economic benefits. Sometimes these expected benefits are realized; sometimes they are not. Nonetheless, conflict between member states threatens to scuttle these anticipated gains by damaging economic relations between participants and the arrangement itself. As trade flows within a PTA rise, so do these anticipated gains and the economic costs of conflict. Consequently, heightened trade is most likely to discourage conflict among members of the same PTA.

Whereas these arguments stress the interactive effects of economic flows and institutions on conflict, other researchers stress that institutions promote both interdependence and cooperation among participants (Nye 1971; Keohane 1984). Institutions facilitate mutual policy adjustments, which can foster interdependence. They also establish focal points, create a forum for negotiation and conflict resolution, reduce transaction costs, and monitor and disseminate information about the actions of member states, all of which contribute to cooperation. Some observers have argued that institutions can also spur cooperation by altering the preferences and the identities of member states (Hopf 1998; Johnston 2001).

These claims are examined in a number of the following chapters. Consistent with the liberal argument, Wu Xinbo focuses on the ASEAN plus three (i.e., ASEAN plus China, Japan, and South Korea) and argues that heightened economic interdependence has stimulated political cooperation and dampened conflict in East Asia. Miles Kahler, however, offers a less sanguine assessment of economic institutions in East Asia, pointing out that although institutions in the region have promoted greater economic interdependence, this is unlikely to have the conflict-dampening effect that liberals would expect. Benjamin Cohen, focusing on regional finance rather than trade and FDI, emphasizes underlying security tensions among East Asian states as a reason to be skeptical that economic cooperation will inhibit military friction in East Asia. Although Cohen also maintains that, over the longer term, efforts to improve financial cooperation might help reduce political tensions in East Asia, to the extent he and Kahler underscore the importance of security concerns, they share much in common with realist critics of the liberal position. These critics charge that liberals privilege the effects of economic relations on political-military relations while giving short shrift to the tendency for political-military relations to drive economic relations.

This critique might suggest, for example, that we observe both heightened economic activity and a relative absence of conflict in East Asia because power
relations in the region and globally have facilitated both peace and increasing economic exchange. During the last decade of the Cold War, when the international system was still bipolar, the United States, its allies, and China all shared an interest in resisting the Soviet Union. This encouraged their political cooperation and led them to welcome the positive security externalities that resulted from their economic interaction (Gowa and Mansfield 1993; Gowa 1994). After the Cold War, realists have argued that the international system became unipolar, dominated by the United States (Wohlforth 1999). The preponderance of U.S. power has helped ensure that existing rivalries in East Asia and elsewhere do not boil over, and it has restrained other powers in the region, most notably China. Moreover, there is a long tradition of realist thought that attributes the existence of a liberal international economy and heightened interdependence to the emergence of a single state that is powerful enough to manage the global system (Krasner 1976; Gilpin 1981, 1987). Global hegemony, in the view of such realists, underlies both the growth of economic exchange and political cooperation in East Asia and elsewhere.

The Prominence of China and U.S.-China Relations

This study illuminates links between the dramatic economic changes and enduring security concerns that have characterized East Asia since the late twentieth century. Some of the authors in this volume adopt a broad regional perspective. Others, however, focus most closely on China’s role in the region, often with special attention to U.S.-China relations. That China looms so large in such a study is easy to explain, because of both its dramatic economic growth and its impressive military modernization. Since the 1980s, China has had the fastest-growing economy in the world’s fastest-growing economic region (see Figures 1.5 and 1.6). In 2010, it surpassed Japan as the world’s second-largest economy, trailing only the United States. And at least since the early 1990s, China has been carrying out an impressive military modernization program during an era in which other major powers, with the noteworthy exception of the United States, have more often eschewed increases or even scaled back such investment (see Figures 1.7–1.9). China’s spending on military modernization has fueled speculation about its likely impact on East Asian security, and about its potential to end the era in which the United States remains the world’s sole superpower and the preponderant power in East Asia. As noted above, some consider American power a bulwark for peace in the
FIGURE 1.5 World shares of GDP, 1969–2009


FIGURE 1.6 East Asia average annual growth rates, 1980–2009

FIGURE 1.7 Percentage change in military spending, 1989–2009

FIGURE 1.8 Military spending, 1989–2009 (millions of 2008 U.S. dollars)
region. Thus, whether one focuses on either economics or security, or, as we do in this volume, on the links between them, it is understandable that China and its relations with the United States are central to the assessment.

The United States remains by far the world's largest economy, representing slightly more than 25 percent of global gross domestic product (GDP), a share that has remained relatively consistent since 1970. Although the size of China's economy still pales in comparison with that of the United States, at roughly 7 percent of global GDP in 2009, it has experienced a remarkable sevenfold increase since 1980 (U.S. Department of Agriculture 2010). China's current position reflects annual economic growth rates that have averaged slightly less than 7 percent over the past thirty years (World Trade Organization [WTO] 2010a). This dramatic success since 1980 followed first from a round of major domestic policy reforms embracing market mechanisms that repaired the damage of a stultifying planned economy. Then, beginning in the 1990s and accelerating in the early 2000s, the reforms to revitalize the domestic economy were complemented by reforms to more effectively open China to the outside world and more thoroughly integrate it with the global economy. In contrast with its minor role in 1980, by 2009 China ranked second in the world in merchandise trade behind the United States, overtaking Germany as the world's top-ranked merchandise exporter and in position to surpass it as the world's second largest merchandise importer (behind the United States) (Central Intelligence Agency 2010a, 2010b; Deutsche Welle 2010; WTO 2010b).
As we mentioned earlier, China has also been a driving force behind the recent growth in East Asian trade and investment. Over the past decade, China became the largest trading partner for Japan, South Korea, and Taiwan, and the second largest for ASEAN. It became the largest export market for Japan, South Korea, and Taiwan, and the second largest for ASEAN. It became the largest source of imports for Japan and South Korea, and the second largest for Taiwan and ASEAN. For some of its regional trade partners (especially Japan, South Korea, and Taiwan), trade with China has become an important engine of growth. Various East Asian firms have relocated factories to China to hold down the production costs of goods that face the increasingly intense competition that is characteristic of globalized markets, a pattern that helps explain why China has become one of the top destinations for FDI among emerging markets (EYGM Limited 2010).

As China's economy boomed, its demand for natural resources became a major factor in the regional and global economy. Most notably, to fuel its burgeoning industrial sector and to meet growing consumer demand for energy-intensive goods (especially automobiles and air-conditioning), China's need for imported oil and natural gas has been increasing steadily since the early 1990s. To ensure the availability of energy imports, China's leaders have crafted policies (including diversification of suppliers and encouraging Chinese participation in exploration, refining, and pipeline deals) that echo steps previously taken by Japan, South Korea, and Taiwan. Both because of its impact on world energy markets and because of potential competition among energy importers in East Asia and beyond who worry about the reliability of supplies and the predictability of prices, this aspect of China's economic rise commands special attention (Downs 2000; Ding 2005; Zha 2005). Its significance and the ramifications for international security are explored in the chapter by Danielle Cohen and Jonathan Kirshner.

Yet, as breathtaking as China's rise has been, the United States remains the world's leading economy and a major economic player in East Asia. The continuing importance of the United States and China's new stature are both reflected in regional trade volumes. China surpassed the United States as Japan's top trading partner in 2007, exceeding $214 billion total trade volume. But even in 2009 the United States remained a major trade partner for Japan, with a total of roughly $147 billion compared with China's total of $232 billion. China is also South Korea's largest trade partner, with trade totaling $156 billion in 2009, although U.S. trade still stood at an impressive $68 billion.
with the prospect of major increases once the United States–Korea (KORUS) Free Trade Agreement enters into force. In 2009 the volume of China’s trade with Taiwan (for whom it became the largest trade partner in 2005) was $106 billion, as compared with $47 billion for the United States. And although China’s trade with the ASEAN states in 2009 amounted to $160 billion, U.S. trade with ASEAN states totaled $147 billion (Census Bureau 2010).

In addition to their roles as two hubs for East Asian regional economic activity, over the past three decades China and the United States have also developed a robust bilateral economic relationship. Since 1980, trade between the United States and China has blossomed. In 1980 China was the thirty-fifth largest source for American imports and the seventeenth largest destination for American exports. By 2009, China had become the United States’ largest source of imports and third-largest destination for exports. In 1980, America was China’s second-largest source of imports and the largest destination for exports, but the absolute amounts for each were comparatively small. By 2009, the United States had become the top destination for China’s exports. Although the United States ranked fourth as a supplier of China’s imports in 2009, compared with 1980, the dollar amount had increased more than fifteen-fold (from $3.8 billion to $77.4 billion) and ranked fourth only because of the even larger increases in imports from Japan, South Korea, and Taiwan. More telling, perhaps, bilateral annual trade volume between the United States and China grew from a meager $5 billion in 1980 to about $350 billion in 2009 (down from $400 billion just before the global recession), thus making China America’s second-largest trade partner, just behind Canada (Census Bureau 2010).

The huge volumes and relative importance to each other as trade partners, however, has also generated friction between China and the United States. The bilateral trade balance, with growing Chinese surpluses and American deficits that rose from $84 billion in 2000 to more than $266 billion in 2008 became a hot political issue. Some Americans accused China of deliberately undervaluing its dollar-pegged currency to facilitate exports to the United States. More recently, some Americans have accused Beijing of devising policies that favor domestic over foreign business operations in China, thus hindering U.S. exports there in ways that some believe contravene the spirit and perhaps the letter of WTO rules (Wolff 2010). Whatever its cause, China’s large trade surplus with the United States during the opening decade of the twenty-first century contributed to Beijing’s rapid accumulation of the world’s largest
foreign-exchange reserves. Because a large fraction of these were held as U.S. Treasury securities, China's purchase of American debt thickened bilateral economic ties between the two countries and created the mutual vulnerabilities that define interdependence. On the one hand, China's T-bill purchases helped keep U.S. interest rates low, thereby sustaining an American economy fueled by credit-based consumption (including mortgage financing of the housing bubble). On the other hand, having invested so heavily in dollar-denominated notes, China acquired its own stake in the health of the U.S. economy and the strength of the American currency.14

In summary, by the end of the first decade of the twenty-first century, the United States and China displayed all the telltale signs of countries whose economies were becoming increasingly interdependent.15 As the liberal theories that we discussed earlier suggest, such relationships provide benefits to both countries that raise the incentives for sustaining cooperation. But, as realist theories remind us, heightened interdependence can also generate points of conflict if one party perceives that the other is benefiting at its expense. The greater the degree of interdependence, the higher the stakes are for both sides and, potentially, the stronger their determination to see disagreements resolved in their favor. Whether, on balance, Sino-American economic interdependence contributes to cooperation or conflict is theoretically indeterminate; the impact of interdependence is affected by the institutional context in which the economic relationship takes place, the economic climate in each country, and domestic political concerns that reflect sectoral and regional interests. Theory aside, however, it is clear that rising Sino-American economic interdependence since the 1990s has increased both the mutual benefits that provide incentives for cooperation and the stakes when economic conflict occurs. Since the mid-1990s, the two sides in a string of American debates—about granting China permanent most-favored-nation (MFN) trade status, the terms for its accession to the WTO, Chinese exchange-rate policy, and the fairness of labor practices in its export sector—have been fueled by the two faces of economic interdependence. Consequently, a close focus not only on China but also on Sino-American relations is central to understanding economic factors that may affect security in East Asia where both play leading roles. Yuan Peng's chapter, in particular, makes clear the potential strategic significance of an erosion in the economic foundations of cooperation between China and the United States that have been in place since at least the 1990s.
The prominence of China in many of the following chapters, then, is partly a reflection of the dramatic increase in the country's international economic role over the previous three decades. At the same time, China draws increased attention because of its concerted effort to tap expanding resources to modernize the country's large, but in many respects still lagging, military. And as in the economic sphere, in the sphere of regional security, as China's salience has increased, so has the importance of its bilateral relationship with the United States.

The expectation that China's increasing military power will permit, or perhaps tempt, its leaders to press harder in pursuing their interests in East Asia has raised concerns about the potential for conflict with regional neighbors or the United States, which maintains a strong military presence throughout the western Pacific. To be sure, China is not the only East Asian country investing economic resources in military modernization. But China's vast territory, its large population that is both proudly nationalist and increasingly well educated, its huge and rapidly growing economy, and its strong central leadership in Beijing all have combined to shape the belief that a bigger, more modern Chinese military will have a significant impact on regional security that overshadows concerns about military modernization by others in the region. Belief that Beijing's ambitious military modernization program will be sustainable rests in part on the recognition that China's economic boom has enabled it to increase military spending since the mid-1990s without significantly increasing the fraction of national resources devoted to the military (see Figure 1.10). Regional concern about a militarily stronger China also reflects the fact that, although Beijing has resolved most of its territorial and sovereignty disputes with its neighbors, as noted above, those that remain put it at odds with key East Asian countries (Japan, the Philippines, and Vietnam) and, perhaps most notably, with Taiwan.

Aside from tensions in the Korean Peninsula, the most prominent East Asian security concerns on the early twenty-first century almost all center on scenarios that involve China, its neighbors, and potentially the United States. Beyond the unusual American relationship with Taiwan, the United States is an ally of many states worried about China's growing military capabilities and possible intentions. Should conflicts emerge between China and these East Asian neighbors, the possibility of American involvement is clearly understood. Moreover, aside from the interests of allies, the United States has professed its own interest in sustaining the region's security architecture
(a large-scale American military presence and its hub-and-spokes network of alliances) that it established in the aftermath of World War II and that it believes helps preserve East Asian peace and provides the collective good of freedom of navigation on the high seas. Thus, regional doubts about the effects of China's rise reverberate in Washington. China's changing military profile, its consequences for regional security, and the American response to it are obviously central to any assessment of the nexus between economic and security relations in East Asia.

The contributors to this volume not only address a diverse set of topics that bear on the interaction of economics and security in East Asia; they also offer diverse assessments of the consequences of deepening economic activity and evolving security concerns in the region. Although there is no fundamental disagreement about the basic facts—increases in international economic exchanges, participation in a growing roster of regional institutions, and personal contacts among elites both in organizations and in less formal dialogues and side meetings—the authors disagree about whether and to what extent these trends are affecting regional security.

Benjamin Cohen's chapter argues that the relationship between cooperation in regional finance and in security matters is mutually endogenous.
Progress in promoting regional financial cooperation, especially since the Asian financial crisis of the late 1990s, has been noteworthy. But Cohen notes that it has also been constrained by the participants' underlying security concerns, especially states' concerns about maintaining control over their own destiny. Cohen is agnostic about the possibility for closer monetary and financial relations to moderate regional security tensions, and he acknowledges their potential for lubricating government interactions and altering national interests. Yet he emphasizes that such positive effects will depend on fundamental shifts in political relations among the East Asian states that seem unlikely for the near future.

Miles Kahler expresses skepticism about the positive effects on regional security that follow from the growth of regional economic interdependence and institutions. Kahler emphasizes both the weakness of East Asian institutional structures and their tendency to segregate economic and security issues. Although he does not rule out the possibility of future economic and institutional developments (especially the negotiation of new preferential trade agreements among key economies and a deepening of regional economic integration) that might significantly affect regional security, he views the current level of institutionalization as insufficient to have a major role in mitigating East Asia's potential for interstate conflict.

Wu Xinbo offers yet a third perspective on the interaction between trends in regional economics and security. As noted above, he considers economic regionalism manifest in the ASEAN plus three as having positive spillover effects on regional security. His chapter emphasizes the way institutionalized economic cooperation has facilitated cooperation on nontraditional security problems, has begun to foster regional consciousness among participants, and has generated common security interests that may give rise to a regional security architecture less dependent on the role of the United States.

Zhang Tuosheng examines territorial disputes in East Asia to determine the relative weight of economic and security interests that affect their intensity and intractability. In his survey of many of the disputes involving China, Japan, and their neighbors in the region, Zhang finds substantial variation in the ability of the parties to contain their disagreements and to finally resolve their disputes. He links these variations to the origins of the conflicts, the extent to which economic or political-security interests are at stake, and the differences between land-border disputes and disputes over maritime claims. Although Zhang expects that many of the disputes, especially those offshore,
will not easily be resolved, he is relatively sanguine that the economic and political interests of the relevant parties will continue to foster dialogue that limits their potential for generating military conflict and that peaceful dialogue should eventually permit negotiated settlements. Thus, for Zhang economic and security interests are linked—both as a source of conflict and as an incentive for cooperation.

The chapter by Danielle Cohen and Jonathan Kirshner examines energy security, a topic that by definition combines the two principal interests in this volume. Discussing the increasing dependence of China, Japan, and the United States on foreign sources of oil and gas, Cohen and Kirshner acknowledge the widespread view that concern about reliable access to reasonably priced energy provides incentives for states to take steps, including preparation for the need to rely on military force, which could trigger interstate conflict. In this one area, the predominant view among analysts and government leaders tends to be pessimistic about the security consequences of economic expansion and interdependence. Cohen and Kirshner are concerned as well, but not because they agree with the conventional wisdom that military forces can provide a solution to the problem of energy security. Instead, they argue that the very real dangers that arise from concerns about energy security are in fact the result of a myth, a consequence of beliefs that are not supported by the facts. They assert that there are few real threats to the energy supplies of the great powers and that military means cannot solve the actual energy problems the great powers may face. For Cohen and Kirshner, it is the “cult of energy insecurity” based on a myth, rather than a real condition of insecurity, that is dangerously and needlessly aggravating political conflict among the three biggest powers interacting in East Asia.

Chapters by Taylor Fravel and Michael Horowitz both examine changes in the nature of military power in East Asia that are linked to the dramatic economic transformation sweeping the region. Fravel’s focuses on the way China’s rapid economic growth and rising international economic role are reflected in its program of military modernization. He explains that economic expansion and military modernization go hand in hand, although not simply in the sense that greater resources are funding larger and more sophisticated capabilities. Instead, Fravel describes the ways in which China’s integration with the regional and global economy has altered the goals and content of the military strategy that modernization is to serve. Beyond traditional missions associated with interstate conflict, Fravel identifies a changed pattern of
investment that aims to serve a Chinese military strategy that includes new goals: ensuring domestic stability and the ability to undertake nontraditional security missions abroad, such as disaster relief, counterterrorism, and peacekeeping.

Horowitz cautions against extrapolating from the apparently pacifying effects in East Asia of growing economic interdependence, which has characterized the past few decades. Instead, Horowitz warns, the globalization of advanced industrial production and information technologies may provide an increasing number of East Asian states with military capabilities that could well exacerbate security dilemmas, encourage arms races, and transform a strategic environment in which disruptive new technologies have made conquest harder into an unsettling strategic environment in which new technologies facilitate offensive power projection. Thus, for Horowitz, it is precisely because of the economic success of East Asia's leading states that they are likely to be among the first with the resources (human and material) necessary to exploit new military technologies with potentially dangerous consequences.

Yuan Peng's chapter examines the relationship between the two leading powers in East Asia: China and the United States. In the chapter, he describes the challenges to, and opportunities for, cooperation in this bilateral relationship, whose profound significance is reflected in the volume's preceding chapters. Yuan identifies four Chinese perspectives or schools of thought about the strategic situation in the region. These schools of thought reflect a dynamic that is clearly being driven by the interaction of economic and security concerns. He asserts that Sino-American economic relations have evolved from a basis for cooperation to a new and growing source of conflict between competitors. As mutually beneficial economic relations no longer so clearly help offset other areas of disagreement between Beijing and Washington, keeping bilateral ties on track becomes ever more complicated and demands greater efforts. Yuan then identifies Northeast Asia as a key area in which the potential for serious military conflicts involving the United States and China can be addressed by more concerted efforts at Sino-American cooperation. Because this part of the region lacks the sorts of multilateral institutions that have grown up around ASEAN, Yuan views Northeast Asia as providing a fresh slate for the United States and China to design a new mechanism for cooperation. While acknowledging the difficulties such a project faces, Yuan also argues that such cooperation in the most contentious area of Northeast
Asia could provide the basis for Sino-American cooperation in the rest of the Asia Pacific.

In recent years, both social scientists and policy makers have expressed a growing interest in East Asia. In part, this reflects the tremendous economic strides that have been made throughout the region. It is also due to the rise of China, ongoing concerns about the Korean Peninsula, and Western interests in promoting regional stability. How the rapid expansion of cross-border economic activity in East Asia is linked to political-military relations is a crucial topic that has not been studied in sufficient depth. As the different perspectives of our contributors suggest, however, recent events provide evidence that the interaction of economic and security considerations in East Asia is not just a complex process. The thickening of economic ties amid remaining security concerns and the flowering of institutional arrangements among the countries of the region can be a double-edged sword.

In July 2010, for example, the ASEAN Regional Forum (ARF) served as a venue in which differences of opinion about competing maritime and territorial claims in the South China Sea, motivated partly by economic interests, led to increased tensions and security concerns among some of the region's key countries. Yet at the July 2011 ARF these same countries worked to defuse those tensions, thus furthering a trend that had begun outside of the multilateral setting earlier in the year. This suggests that East Asian regional institutions, like their counterparts elsewhere, do not in and of themselves forestall conflict or ensure cooperation, but instead they establish a pattern of regular interaction and a focal point for addressing vital issues. Such regular interaction can provide an opportunity for member states to clarify conflicting economic or security interests. However, it also establishes a predictable rhythm for attention to such issues that can facilitate attempts to mitigate conflicts if and when the member states see such efforts as useful for repairing relations damaged by disputes.

Outside of multilateral regional institutions, the complex implications of economic and security concerns have also been apparent. In September 2010, a sharp dispute erupted between China and Japan over the arrest of a Chinese fishing-boat captain whose ship collided with a Japanese Coast Guard vessel after he refused to comply with calls to leave disputed waters in the East China Sea. While a disturbing diplomatic standoff between Beijing and Tokyo played out, reports surfaced that China's exports of economically crucial rare-earth minerals to Japan had been halted. Although these reports proved
difficult to confirm, the perception that China was using economic leverage to exert political pressure on Japan fed broader security concerns about potentially worrisome aspects of China’s growing clout in the region. At the same time, however, China and Japan’s interest in sustaining their extensive, mutually beneficial economic ties provided powerful incentives to prevent the incident from escalating. Consequently, despite the incident’s adverse effects on Japanese public opinion toward China and a surge of Chinese anger directed at Japan, once Tokyo decided to release the fishing-boat captain, official relations with Beijing were quickly normalized.

The nexus of economics and security affairs may also be evident in a broader pattern that caught the attention of observers after the global economic crisis erupted in 2008, especially once it became clear that the crisis would cause relatively little damage to China. In 2009–2010, some observers began commenting on what they viewed as China’s more assertive behavior in East Asia, focusing mainly on what they saw as Beijing’s stepped-up efforts to back territorial claims in the South China Sea that were disputed by the Philippines and Vietnam and claims in the East China Sea that were disputed by Japan. To explain this apparent change in China’s regional behavior, analysts suggested that America’s economic difficulties during the financial crisis, together with its military burdens in Iraq and especially Afghanistan, had convinced leaders in Beijing that China’s strength relative to that of the United States was growing more rapidly than previously anticipated (Glaser and Dooley 2009; Glaser and Morris 2009; Swaine 2011; Swaine and Fravel 2011). In this account, America’s domestic and international preoccupations and a rising China’s role as an indispensable global economic actor had created an opening for China to press harder on behalf of its regional interests than had been possible during the preceding decade. Whether such claims accurately described an objective change in China’s policy and behavior or simply reflected others’ subjective interpretation of regional events, the new perception was widespread and was having real consequences. Beijing apparently recognized the problems being created by the perception that it had become increasingly assertive. Those who considered China’s greater regional activism a worrisome challenge to their own interests were beginning to cooperate in ways that could be inimical to China’s security and jeopardize the benefits China derived from robust economic relations in the region. This reality led Beijing at the end of 2010 to reiterate its previous commitment to peaceful development. In doing so, China’s leaders emphasized that a stable security
environment was as essential for its own continued economic rise as for the prosperity of others in the region (Dai 2010).

The aforementioned examples do not constitute evidence conclusively confirming either optimism or pessimism about the security implications of burgeoning economic relations in East Asia. Instead, as is apparent in the varied perspectives contained in the following chapters, such examples illustrate that economic and security affairs in the region have become inextricably intertwined. The nexus of economics, security, and international relations in East Asia demands greater attention and a more concerted effort by students of international political economy and international security affairs to closely coordinate their research agendas. This book constitutes a modest step in that direction.

Notes

1. As reflected in Figures 1.1 and 1.2, whether one focuses on the incidence of military conflicts or on battle deaths, the major data sets on which international relations scholars rely provide clear evidence of this trend. In retrospect, the 1980s marked the beginning of this trend in East Asia, although the trend became most pronounced with the end of the Cold War. In this respect the Uppsala Conflict Data Program and Peace Research Institute Oslo (UCDP/PRIO 2010) data are consistent with the updated list of wars from the Correlates of War project; see http://www.correlatesofwar.org/COW2%20Data/WarData_NEW/WarList_NEW.pdf (Sarkees and Wayman 2010).

2. These figures do not include Taiwan because it is not possible to obtain reliable data on Taiwanese trade before 1990.


4. We also include two internationalized civil wars in our list of wars. One was fought by Laos and Vietnam; the other was waged by Cambodia and Vietnam. These are included because, in both cases, the insurgency was being actively supported by Vietnam.

5. China's preferences about the future of Korea differ from those of the United States, Japan, and South Korea. All four, however, share an interest in minimizing the risks generated by North Korea's nuclear weapons program; this has sustained
multilateral negotiations seeking a diplomatic resolution of the issue. Similarly, although China (unlike the United States) did not embrace the findings of the official South Korean report citing the North Koreans for the sinking of the Cheonan in March 2010, the official Chinese response focused on preventing escalation of North-South tensions and on the need to preserve stability and peace on the peninsula. Beijing's stance on both the nuclear standoff and the Cheonan sinking are consistent with its broader Korea policy since the 1990s: (1) placing top priority on stability to avoid potentially catastrophic turmoil along its northeastern border, (2) refusing to publicly take sides against the North (with whom it still has a treaty of alliance), and (3) engaging in quiet diplomacy and pressure behind the scenes to send the message to Pyongyang that it cannot count on China to rescue it from the consequences its military provocations may trigger.

6. The potential for American entanglement, intended or not, was reflected in the sharp Chinese reaction to U.S. Secretary of State Hillary Rodham Clinton's July 2010 remarks about territorial disputes and maritime rights in the South China Sea. Some interpreted the venue (the ASEAN Regional Forum held in Hanoi) and the American call for multilateral negotiations, as an indication that the United States was taking sides and opposing China's preference for bilateral negotiations to resolve the disputes. Others viewed Clinton's remarks as merely a restatement of long-standing American policy urging the noncoercive resolution of East Asia's territorial disputes and supporting the principle of freedom of navigation on the high seas, along with an offer to play a role in regional diplomacy if the principals should find that helpful (Landler2010).

7. For a comprehensive discussion of cross-strait economic relations and their relevance for China-Taiwan political developments, see Kastner (2009).

8. In addition to the disagreements about naval rights in the South China Sea, the United States and China sharply disagreed about military exercises that the United States and South Korea conducted in reaction to the sinking of the Cheonan. Although not claiming the waters as China's territorial seas, Beijing objected to military operations in the Yellow Sea by the U.S. Navy, especially including the George Washington aircraft carrier, arguing that proximity to China's coast gave it special security interests in those waters. The United States dismissed the concern and reasserted its right to conduct military exercises in international waters, although the initial joint exercise with South Korea was actually held in the Sea of Japan off Korea's eastern coast.

9. Confidence that war is unattractive for all concerned may encourage intransigence and diplomacy backed by military force held in reserve. During the Cold War, military analysts spoke about the stability-instability paradox, arguing that the clear irrationality of general nuclear war made limited conventional wars more likely; states allegedly would believe that they could safely fight small wars because escalation to a major war was so unlikely.

10. This ranking refers to GDP calculated at the market exchange rates for currencies. An alternative approach to calculating GDP is to rely on purchasing power parity (PPP), a methodology that Alan Heston and Robert Summers developed to
adjust for variations in the prices of goods in different countries. The PPP figures depend on local surveys of baskets of representative goods to determine how much nominal GDP figures must be adjusted. In the 1990s, the World Bank adopted the PPP estimates, a change that dramatically increased the reported size of China's (and some other countries') GDP. Using PPP, some estimated that China's GDP was the world's second largest economy more than a decade ago. The PPP methodology has been contested, however, and difficulty in evaluating the validity and reliability of PPP estimates led the World Bank in 2007 to recalculate its PPP estimates, which resulted in a 40 percent downward revision for its figures on China's GDP. China's economy, however, has grown to the point that even by the more conservative exchange rate method, it was larger than Japan's in 2010 (Summers and Heston 1991; Davis 2007; Keidel 2007).

11. Estimates about China's military spending are even more hotly contested than estimates of the country's GDP. In the case of military spending, however, the controversy reflects disagreements about the comprehensiveness of data. China's official military budget is at the low end of the available estimates, with others estimating totals that range as high as twice China's reported total. For the purposes of this volume, however, two facts about which there is little controversy are most important. First, the rate of increase in China's military spending since 1990 has been very large (averaging well more than 10 percent per year). Second, whatever the actual size of China's military budget, since 1990, and especially since 1996, there has been a marked improvement in the quality and quantity of the most modern forces that the PLA deploys. See also Stockholm International Peace Research Institute (2009).

12. The rankings are for ASEAN trade with individual countries. Otherwise, the EU as an aggregate of countries ranks second behind Japan (ASEAN 2009). See also entries in The World Factbook (Central Intelligence Agency 2010a, 2010b); Blustein (2005); Kim and Buckley (2009); Ujikane (2010); Xinhua (2010).

13. Indeed, beyond the region, the central roles of the United States and China, and the importance of consultation between them to address international economic problems, were brought into stark relief during the economic crisis of 2008. Leaders and analysts around the world immediately looked to the United States and China to spearhead responses that would mitigate its worst effects and help spur recovery. The G-20 (which includes China) overshadowed the G-8 (which does not include China) and became the institutional focus for global economic consultation about the crisis. Some even argued for relying on a G-2 (United States and China) to manage the international economy, although this was quickly dismissed by most as at best premature. Along the same lines, Niall Ferguson coined the neologism Chimerica to represent the alleged global preponderance and thorough interdependence of these two economic giants. See Ferguson (2007); Clarke (2009); Bergsten (2009); Economy and Segal (2010).

14. "From June 2002 to June 2009, China's holdings of U.S. securities as a share of total foreign holdings of U.S. securities rose from 3.9% to 15.2%, increasing its
ranking of major foreign holders of U.S. securities from fifth to first. Over this period, China’s holdings grew by nearly $1.28 trillion (or 707%), by far the largest increase in U.S. securities holdings of any other country. . . . The largest type of U.S. securities held by China are short-term and long-term U.S. Treasury securities, which are used to finance U.S. federal budget deficits. . . . China’s holdings of U.S. Treasury securities rose from $18 billion (or 9.6% of total foreign holdings) at the end of 2002 to $895 billion in 2009 year-end. . . . As of April 2010, those holdings stood at $900 billion, which were 23.6% of total foreign holdings. China has been the largest foreign holder of U.S. Treasuries since September 2008” (Morrison 2010: 11).

15. Such interdependence reflects the high costs and difficulty of adjusting to any major disruption in their economic relationship that both sides face. In this sense, the relationship displays vulnerability interdependence rather than just sensitivity interdependence. See Hirschman ([1945] 1980); Keohane and Nye (1977); Baldwin (1980). Although the benefits each side derives from the relationship are not equal, the costs of a disruption for both (and given their global roles, the fallout for others, as well) would be severe—especially in terms of its impact on employment, inflation, and financial markets. The depth and breadth of the economic relationship also produces sensitivity interdependence. For example, adjustments in interest rates and stock indexes in one country reflect reactions to economic announcements and decisions in the other. Announcements by the U.S. Federal Reserve Board about interest rates or comments about the composition of China’s foreign exchange reserves elicit quick reactions among investors in both countries.

16. As noted above, the Taiwan Relations Act, though not providing the kind of security guarantee embodied in a bilateral treaty between states, signals the possibility of U.S. intervention if conflict erupts between China and Taiwan. Since the late 1990s, U.S. policy has explicitly opposed any attempt to alter the status quo in the Taiwan Strait except by peaceful means that are acceptable to both sides. Other than the distinctive relationship with Taiwan, in East Asia the United States has treaties of alliance with the Republic of Korea, Japan, the Philippines, and Thailand, and it has increasingly close ties with Vietnam.

17. The United States maintains military bases in the Republic of Korea and Japan; has agreements facilitating military operations with Thailand, Singapore, and the Philippines; and maintains naval and air bases in the U.S. territory of Guam. The American view about the regional benefits of its military presence is articulated most clearly in reports issued in 1995 and 1998, see East Asian Strategy Report (1998).

Works Cited


If there is one idea that has consistently influenced western foreign policy since the Cold War, it is the notion that extending interdependence and tightening economic integration among nations is a positive development that advances peace, stability, and prosperity. As a post-Cold War idea guiding U.S. and European foreign policy, there is much to be said for it. The absorption of Eastern Europe in both the European Union and NATO helped consolidate market democracy. Globalization led to unprecedented growth in western economies, and facilitated the ascent of China and India, among others, taking billions of people out of poverty. Access to the international financial institutions also offered emerging powers the strategic option of exerting influence through existing institutions rather than trying to overturn them. Some policymakers and experts believe that this process holds the key to continuing great power peace and stability.

Until recently, countries have acted as if increasing and freewheeling economic interdependence is a force for good in itself. Yet over the past five years it has become increasingly apparent that interdependence and integration carries strategic risks and challenges with it. These include a much greater level of volatility in the global economy, potentially destabilizing vulnerabilities in the U.S.–China bilateral relationship, tensions in Asia that stem in part from the reliance of small economies upon China, and an existential crisis in the European Union. Nations have begun to hedge against some of these risks by reining in some types of economic interdependence and by adopting national security policies to counterbalance them. For example, South East Asian nations have deepened their strategic ties to the United States to offset the effects of economic interdependence with China, and Western countries are placing restrictions on the activities of Chinese technology companies.

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Two factors have caused states to reassess the benefits of increasing interdependence and ever deepening integration. The first is that the tremendous increases in economic interdependence and integration have produced complexities in the global economy that create the conditions for major crises, such as the Eurocrisis and the 2008 international financial crisis, which may be beyond the capacity of states to manage effectively. The second is that states are increasingly engaged in geopolitical competition with each other, albeit in an interdependent world. China, the world’s second-largest economy, is a geopolitical competitor of the United States, Japan, and India, and it also has significant disputes with many of its neighbors in South East Asia. The United States and Russia once again have a competitive relationship—particularly over Syria, where a proxy war seemed possible in August 2013, but also more broadly. In a stagnant global economy, nationalism is on the rise in many countries, albeit to differing degrees. Post-Cold War integration and interdependence was pursued at a time when geopolitical competition between the major states was low and the prospect for cooperation seemed great. The key strategic question now is: what will happen if security becomes a more prevalent consideration of state behavior? What will interdependent competition look like?

States are seeking to carve out spheres of independence for themselves to hedge against the risks of interdependence, and these efforts are likely to accelerate over the next decade. These spheres of independence will be imperfect and porous, but they likely mark the first step in a strategy to preserve the state’s autonomy in the face of greater volatility and uncertainty. Critically, this effort will not involve reducing trade ties. Modern trade is integral to national economic health and incredibly complex. States will still struggle over expanding free trade as they always have, but they will be deterred from protectionist measures to roll back the status quo. In some cases, states will seek to hedge against the risks of certain types of trade, such as asymmetric trade with a potential rival, but this will entail countervailing security and economic ties rather than reducing trade itself. Primarily, the spheres of independence will focus on those aspects of interdependence that are perceived to pose a systemic threat to the nation’s interest (e.g. capital flows, financial imbalances, energy interdependence).

In this article, I focus on three areas where interdependence will pose strategic challenges for actors involved to manage: the bilateral relationship between the United States and China, East Asia as a region, and the global economy. The challenge facing the United States and other countries will be to manage the integration process effectively, encouraging the positive elements while rolling back or mitigating the negative. Done right, strategically managing integration and interdependence should produce a stronger and more sustainable international order. Toward this end, I make a series of recommendations including U.S.–Chinese cooperation to explore ways to selectively reduce each other’s leverage on a mutual basis, continued U.S. rebalancing
toward Asia to mitigate the effects of asymmetric regional interdependence, reforming international financial institutions to include regulation of financial markets, and greater flexibility in European integration.

The U.S.–China Bilateral Relationship

Any treatment of modern interdependence must begin with the United States and China. Not only are they the two largest economies in the world, but they are also geopolitical competitors. Interdependence between these two countries continues to reach new heights across multiple areas. For example:

- In 2012, the United States imported $425.5 billion of goods from China, up from $321 billion in 2007, and $125 billion in 2002. The United States also exported $110 billion worth of goods to China in 2012, up from $63 billion in 2007, and $22 billion in 2002. The U.S. trade deficit with China is $315 billion, up from $258.5 billion in 2007 and $103 billion in 2002.\(^2\)
- At the end of May 2013, foreign investors held $5.678 trillion in U.S. debt which, according to the Congressional Research Service (CRS), is “the largest share of privately held public debt attributed to foreign holdings since these estimates have been compiled.”\(^3\) Of that, China holds approximately 23 percent, the largest of any foreign holder. (Japan is the second-largest, with approximately 19.5 percent.)\(^4\)
- Educational exchange between the United States and China is rapidly increasing. China is the fifth most popular destination for U.S. students studying abroad, and the number of U.S. students studying there has more than doubled between 2004-05 and 2010-11, the last year for which data is available.\(^5\) Meanwhile, China tops the chart of foreign students studying in the United States, with over 194,000 in 2011-12. This is more than a 300 percent increase since 2005-06, over 25 percent of the total number of foreign students, and almost twice the number of the second-ranking country, India.\(^6\)

Senior policymakers seem to believe that interdependence will reduce tensions between the United States and China. Interdependence is the key reason why China’s President Xi Jinping called for “a new model of major country relationship.”\(^7\) As former Secretary of State Hillary Clinton put it, “Interdependence means that one of us cannot succeed unless the other does as well. We need to write a future that looks entirely different from the past.”\(^8\) Chinese Premier Li Keqiang speculated “I don’t believe conflicts between big powers are inevitable...Shared interests often override their disputes.”\(^9\)

The United States and China are highly interdependent with each other, but they are also geopolitical competitors in the Asia–Pacific.\(^10\) To a significant extent, the United States and China are competing for regional influence, including whether the United States can remain the hub of the regional security order, how maritime territorial...
disputes in the South China Sea and East China Sea are to be resolved, and whether the United States can project power quickly into the region. China and the United States are also at odds on several issues that could escalate into a crisis including Taiwan and the future of the Korean peninsula.

Thus, the U.S.–China relationship is best understood as one of interdependent competition. It is unique in modern history. We have to look back to the period before World War I for cases of such levels of interdependence between great power competitors. The Western world was largely independent of the Soviet bloc during the Cold War, and interwar Europe was much less interdependent than it was a quarter of a century earlier.11 The apparent tradeoff between the common interests generated by interdependence and the tensions stoked by geopolitical competition make it difficult to predict where U.S.–China relations are headed.

Even if interdependence continues to grow, it will not remove the causes of U.S.–China security competition. Each side is more likely to believe that the other will compromise on issues where they differ, but they will be unwilling to compromise themselves.12 Take Taiwan as an illustration: it is inconceivable that either China or the United States would abandon their respective positions and accede to the will of the other for the sake of economic inducements. In fact, in practical terms, it is hard to imagine any controversial area where a U.S. president would back down from a formal commitment for economic reasons. Rather, the danger is that Washington and Beijing could miscalculate by assuming that the other side is more commercially minded than they are. So, interdependence and geopolitical competition will continue to exist. When the two come into conflict, geopolitical calculations will be uppermost in policymakers’ minds. The question that they are coming to grips with is: what impact will interdependence have? Does it always help the cause of peace, or are there occasions when it will hurt?

The key to understanding the strategic effects of interdependence on the bilateral relationship is to understand that it is not a monolithic force. Some types of interdependence will encourage cooperation and decrease tensions. Others will have the opposite effect, increasing tensions and friction. How can we tell the difference between the two? The positive type of interdependence is one where the benefits are shared and it is difficult for either side to turn it into leverage that can be used to inflict disproportionate damage on the other. To use the language of international relations theory, there is symmetric vulnerability. The negative type of interdependence is one where one side gains disproportionate leverage over the other and could seek to use this leverage as an economic weapon at a time of crisis. If one side has an asymmetric vulnerability that the other side tries to exploit, it might also retaliate in another area—horizontal escalation—in which it holds an asymmetric superiority. This increases the risk of miscalculation and a spiraling crisis.

Trade: Now a Positive Form of Interdependence

There is a vast literature on the relationship between trade and conflict, with liberals arguing commerce creates shared interests in cooperation and realists arguing that it rarely evenly divides and can create vulnerabilities.13 However, there is a new element in modern trade. The international trading system, with its vast supply chains, is so complex that no one can figure out how to manipulate it in such a way that would
disproportionately hurt the other side. As Stephen Carmel, a senior executive at Maersk Line, Ltd, one of the world’s largest shipping companies, has put it:

To say that the world’s economies are interdependent does not adequately, or even remotely, express the true nature of today’s global economic activity. Vulnerabilities exist everywhere, the most serious being those obscured by the very complexity of the system. The demise of the meaning of the ‘made in’ label means we can no longer gauge with any accuracy where the incidence of a specific trade sanction will fall or where failures in the global supply chain may manifest themselves.14

Simply put, the United States and China have no way of significantly reducing trade with each other through protectionism without setting in motion a general unraveling of the global trading system that each relies upon. Thus, trade produces little leverage for either country; meanwhile, it gives each country a stake in the success of the other.

**China’s Holdings of U.S. Debt: Mutual Harm Not Enough**

Chinese holdings of U.S. debt is a leading example of negative bilateral interdependence. As detailed above, these reached record levels in May 2013. Analytically, there are two questions here: One is whether it is bad to have foreigners holding such a large share of a growing U.S. debt. The other is whether there is something special about China since, unlike Japan for example, it is not an ally of the United States. For reasons of space and because it merits an article to itself, I leave aside the question of whether growing debt is itself a national security threat. From a pure economics perspective, it is better to have foreign investors buy some U.S. debt than to have the burden fall entirely on U.S. investors. As the CRS puts it, “all else equal, foreign purchases of Treasury securities reduce the federal government’s borrowing costs and reduce the costs the deficit imposes on the broader economy.”15

With China, the question is whether its holding U.S. debt is stable from a national security viewpoint. While U.S. officials maintain that China’s holdings exercise no influence over U.S. policy, some Chinese officials and analysts have hinted that they may consider such a strategy if China’s sovereignty was threatened.16 China’s holdings are also politically controversial with the Chinese people.17 Most analysts believe that China cannot use its holdings of debt as a weapon because China’s economic interests would be badly damaged if it began to dump U.S. debt.18 This is true most, but not all, of the time. There are two scenarios in which it could destabilize U.S.–China relations.

The first is in a real political crisis between the United States and China. If the United States and China were on the brink of conflict over Taiwan or disputed islands in the East or South China Sea, Beijing may calculate that unloading U.S. debt would hurt the U.S. economy more than the Chinese economy, either in absolute terms or in the relative pain that each country could endure during the crisis (if the Chinese felt more strongly about Taiwan than the American people, for example, this balance would be in their favor). Even if China did not execute this strategy, giving the impression that it
would be willing to do so could be effective, especially if Beijing were simply trying to
deter the United States from taking an action (such as entering a conflict on the side of
an ally) rather than compelling it to do something.

The second scenario is if world markets lost
confidence in U.S. treasuries and began to offload
them. In such a case, the United States would highly
value China’s cooperation in continuing to hold U.S.
debt and Beijing could seek to leverage it into political
influence. China would otherwise serve its own
economic interests by unloading its holding before the
rest of the market does; indeed, it would need a strong
incentive not to do so. In the past, the United States
could invoke a security alliance to encourage its
economic partners to take actions that were not in
their immediate economic interest for the wider good. But since the United States and
China are competitors, not allies, that would not work.

The risks of China’s vast holdings of U.S. debt should not be exaggerated, but
neither should these be dismissed. There are specific scenarios in which it could prove
destabilizing, and in the present environment—of increasing geopolitical competition
and a volatile global economy—Washington and Beijing should take them seriously.

**Information Technology and Cyber-Risk**

A second area where interdependence is having negative strategic effects is the
integration of networks and information technology. The United States is concerned
that China is using market openness to penetrate U.S. companies and technologies in
ways that Beijing could strategically exploit at a time of crisis. In a 2013 interview,
former director of the CIA and NSA (National Security Agency) Michael Hayden said,
“if you’ve got a foreign company supply you with essential communications infrastructure
and/or helping build your network, the detailed knowledge that company obtains can be
a powerful intelligence tool for foreign security services to leverage off to map out and
target your telecommunications network for espionage and other malicious purposes.”

Later in the interview, Hayden singled out Chinese technology giant Huawei,
saying it represents an “unambiguous national security threat” to the United States
and Australia. In 2012, a House Intelligence Committee Report into the activities of Huawei
and ZTE, another Chinese telecommunications company, recommended that both be
viewed with suspicion and be banned from mergers, acquisitions, and takeovers in the
United States or from supplying vital components to the U.S. telecommunications
infrastructure.

Huawei and ZTE are meeting with stiff resistance in the United States, but they
have had a more mixed experience elsewhere: Taiwan, Germany, India, and Australia
blocked Huawei and/or ZTE from major contracts. However, Huawei enjoyed the
support of UK Prime Minister David Cameron in making a £1.3 billion investment in
the United Kingdom (despite considerable concerns from Parliament), and the European
Union as a whole continues to do business with it. Unconditional interdependence
would allow Huawei and ZTE to fully avail of all of the opportunities globalization
offers—but there is widespread recognition that technology infrastructure is a special
case where “Trojan horse” concerns are real. Further integration is unlikely to ease tensions; it will only exacerbate them.

**Energy**

The U.S. energy revolution may mean the United States is becoming less dependent upon the Middle East for oil, but China is moving in the opposite direction. As China’s economy grows, it has an almost insatiable demand for energy imports. The International Energy Agency (IEA) estimates that by 2035, Asian countries will account for 90 percent of the Middle East’s export of oil.\(^{23}\) Approximately 80 percent of China’s oil imports already flow through sea lanes patrolled by the U.S. Navy.\(^ {24}\) China worries that the United States could choose to cut off these “lifelines” during a major crisis in an effort to change Chinese behavior. As Zhang Wenmu, a Chinese academic and strategist, put it, “China is almost helpless to protect its overseas oil import routes. This is an Achilles heel to contemporary China, as it has forced China to entrust its fate (stable markets and access to resources) to others…If one day, another nation(s) finds an excuse to embargo China, what can China do?”\(^ {25}\) As geopolitical competition between the two grows, so too does this fear.

For China, energy interdependence is dependence upon the U.S. Navy. Naturally, China finds this intolerable, so it is developing capabilities and a strategy to ensure access to these resources.\(^ {26}\) Part of it involves diversifying sources of supply. For instance, China recently signed a deal with Russia to import $270 billion of oil over twenty years.\(^ {27}\) But diversification of supply won’t be enough, so China’s strategy also includes transforming the navy from one designed for coastal defense to one that projects power, considers a forward presence overseas, and makes preferential agreements with resource suppliers. New naval capabilities may be acquired for defensive purposes, but its neighbors, including India and Japan, will also see it as a strategic threat. For the purposes of this article, the key point is that China’s naval ambition is influenced and shaped by energy interdependence. It is a desire to push back against the market for geopolitical reasons.

**Interdependence Depends…**

There are aspects to bilateral interdependence between the United States and China, such as trade and educational exchange, which contribute toward mutual cooperation as well as understanding and are likely to endure. However, other aspects have raised concerns. Either the United States or China will see Chinese holdings of U.S. debt, cyber-interdependence, and energy interdependence as a significant source of threats. Some people will argue that this vulnerability is actually a positive since it can deter the other state from taking destabilizing actions. For example, if China were to invade Taiwan, the United States could respond by cutting off supplies of energy. Or conversely, if the United States were to support a unilateral declaration of independence by Taiwan, China could respond by offloading its holdings of U.S. treasuries.

There is reason to question such claims. Economic weapons alone rarely compel much smaller countries to capitulate, let alone large ones.\(^ {28}\) If the United States or China find themselves facing the threat of economic warfare, they are likely to seek to reduce their vulnerabilities and may retaliate in kind. The United States and China will
have to make a strategic choice: in the hope of achieving a greater degree of stability, do they want to use interdependence between them to maximize the leverage that each has over the other, or do they want to reduce this leverage (and some types of interdependence)? Thus far, neither country has answered this question.

**Asymmetric Interdependence in East Asia**

The Asia–Pacific region contains the world’s three largest economies, its most populous areas, outstanding territorial disputes, a mix of authoritarian and democratic regimes, and multiple security dilemmas. The International Monetary Fund (IMF) projects Asia will lead the recovery from the great recession. Meanwhile, its geopolitical characteristics are unique in modern history: its economic activity is largely organized around China, while its security order is largely organized around the United States. There is very little precedent for such a dichotomous structure. Geopolitical competition in the first half of the 21st century is likely to see the Asia–Pacific region as its center of gravity.

China is Asia’s largest economy and the largest market for most of its neighbors. According to a report by the United Overseas Bank (UOB) of Singapore, China accounted in 2011 for 11.5 percent of ASEAN’s total exports—more than any other single nation and more than the EU—a number up from 3.9 percent in 2000. Moreover, as John Wong of the East Asia Institute has put it, China’s production network means that its economy “operates not just as an engine of growth for the [East Asia] region but also as a catalyst of regional economic integration.”

China is also the world’s largest consumer of many natural resources and commodities including steel, oil, gas, and aluminum. Its economic growth created a commodities boom, which was the primary reason countries like Australia did not fall into recession after the financial crisis.

The rise of the China-centric economic order has generated fears among its neighbors that China would use its disproportionate economic power to upend the status quo and create a new regional order organized around Beijing’s interests and preferences. China has been willing to use economic sanctions when its interests are threatened, including on bananas and tourism in a dispute with the Philippines over the Scarborough Shoal, on rare earth metals in a dispute with Japan over the arrest of a Chinese fisherman in 2010, or with popular protests and boycotts of Japan in response to its purchase of the Diaoyu/Senkaku Islands in September 2012.

China’s neighbors have also been concerned by the impression Beijing has given that China should get its way more as its economy grows. For instance, many remember the comment by then-Foreign Minister Yang Jiechi who remarked in 2010 at the ASEAN Regional Forum in Hanoi that “China is a big country and other countries are small countries, and that’s just a fact.” These fears find their roots in traditional realist critiques of asymmetric interdependence. In his seminal work, *The Structure of International Trade*, Albert Hirschman showed how a similar economic imbalance in the 1930s created dependencies that enabled Germany to coerce and pressure smaller states in Central Europe. According to this logic, if other states become dependent on China, China can threaten to cease trade ties in an effort to coerce the smaller state. Because it is so much larger than most of its neighbors, China has almost all the
leverage. It can cut off one of its smaller neighbors and feel little effect. Also, the mere fact that trade with China is so important will lead to the creation of pro-China interest groups and constituencies in the smaller state, or so the argument goes.

The fears of a Hirschman-style scenario rose after 2008 when China was perceived to have adopted a more assertive foreign policy, which included pursuing maritime territorial claims, using smart sanctions against companies or countries that defied China on Taiwan, Tibet, or other core interests, and reminding its neighbors that they should accommodate China’s interests. With a more assertive foreign policy, maybe China would try to use its economic power as leverage? However, having recognized the risk of an asymmetric economic order early on, China’s neighbors set about trying to balance its negative effects. As a 2008 RAND report said, even before China’s assertive turn, “high levels of economic interactions and positive views of China are not strongly correlated.”

The region’s attempt to balance asymmetric interdependence with China has four pillars. The first is to deepen security ties with the United States. Australia, Japan, the Philippines, and South Korea all sought to deepen their U.S. alliances, which Washington facilitated through the rebalance (or pivot) strategy. Non-ally countries like Indonesia, Vietnam, and Burma have also engaged with Washington, which many interpret as partly designed to counterbalance Chinese influence.

The second pillar is to deepen security ties with other Asian nations. A report by the Center for a New American Security (CNAS) elucidates this, saying the regional security environment “is no longer solely defined by the U.S. hub-and-spoke alliance system. Instead, a more diverse array of bilateral security ties is emerging among Asian countries. Regional actors are integrating with each other in unprecedented ways, from India training Vietnamese submariners to Japan’s first security agreement outside the U.S.–Japan alliance (signed with Australia) to countries turning to their neighbors for arms.”

The third is to deepen regional institutions and architecture, including ASEAN-centered dialogues and processes as well as bilateral FTAs with other Asian nations. Southeast Asian states increasingly recognize the need to pool their resources in order to be considered a legitimate counterweight to regional counterparts and powerhouse economies, like China and India. Thus, Southeast Asian nations are working toward the fulfillment of the ASEAN Free Trade Area and the creation of an ASEAN Economic Community (AEC) by 2015. ASEAN is also at the center of regional architecture through the ASEAN Regional Forum, the ASEAN Plus Defense Ministerial Meeting (ADMM+), and the East Asian Summit (EAS).

The final pillar is to diversify sources of economic growth, including through the Trans-Pacific Partnership (TPP) and deepening economic ties with the European Union. This effort to build strategic ties and additional economic interdependencies with states other than China is a conscious strategy to counterbalance the effects of asymmetric regional interdependence.

These four components constitute a significant effort to mitigate the negative strategic effects of a China-centric regional economic order by anchoring the United States at the center of a regional security order. Their behavior suggests a preference to maintain the dual order—an economic order generally organized around China, and a security order organized around the United States. However, it is unclear whether these
two orders can continue to coexist indefinitely or if one will cause the erosion or collapse of the other. The past five years allows us to draw some tentative conclusions.

First, little evidence exists that China has been able to use its economic position to push countries into accepting a China-led security order or simply to push the United States out of East Asia. The mere presence of a counterbalancing strategy is evidence of that. Moreover, as described earlier, the trade system is so complex and interconnected that it is extremely difficult to manipulate without damaging one’s own economy. China could use economic sanctions over a political crisis, for example, but over the medium-to long-term, economic sanctions are a double-edged sword since China relies upon its neighbors for commodity imports, export markets, and foreign direct investment. The benefits of being the center of the regional economic order are, to date, more symbolic or theoretical than a means of coercing another neighboring state.

Second, U.S. engagement is critical to ensuring that China cannot use asymmetric interdependence to overturn the existing order. Given the choice between maintaining their independence or growing economically, nations will almost always choose the former. However, these countries must have a willing partner in the United States to remain independent. If the United States is not fully engaged in Asia and not willing to accommodate the desire of Asian nations to hedge against an economically powerful China, those nations may have no choice but to accept Chinese regional leadership. Similarly, if China continues to grow and the region becomes fully dependent upon it far beyond current levels, they may be able to leverage this position into diplomatic influence that could pry countries away from the security order. U.S. leaders must understand that asymmetric interdependence in East Asia is of strategic benefit to China, but the United States can mitigate its effects through deep regional engagement on military, political, and economic matters.

Third, while it is true that U.S. allies have not flipped over to China simply for economic ties, asymmetric interdependence could still constrain U.S. strategy in ways that are advantageous to China. As we have seen above, if China tries to use its economic influence to coerce a U.S. ally in a dispute involving a vital interest, Beijing will not back down. However, the situation may be more complicated for U.S. allies that are not directly involved in the dispute in question. For example, if the United States intervened in a severe crisis between China and Taiwan, or China and Japan over the Diaoyu/Senkaku Islands, it may need the cooperation of other Asian allies to project power in a timely manner. Since these allies are not directly involved in the dispute, they may think twice if interfering involved angering China on something it deemed to be a core national interest. Beijing could be willing to undertake radical action, such as economic warfare, even if it hurts China too. The mere prospect of this scenario would complicate U.S. planning and military operations.

Fourth, geopolitics is also impairing regional integration and interdependence. Take energy as an example. As major energy consumers, China, India, and Japan have an interest in cooperating with energy suppliers to achieve better terms, or in working together to guarantee continued access to energy supplies. At least that is the logic of interdependence and integration. However, geopolitical tensions between China and Japan as well as between China and India make such collaboration highly unlikely. Similarly, geopolitical concerns will limit the extent that nations will open up their
communications infrastructure to Chinese companies, just as was discussed earlier, in the U.S.–China bilateral relationship.

We should expect Asian nations to continue to develop strategic ties to offset China’s role at the center of an Asian economic order. But another risk looms large in East Asia: a sustained downturn in China’s economy would constitute a significant shock to the region as a whole. Chinese commodities demand is already decreasing and will fall much further. Chinese imports will likely plummet. This will lead to some unraveling of regional economic interdependence, not because of policy choices but simply because the key drivers of economic integration—the insatiable demand for closer ties—would disintegrate. This will reduce China’s leverage over its neighbors. If a more humble foreign policy (and a rollback of the post-2008 assertiveness) accompanies this reduction, however, it may also have the ironic, commensurate effect of decreasing the incentive for closer security ties with the United States. In turn, the weakening of the Chinese-centered economic order could also heighten Chinese nationalism in response to worsening economic conditions and a rise in regional geopolitical tensions.

The bottom line is that the United States, China, and China’s neighbors have an interest in a strong Chinese economy that creates and deepens regional interdependencies, even if they are asymmetric. The strategies outlined above can counterbalance these asymmetric interdependencies. It is an imperfect and vulnerable structure, but preferable to the likely alternatives.

Volatile Interdependence in the Global Economy

For the past two decades, the United States championed the process of globalization, and especially the deregulation and integration of the world’s financial markets. This effort included the 1999 repeal of the 1933 Glass–Steagall Act. This Act prevented the merger of commercial and investment banks; relaxed capitalization requirements for banks; deregulated derivatives; and pursued a foreign economic policy advancing the so-called Washington Consensus, which encouraged other countries, particularly those in IMF programs, to open their economies to investment and trade and introduce pro-market structural reforms. This period of deregulation accompanied, and probably contributed to, a massive increase in global economic interdependence and integration. Capital flows exploded; banks became too big to fail. Financial instruments became so complex that even the chief executives of the banks that designed them could not understand them. This deepening interdependence and greater integration produced growth, but it also increased volatility and made the global economy more crisis prone. Indeed, the two-decade period saw major crises in Mexico in 1994, East Asia in 1997, Russia in 1998, and the United States as well as Europe in 2008.

Liberal international theory placed great faith in the process of globalization as a means to create a mutually beneficial global economy, open up societies, and provide the conditions for inter-state peace. But for the first time since the Cold War, the driving narrative behind the global economy is no longer how to increase the openness of markets and economies. Instead, it is how to repair the global economy so it produces growth but is not susceptible to catastrophic crises.

To take one prominent example that illustrates the changing climate, Financial Times correspondent Martin Wolf wrote a book in 2004 called Why Globalization
Works—but today he is one of the strongest critics of unfettered deregulated financial markets.\textsuperscript{42} Cornell University Professor Jonathan Kirshner observed that much of the world does not see the crisis as a black swan—that is, a rare and unpredictable event—but as a direct consequence of the particular model of global capitalism that has been pursued.\textsuperscript{43} The G-20 averted a full scale collapse in 2008 and 2009, but the risk remains. Indeed, some of the problems that drove the 2008 crisis have gotten worse—for instance, the consolidation of too-big-to-fail banks means they are even bigger now than before. As then-University of Chicago Professor and now head of India’s Central Bank Raghuram Rajan put it, “There are deep faultlines in the global economy, faultlines that have developed because in an integrated economy and in an integrated world, what is best for the individual actor or institution is not always best for the system.”\textsuperscript{44}

In this environment, world leaders are looking for ways to insulate themselves from future volatility and crisis. Some of this is multilateral. Countries have agreed on tougher standards for bank capitalization (like Basel III, which regulates capital adequacy, stress testing, and market risk) despite the opposition of the financial industry. They created a Financial Stability Board with responsibility for regulation. Some of it is “minilateral,” or small groups of countries: France, Germany, and some other European nations have come out in support of a Tobin Tax (a tax on conversions from one currency to another, suggested by James Tobin in 1972) or other mechanisms to reduce capital flows, although the practical problems with this proposal are legion. And some of it is national: as Harvard University’s Michael Spence observed, emerging markets are undertaking a series of steps to hedge against future instability, including placing significant parts of their financial sectors under national control, building reserve currency holdings, and limiting the openness and exposure of their financial systems.\textsuperscript{45}

One highly significant feature of hedging against globalization is that it has not included limiting international trade. Actors have made no move toward the protectionism of trade tariffs and barriers.\textsuperscript{46} As described earlier, trade today is so complex that it is almost impossible to manipulate without shooting one’s own economy in the foot. Moreover, trade is widely seen as part of the solution, not part of the problem—the years ahead may even strengthen the positive case for trade. Hans Kundnani, of the European Council on Foreign Relations, has argued that the next wave of technological innovation, such as 3D printing, “could change the [way] manufacturing works and lead to a wave of reshoring,” which would remove one of the grievances of domestic interest groups opposed to trade.\textsuperscript{47} In general, agreeing on new trade deals will prove difficult for the same reasons they always have, but we will not likely see a major rollback of existing agreements. Instead, the new protectionist sentiment is focused on ways of hedging against the real risks that emerge from other parts of the financial system, such as too-big-to-fail banks and dangerous forms of financial innovation.

Some countries, such as continental European nations and large parts of Asia, want to hedge against risk. The Anglosphere economies are more inclined to preserve existing financial institutions and structures and the growth rates they are perceived to provide, although even they have introduced some restrictions on markets (e.g. the
Dodd–Frank Act to clean up U.S. financial regulation). But few states on either side have viable ideas about how to reduce the volatility in the system while maintaining the benefits that it provides. Thus, hedging measures are very limited in scope and are unlikely to dramatically change the character of the global economy.

Future crises will continue to occur, but they will become more difficult to manage. As Duke University professor Michael Mastanduno explains, “the United States is no longer in a position to dictate the terms...[It] no longer enjoys the same type of security leverage it once possessed.”48 This is not to say that the other major economies will seek to undermine the global economy; it is merely to observe that these economies will not be inclined to set aside their own legitimate national interests and take on a disproportionate share of the burden to stabilize the global economy in a future crisis, as Japan and Germany did in the Plaza Accord of 1985. If problems emerge in managing the global economy, countries are more likely to seek unilateral options to hedge against increased volatility and the risks of interdependence.

While unfettered interdependence poses problems in the global economy, it has manifested itself in a very unique way in the Eurozone. The Eurozone suffers from both too much and too little interdependence. It has too much in the sense that it should never have pursued monetary union without integration on fiscal and banking policy, but it did so anyway for ideological reasons. It has too little in the sense that, now with a single currency, it needs to make further progress on that integration. The Eurozone will not likely pursue fiscal and financial union, nor will it seek to unwind the existing arrangement, so it appears destined for a long period of stagnation.49 Germany is, and will remain, the most important power in Europe, using its geoeconomic strength to impose its preferences and protect its interests.50 The inevitable consequence will be a two-tier Europe, with growing political opposition in countries disadvantaged by European integration.

Managing Interdependence: Sifting the Bathwater from the Baby

As the world has hurtled toward ever closer interdependence and integration, the risks of this process have become more apparent and states have begun to hedge against them. During the Great Depression, this hedging including trade protectionism that proved to be catastrophic, but today trade is too complex and embedded in each nation’s economic model to be targeted for protection. Politicians may engage in symbolic actions, but a significant rolling back of world trade is extremely unlikely and undesirable. Instead, politicians are focusing on other areas including those parts of the financial system which can produce shocks and where geopolitical competition may create destabilizing vulnerabilities. For the most part, this is a sensible response to real risk, but it is important that the attempt to manage interdependence is carefully targeted and does not throw the baby out with the bathwater. Thus, policymakers should keep the following recommendations in mind.
First, the United States and China must engage in a dialogue about whether they should work together to reduce the leverage that each has over the other through various forms of interdependence, or if they want to continue on the current trajectory of maximizing each other's vulnerability. The working assumption from the Cold War is that mutual vulnerability is stabilizing, but (as argued above) there is reason to believe that the opposite may be the case. Mutually reducing leverage would include gradually unwinding financial imbalances, safeguarding each nation's technological infrastructure as much as possible, and making each nation more energy secure. At the same time, China and the United States would deepen their relations in positive areas of interdependence such as trade and educational exchange. The key is to find a stable equilibrium that will not lead to an inadvertent spiral at a time of crisis.

Second, the United States should continue its rebalancing to Asia—including a deepening of alliances and partnerships, increased economic engagement, support for regional institutions, and norm building—to provide East Asian nations with a viable option as they seek to hedge against a rising China. U.S. rebalancing, combined with strengthening intra-Asian ties, will help mitigate the effect of Chinese-led asymmetric interdependence. Without robust U.S. engagement, Albert Hirschman's prediction—that a dominant economic power can use its market access to bring neighboring states into its geopolitical orbit—may come true.

Third, states need a way of better managing interdependence in the global economy, including regulating the financial sector. While much has been accomplished since 2008, including the adoption of Basel III standards on banking capital standards, much remains to be done. This is not just a matter of strengthening surveillance through the IMF, although that would help. There also needs to be greater international cooperation and coordination to repair the faultlines in the global economy. Possible options include increasing the capacity of the G-20 or expanding the role of the World Trade Organization or the International Monetary Fund.

A nuanced approach to interdependence will not lead to globalization unraveling. In fact, the world will remain, and will continue to become, more globalized and integrated than at almost any time in history. Crucially, this approach will put interdependence and globalization on more stable footing which will serve the world well as it faces what could become a competitive and volatile couple of decades.

Notes


4. There is a large drop to 3rd place, which is held by a collection of oil exporters with a total of $266 trillion. See “Major Foreign Holders of Treasury Securities,” op. cit.


6. Ibid.


34. For an excellent account of China’s thinking on the use of sanctions in pursuit of its national interest, see James Reilly, “China’s Unilateral Sanctions,” The Washington Quarterly 35, no. 4 (Fall 2012), pp 121-133, csis.org/files/publication/twq12FallReilly.pdf.


37. For an excellent theoretical analysis of the logic behind the regional response to asymmetric interdependence see Darren Lim, “Commerce With Competitors: Economic Interdependence and Security Policy in Contemporary East Asia,” Draft Paper, Princeton University, September 2013.


41. The ignorance amongst CEO’s of major banks of the financial instruments their employees designed and used is vividly portrayed in Michael Lewis, The Big Short: Inside the Doomsday Machine (New York: W.W. Norton, 2010).


Despite high levels of economic interdependence, most parts of Asia are still preoccupied with security concerns. Historical memories have inhibited the fostering of trust among China, Japan, and South Korea, and the legacy of the Cold War lingers in the Korean peninsula and the Taiwan Strait. Military confrontations over national borders are continuing between India and Pakistan as well as between Thailand and Cambodia. Furthermore, maritime security concerns have emerged as a significant issue in the East China Sea and the South China Sea; the search for energy resources has exacerbated these security tensions.

This chapter explores the theoretical and empirical implications of economic-security linkages in Asian politics. It argues that enhanced economic interdependence has become a catalyst in promoting institutionalization of political relations in Asia, but its influence on alleviating political-security tensions and promoting security cooperation is still limited. Moreover, lingering historical animosity reinforced by growing concerns about energy security encourage Asian states to use economic instruments such as trade, foreign aid, and commercial agreements to pursue their key diplomatic objectives.

This chapter is organized as follows. The initial section examines theoretical debates on the economic-security nexus and explores two of its dimensions: first, the relationship between enhanced economic interdependence and the likelihood of interstate conflict; and second, the use by states of economic instruments to achieve political-security objectives. The second section explores the relationship between economic interdependence and regional stability in Asia. It articulates the complicated relationships in sub-regions of Southeast Asia, South Asia, and Northeast Asia. The third section highlights states’ external policies and relations in terms of economic-security linkages. It illustrates these linkages mainly through a case study of China’s policies and relations with other Asian countries.
29.1. The Economic-Security Nexus in Theoretical Context

For a long time, research on security was primarily concerned with the threat, use, and control of military force among states. However, the end of the Cold War became a catalyst in broadening the scope of security studies, and various risk-related issues such as environmental deterioration, health, human rights, food, and poverty became the target of research (see also the chapter by Reimann in this volume). The multidimensional character of security has attracted growing scholarly interest, an important component of which has been linkages between economics and security.

Past research has mainly highlighted two dimensions of linkages between economics and security. The first is the relationship between economic interdependence and international conflict (see Haggard in this volume). There have been intensive theoretical debates on the question of whether or not economic interdependence dampens the likelihood of political conflict. Liberals have argued since the middle of the nineteenth century that economic interdependence is likely to decrease the possibility of interstate conflict in two ways. First, increasing cross-border personal communication accompanied by economic transactions is expected to reduce misperceptions and misunderstandings among states. Interaction and communication between peoples improve the prospects for international cooperation and peace by increasing each people’s knowledge of others and their ways, customs, practices, and concerns (Stein 1993, 249–50). Second, interests created by increasing commercial transactions provide the foundation for stable political relations. Increased economic interdependence makes private actors and government officials recognize that their own wealth and prosperity rely on economic linkages with partners and that military conflict would impose significant costs on their economic benefits and overall wellbeing (Cain 1979; Stein 1993). Commercial exchanges render private traders and consumers dependent on external markets, and the cutting or disruption of commercial ties would bring overwhelming costs for these beneficiaries. Government officials who rely on support from societal groups are forced to attend to interests and demands from these groups.

Increasing economic interdependence accompanied growing economic transactions is frequently supported by multilateral institutions that coordinate the interests of the parties concerned. Subsequently, these multilateral institutions are claimed to create mutual and vested interests among participating states. Once planning and decision-making processes for institution-building begin, some distribution of labor in the expertise and planning capacity is formed with the expectation of continuity of commitment. Such situations can raise the costs of breaking connecting links and may dissuade a state from adopting policy changes in isolation (Ikenberry 2001, 67). Moreover, multilateral institutions can rectify various problems in the anarchical, self-help system—asymmetric information, moral hazard, and potential dishonesty—by providing legal liability that establishes stable and mutual expectation about others’
patterns of behavior; by offering relatively symmetrical information to the members, thereby reducing levels of uncertainty and the risks of making agreements; and by reducing the transaction costs of legitimate bargains and increasing them for illegitimate ones (Keohane 1984).

Realists have presented a contrasting view on the relationship between economic interdependence and interstate conflict (see also Mastanduno in this volume). Formulation of the concept of interdependence, they argue, is vague and elusive, and it ranges from symmetrical interdependence and sensitivity interdependence to vulnerability interdependence, relying on the costs that states would bear when relations between them are disrupted (these terms connected with interdependence are explained in Keohane and Nye 2001). Realists hold that interdependence is not a matter of mutual and symmetrical exchanges among states, and the power inherent in asymmetrical economic relationships does matter for the states concerned (McMillan 1997). Asymmetrical economic interdependence can jeopardize the security positions of states. If a state relies on a trading relationship much more heavily than another state, the net costs associated with attenuating or severing the relationship are far higher for the former than the latter state (Mansfield and Pollins 2001, 836; Barbieri 2002, 3). Such unequal relationships inevitably increase the vulnerability of the dependent state. Interdependence can also lead to increasing insecurity and even increase the likelihood of armed conflict because international trade makes some states overly dependent on the world market, producing uncertainty about the continued and stable supply of vital goods (Gilpin 1977; Mearsheimer 1990). Furthermore, realists posit that the state has a significant degree of autonomy from society in its pursuit of its primary goal of maintaining national security (Simmons 2003). Thus, economic interdependence heightens the possibility of political and military conflicts by enhancing inequalities and uncertainties in interstate relations.

Importantly, security externalities and relative gains underpin the difficulty in realizing the potentially positive relationship between economic interdependence and national security. Gowa (1994) argues that international trade creates “security externalities” by increasing the national wealth of any country engaging in it and thereby enhancing its potential military power. Accordingly, a state tends to enhance trade with an ally while it is reluctant to promote trade with an adversary. Gowa’s argument suggests that international trade will be heavily influenced by security concerns. Grieco (1990) holds that states care about relative gains rather than the potential absolute gains from increased economic interactions. This is because states worry that joint gains from economic interaction that advantage a potential adversary in the present might serve as a basis for political-military strength and produce potential danger in the future. The security externalities and relative gain concerns explain states’ reluctance to promote economic transactions with other states even if such transactions have the potential to produce economic benefits.

The second dimension of the economic-security nexus is pertinent to a state’s external policies. Some scholars have explored how states use economic activities such as trade, investment, and foreign aid as instruments to achieve their strategic and security policy
objectives (Hirschman 1980; Baldwin 1985). The state uses economic power as a tool of influence or enforcement to change other states’ behavior. In this view, economic interactions are part of the toolkit of statecraft, which Mastanduno (1998, 826) defines as “the use of policy instruments to satisfy the core objectives of nation-states in the international system.”

Economic instruments can be used to attain a state’s political-security goals in both the short term and the long term. In the long term, a state seeks to improve its security position by creating asymmetries in its economic and strategic relationships with other states. The state takes advantage of its strong economic base and manipulates economic policies in order to enhance political and security advantages and translate them into military power and political influence. Hirschman’s (1980) study of how Nazi Germany set out to make its central and southeast European neighbors subordinate to its economy is the seminal work on this topic. To attain these objectives, Germany adopted policies to increase the trading partners’ gain from trade and adjust for difficulties in case of trade stoppage. Such policies led the trading partners to rely on the German economy to a significant level. Moreover, strong vested interests to accommodate the source of interdependence with Germany were created in domestic society in the partner countries (Hirschman 1980, 28–29). As Hirschman’s research indicates, after the construction of asymmetrical dependent relationships, the core state may be able to exert political influence and control through skillful means such as extraction—the use of the relationship to extract crucial resources and funds—and entrapment—the transformation of interests among firms and government in the dependent state—(Kirshner 1995).

In the short term, states can rely on economic sanctions and economic inducements as tools to exert pressure on their partners in order to obtain concessions on a specific diplomatic issue. In particular, the state uses economic sanctions such as restrictions on trade, a reduction in foreign aid, or the expropriation of foreign assets. Imposing restrictions on trade requires a strategic calculation of potential costs and benefits. Since trade is basically a mutual activity, the interruption of commercial linkages imposes costs on the state that adopts the measure. Accordingly, in assessing the likely impact of sanctions, it is necessary to examine carefully the extent and mode of dependence, the availability of alternative sources, and likely responses from the targeted state.

Baldwin (1985) considers the purposes of economic statecraft broadly. He suggests that these range from changing the target state’s behavior to engaging in economic warfare, rallying domestic political support, demonstrating resolve to third-country audiences, to simply inflicting punishment. He then contends that the effectiveness of economic statecraft should be judged with an assessment of the costs and benefits associated with alternative policy instruments, and reaches the conclusion that economic sanctions are often successful in achieving their broad objectives. Mastanduno (1998) highlights the issue of what factors influence how state policymakers treat the relationship between international economics and national security, and suggests three elements: the structure of the international system, the specific features of the international strategic environment, and the competitive position of a state in the international marketplace. Mastanduno then explores the integration of economics and security in US statecraft, and concludes that while US policymakers sought to integrate
economic and security policies in the early Cold War period and the post–Cold War years, they separated the pursuit of economic and security objectives in the later phase of the Cold War within a firm bipolar structure. Mastanduno’s research has significant resonance in the development of Northeast Asian economies. Japan, South Korea, and Taiwan could achieve high rates of economic growth largely because preferences for economic and security linkages encouraged the United States to keep its market open while tolerating discrimination from these partners.

29.2. The Limited Influence of Economic Interdependence on Political-Security Conflict

For a long time, Asia has been an empirical target of research on the implications of growing economic interdependence for the possibility of war or military conflict. In the 1990s, Morrison (1997) observed that not only was the level of economic interdependence in East Asia too low to promote substantial security enhancing effects, but it was also difficult to attribute important improvements in regional security affairs to economic interdependence. Narine (2007) holds that the initiatives in promoting regional economic integration are still too nascent and weak to constitute the building blocks for a security community in East Asia, and a security community characterized by a genuine shift in regional identity is unlikely to develop in the near future.

In contrast, several scholars have argued that a positive relationship exists between economic interdependence and the reduction of political-military hostilities in Asia. Berger (2000) contends that the growth of economic interdependence in the form of intraregional trade and foreign investment has pushed up the costs of military conflict and reinforced the political influence of societal groups that favored a cooperative approach to foreign relations. In a similar vein, Ravenhill (2009) argues that transformations in the character of economic interdependence in the form of production networks, evolving economic institutions, and changes in dominant domestic coalitions have increased the costs of conflict for Asian countries (see also Ravenhill’s chapter in this volume). Using a large-sample quantitative method, Goldsmith (2007) examines the correlation of economic interdependence and conflict in Asia. His research found that while the pacific effects of multilateral institutions and democracy were weak, trade dependence was robustly associated with lower levels of conflict in Asia. The effects of economic interdependence on reducing the possibility of conflict may derive from regional states’ purposeful strategy. Kahler (2004) holds that South Korea, Taiwan, and Singapore adopted strategies that deployed economic interdependence to advance their security goals with larger or militarily threatening neighbors.

Previous research generally approached the issue of how economic interdependence influences the possibility of interstate conflict in Asia by focusing on a broad
geographical area of Asia or East Asia. However, it seems appropriate to highlight subregions in Asia because economic interdependence and its possible impacts on interstate conflict vary from one subregion to another.

In Southeast Asia, political leaders have pursued steady economic development to legitimize their political power. They have set up regional institutional arrangements that underpin continuous economic dynamism (see also chapter 35). ASEAN leaders launched the idea of the ASEAN Free Trade Area (AFTA) in 1992. After the AFTA was completed in 2002, they envisioned the creation of the ASEAN Economic Community—an FTA-plus economic arrangement—by 2015. These economic arrangements contributed to increases in intraregional trade and investment. The value of intraregional trade within ASEAN increased from US$52 billion in 1990 to US$181 billion in 2000 and to US$493 billion in 2010.

ASEAN's policymakers have held numerous meetings to advance multilateral institutions in trade in goods, services, investment, transport, information technology, and so on. The exchange of information and views through such meetings has deepened understandings about other states' diplomatic stances and interests, and created vested interests in maintaining stable political relations among the members. Importantly, a distinctive normative structure—the ASEAN Way—has facilitated frank diplomatic dialogues and regional institution-building (Kivimäki 2001; Acharya 2001; Haacke 2003). The major norms in the ASEAN Way, such as consultation, nonintervention in internal affairs, and nonuse of force, have created both regulative effects and constitutive effects on diplomatic behavior, and a common identity among ASEAN members (see Acharya's and Leheny's chapters in this volume).

Since ASEAN members have also expanded trade with extraregional states, the ratio of intraregional trade showed only a modest increase in the new millennium: from 22.8 percent in 2000 and to 24.6 percent in 2010 (see also Dent in this volume). The perceived necessity of increasing intraregional interdependence to avoid high dependence on extraregional economies has created further momentum to promote economic integration. ASEAN members launched the ASEAN Community, and the ASEAN Economic Community became the engine of community building. Moreover, ASEAN members advanced formal, rule-based institution-building in economic integration. In August 2007, ASEAN economic ministers agreed to transform the Common Effective Preferential Tariffs for the ASEAN Free Trade Area (CEPT-AFTA) into a more integrated instrument, and the ASEAN Trade in Goods Agreement (ATIGA) was signed in February 2009. With ninety-eight clauses in eleven chapters, the ATIGA covers a wide range of issues including trade facilitation, customs, as well as standards, technical regulations, and conformity assessment procedures. In trends toward formal institutionalization, the ASEAN Charter was signed in November 2007 and came into force in December 2008. The charter has clauses regarding settlement of disputes among member states such as good offices or mediation by the chairman of ASEAN or ASEAN secretary-general (Article 23) and the reference of unresolved disputes to the ASEAN Summit (Article 26). Thus, enhanced economic interdependence stimulated
the formal, rule-based institutionalization of interstate relations, and such moves proliferated in political and security areas.

ASEAN members generally recognize the importance of rules and procedures that the ASEAN Charter and other agreements stipulate. However, they have not necessarily respected them in real interstate conflicts. When the Thailand-Cambodia conflict on national borders escalated in 2010, ASEAN’s chair countries proposed mediation to settle the conflict peacefully. Bangkok resisted such proposals, preferring a local, bilateral resolution. In Southeast Asia, institutionalization of interstate relations has been advanced, but the influence of such institutions is still hindered by historically oriented regional politics and domestic political struggles.

In the case of South Asia, states are members of a multilateral organization, the South Asian Association for Regional Cooperation (SAARC). Established in 1985, the SAARC is a comprehensive regional institution that covers cooperation in economic, social, and cultural fields. SAARC members have launched two trade initiatives. The South Asian Preferential Trading Agreement (SAPTA) was launched in 1995 and expired in December 2003. Then, the Agreement on South Asian Free Trade Area (SAFTA) was signed in January 2004 and came into force two years later. Under SAFTA, the member states aimed at lowering tariffs to 20 percent in the first two years, and then to zero in the second phase ending in 2015.

The impact of regional trade arrangements on intraregional trade has been limited in South Asia (see also Dent). The ratio of intraregional trade in the region has remained low: a mere 4–5 percent since the new millennium. Even though member countries adopted preferential trade arrangements, they maintained various protective measures. Trade liberalization within SAFTA has been hindered by long negative lists, safety clauses, restrictive rules of origin, and so forth (Pattanaik 2006). Equally important was that the lack of trade complementarity undermined the growth of economic interdependence. A country in South Asia is unlikely to be a supplier of its neighboring country’s leading import products (Sáez 2008). It is unlikely that a trade relationship in the region will produce such significant economic interdependence that it will have an effect on the reduction of interstate conflict. On the other hand, interstate conflict in the region has had negative effects on the development of economic interdependence.

While the SAARC has played a critical role in providing a venue for diplomatic contacts among member states, its presence and activities have not had a strong influence on interstate conflict. This was largely because bilateral issues were excluded from the SAARC’s purview in order to avoid a situation in which political conditions would stall regional economic cooperation (Khan 2009). More fundamentally, SAARC members have failed to establish strong political and economic unity. The weak unity has much to do with the fact that politics in South Asia has been dominated by one hegemonic state—India—which has an unresolved conflict with Pakistan over Kashmir. India has not displayed much interest in regional multilateral institutions, preferring a bilateral diplomatic approach. Moreover, this regional hegemon has had weak stakes in deepening economic linkages in South Asia because its neighbors are small countries; rather,
it has pursued closer links with the more dynamic economies of Southeast Asia and Northeast Asia.\textsuperscript{4}

Since the early 1990s, China, Japan, and South Korea—the major states in Northeast Asia—have gradually deepened economic interdependence through expanding trade and investment. The share of intraregional trade among the three states increased from 12.3 percent in 1990 to 19.0 percent in 1996 and to 21.9 percent in 2010. In 2010, China was the primary trade partner for South Korea and Japan, and Japan was the second largest trade partner for China and South Korea (see also Dent). South Korea was the third largest trade partner for Japan and China.

Liberals posit that efficiency gains from heightened interdependence encourage private actors to favor stable political relations, as explained further in Haggard’s chapter. In the first decade of this century, major business groups in Northeast Asia began to express their interests in closer regional cooperation. In 2009, business associations of the three states—the China Council for the Promotion of International Trade, the Japan Business Federation, and the Federation of Korean Industries—began the China-Japan-Korea Business Summit. The three associations had organized trilateral dialogue meetings even before 2009. The business summit after 2009 became a more institutionalized meeting to be always held on the sidelines of the trilateral summit among political leaders. At every business summit meeting, the three associations have issued a joint statement that encouraged political leaders to promote trilateral economic cooperation and harmonize approaches to address global issues.

Growing economic interdependence induced the three states to coordinate economic interests through various trilateral institutions. In December 2008, the three states adopted the “Action Agenda for Improvement of the Business Environment,” which spelled out concrete measures to improve the business environment such as transparency in laws and regulations, the protection of intellectual property rights, a dispute consultation mechanism, and the coherence of national and local administrations (Yoshimatsu 2010). In May 2012 the three states signed a trilateral investment agreement as the first legal framework in the economic field. By 2011, the number of trilateral consultative mechanisms had increased to more than fifty, including seventeen ministerial meetings.

In September 2011, the Trilateral Cooperation Secretariat was established in Seoul. The secretariat is expected to play a valuable role in facilitating communication and talks among policymakers and the sharing of information that is conducive to further cooperation. The three states proclaimed in their 2012 joint statement that they would advance cooperation in nontraditional security issues, such as piracy, energy security, cybersecurity, communicable diseases, terrorism, and proliferation of weapons of mass destruction (WMD).

It is not easy, however, to discern a positive influence of economic interdependence on traditional security areas in trilateral relations. Japan and South Korea hoped to refer to the North Korean security crisis in the summit’s official documents. Yet China was cautious about such a commitment because of its concern about the possible impact on the relationship with its traditional ally, North Korea. At the time of writing,
this initiative has further stalled as a result of tensions in relations among the three parties over territorial and other disputes.

The positive influence of economic interdependence on traditional security areas has, though, at times shown its effects in shaping bilateral relations. Current ties between Japan and China are in 2013 fraught, but when Chinese president Hu Jintao made a formal visit to Tokyo in May 2008, Hu and Japanese prime minister Yasuo Fukuda issued the Joint Statement on the Comprehensive Promotion of a Mutually Beneficial Relationship Based on Common Strategic Interests. The statement contained a phrase indicating that the two countries would work “to enhance the exchange of high-level visits in the area of security, promote various forms of dialogue and exchange, and further enhance mutual understanding and trust” (MOFA Japan 2008). Both governments, in the past, have promoted defense cooperation in order to advance the spirit of the statement. For instance, when the Japan-China defense ministers’ meeting was held in November 2009, the ministers organized a joint press statement for the first time, referring to the first implementation of joint exercises related to maritime search and rescue, as well as to the establishment of a maritime communication mechanism between the defense authorities. Although cooperation was relevant to very specific areas, it could be regarded as an important necessary step to deepening security relations. Were relations to improve between these two states, then this groundwork could prove helpful to the further enhancement of their ties.

As I explain later, the Japanese government conceived of security comprehensively to include economic dimensions. The growing importance of economic linkages encourages China, Japan, and South Korea to consider national interests and security broadly, giving due attention to nonmilitary, functional aspects. Practical and realistic benefits that derive from economic linkages can help to sustain economic growth and social stability, the core interests of national policymakers. The development of policy networks involving various state and nonstate actors for expanding such benefits may contribute to mitigating possible political hostility and security tension.

As the above explanation indicates, discernible diversities exist in subregions of Asia in terms of the level of economic interdependence and its effects on political-security relations. Despite such diversities, extensive economic interdependence offered a stimulus to the development of multilateral institutions (see Stubbs and Mustapha in this volume). However, the potential positive effects of such multilateral institutions on political cooperation and security stability have been offset by asymmetrical power relations and complicated regional politics.

### 29.3. Growing Reliance on Economic Instruments for Diplomatic Objectives

In Asia, substantial research has been conducted on Japan’s use of economic instruments to pursue political and security objectives. After defeat in the Second World
War, Japan pursued a route to develop as a nonmilitarized trading state. Such a development route derived from the bitter experience of the Pacific War; it was encapsulated in the Yoshida Doctrine. The social norms of antimilitarism reinforced by Article 9 of the Japanese Constitution also helped to define Japan’s security policy (Katzenstein and Okawara 1993).

The pursuit of a nonmilitarized trading state strategy did not imply that Japan was indifferent to national security issues. Japan considered national security with due attention to economic dimensions, and its government formulated the concept of “comprehensive national security” in the late 1970s (Akaha 1991; Hughes 1999). This derived from new international developments in the 1970s such as the collapse of the Bretton Woods system, the energy crises, and global economic recession and resultant trade frictions. In particular, the energy crises resulting from the two oil shocks underlined Japan’s resource-scarce vulnerability. The comprehensive national security doctrine considers national security in a broad and integrated manner in terms of objectives and measures. The objective of security maintenance extends from military defense and alliance maintenance to nonmilitary aspects such as the reliable supply of raw materials and foodstuffs as well as stable access to foreign markets for Japanese goods. To pursue this kind of national security, the government placed stress on pursuing diplomatic, economic, and defense measures. The measures include maintaining a strong military alliance with the United States, the creation of stable diplomatic relations with neighboring states, and the establishment of closer ties with resource-rich nations.

Japan’s concept of comprehensive national security has two critical implications in terms of economic-security linkages. First, technological and economic capabilities were regarded as crucial instruments to maintain national security and advance the national interest. Heginbotham and Samuels (1999) characterize Japan’s foreign policy as “mercantile realism,” in which policies designed to enhance technological and economic fortunes are pursued to increase a state’s political leverage and independence even in the absence of military-security considerations. Japan did not take advantage of its economic prowess to increase military power, but regarded declining techno-economic power as a threat to its national security. Second, Japan came to link a stable international economic order to the maintenance of national security. In the 1960s and 1970s the Japanese government used foreign aid to pursue neomercantilist objectives: especially the creation of trade opportunities and investment expansion of Japanese firms in overseas markets (Hatch and Yamamura 1996). After the 1980s, it gradually reformulated its external policies including those on foreign aid, with the objective of sustaining a favorable international environment for its national security (Chan 1992; Kato 1998). While the liberal international economic order was regarded as a factor contributing to Japan’s comprehensive national security, growing economic capabilities allowed Japan to make substantial commitments to sustaining the liberal economic system that gradually eroded after the 1970s.

In the new millennium, China became a main target of research on the relationship between economic policy and political-security objectives. China’s emergence as
the world’s second largest economy encouraged researchers to focus on two aspects of linkages between economic instruments and security concerns in Chinese external relations. The first concerns the importance of the stable supply of natural resources as the basis of national security. As in the case of Japan in the 1980s, China regarded the security of supply of energy resources as a factor directly linked to its national security, as Jain discusses in this volume. Such considerations became particularly salient as rapid economic growth sharply increased domestic energy consumption.

In pursuit of these strategic objectives, China intensified its commitments to the exploitation of energy resources in Central Asia. China negotiated contracts to build pipelines to carry gas from Central Asia to China, such as an agreement with Turkmenistan in 2008, which would carry four-fifths of the country’s gas production and supply nearly half of Chinese consumption. The contract represented an intrusion into what Russia perceived as its sphere of influence and broke Russia’s control over the flow of Central Asian natural gas (Jakobson and Knox 2010). Moreover, Chinese state-owned oil companies—the China National Petroleum Company (CNPC), China Petroleum & Chemical Corporation (Sinopec), and the China National Offshore Oil Corporation (CNOOC)—reached various agreements to purchase oil and gas fields in Central Asia. These agreements were among the largest of those that the Central Asian governments concluded regarding oil and gas development, and indicated China’s determination to gain access to energy resources in the region (Swanström 2005). The Chinese government undertook summit diplomacy in order to strengthen linkages with Central Asian states over energy resources. Over half of Chinese president Hu Jintao’s foreign visits between January 2005 and July 2010 were to countries in which at least one of the three Chinese state-owned companies had business operations for the supply, joint exploration, or asset transfer of oil or natural gas. The top political leader’s commitments provided the opportunity for senior corporate managers to interact with political leaders and their foreign policy advisors (Jakobson and Knox 2010).

In addition to summit diplomacy, China used economic instruments in order to secure natural resources in Central Asia. China provided Central Asian states with loans to expand oil and gas businesses and to assist the development of relevant infrastructure. In 2009, for instance, China concluded an agreement to provide a loan of $10 billion for Kazakhstan. While the Chinese Export-Import Bank provided $5 billion to the Development Bank of Kazakhstan, the CNPC offered another $5 billion to KazMunaiGas, a state-owned national oil and gas company, as a partnership to develop oil and gas in Kazakhstan. As shown in this case, loans typically were arranged with large state-owned companies in Central Asia with significant political involvement. Moreover, some of the loans were directed toward securing the purchase of Chinese goods and services. For instance, China granted Kyrgyzstan a loan of $5.7 million and Tajikistan a loan of $5 million to buy Chinese commercial goods (Swanström 2005, 579).

China has a huge capital base and is willing to grant better loan conditions than its Western rivals. This economic power has been used to make China a significant buyer of natural resources from Central Asia, gradually reducing the relative influence of
Russia and other Western states. The economic aid intensified the reliance of weak Central Asian economies on China as the destination of their exports of resources and as the source of supply of capital and consumer goods. China enhanced its security environments by strengthening diplomatic and economic linkages with neighboring states in general, and enhanced energy security by implementing measures to improve the stable supply of natural resources in particular.

Other Asian countries have also adopted similar policies. For instance, the Korean president made formal visits to Mongolia, Uzbekistan, and Kazakhstan in August 2011. The main objective of the visits was to strengthen linkages in the resource and energy fields. In Uzbekistan, for instance, two presidents reached an agreement to promote the development of gas fields and construction of a related plant. The two leaders also pledged to expand the scope of economic cooperation in the field of information technology, health care, medicine, and the fiber industry.

As free trade agreements (FTAs) have emerged as a crucial arrangement to strengthen economic and political linkages between contracting parties, they have become instruments through which states have attempted to secure access to raw materials and energy resources. The use of FTAs to improve resource security was particularly the case for Northeast Asian countries whose governments pursued FTAs with resource-rich partners such as Australia, the Gulf Cooperation Council (GCC), and Canada. South Korea and Japan insert “resource clauses” aimed at securing energy and mineral supply into their FTAs with Asian trade partners such as Indonesia, India, and Brunei (Wilson 2012).

In Asia, resource-poor states such as Japan and South Korea continuously require a stable supply of energy resources and raw materials for industrialization. The newly emerging countries such as China and India have also increased their demands for energy. Energy security has become an increasingly crucial pillar of national security. In particular, steady economic growth has provided the newly emerging countries with more resources to employ economic instruments to gain access to energy and mineral resources. These developments offer the prospect that competition and rivalry for securing energy resources will intensify and economic activities as a tool of statecraft will become more important in Asia.

The second aspect is China’s use of its economic capabilities to attain specific security objectives. This was seen in disputes with Japan over the Senkaku/Diaoyu Islands in the East China Sea. In September 2010, for instance, the Chinese government allegedly used trade policy instruments to exert pressure on Tokyo after the Japanese Coast Guard arrested the crew of a Chinese fishing boat suspected of operating in Japanese territorial waters. The Chinese customs office suspended exports of rare earth elements necessary for the production of many high-technology goods such as hybrid cars, mobile phones, and solar cells as well as for many advanced military technologies and defense applications such as precision-guided bombs and missiles.

The Chinese government maintained that the export restraint measure was adopted in order to protect domestic reserves and to provide better protection to the environment. Moreover, the government denied that it had ceased exports of rare earth
elements to Japan, and that the stoppage stemmed from a spontaneous and simultaneous decision of the licensed exporting companies. However, the Chinese government’s policies toward other trade partners revealed its strategic intent. China also stopped exports of rare earth elements to the European Union. This export restraint superficially aimed to justify the embargo on Japan by showing that virtually all shipments were delayed because of customs authorities’ detailed examination of the products. However, the measure was clearly intended to prevent Japanese companies from bypassing the embargo through purchase from European companies’ stockpiles (Lackner and McEwen-Fial 2011).

The rare earth element case demonstrates how the Chinese government has manipulated economic policy instruments to attain security objectives. China pursued policies that encouraged Japan and other industrial states to rely on it for the supply of strategic resources, which led to their becoming vulnerable to China’s monopolistic power. China proved willing to use asymmetrical trade dependence as a lever to attempt to persuade Japan to change its policy in a maritime security dispute.

China’s trade policy has acted as a catalyst in the formulation of new strategic relations in Asia. The Chinese policy led Japanese policymakers to recognize the risk of dependence for the supply of strategic resources on a trading partner that takes advantage of asymmetrical trade relations to attain foreign policy objectives. Accordingly, Japan began to diversify its sources of rare earth elements, and approached Vietnam and India in an attempt to secure a stable supply. Given that India and Vietnam are two countries that have had security tensions with China, a search for closer links to them could be seen as a purposeful strategy to balance against China (Khoo 2011, 111). In fact, closer economic linkages have been accompanied by reinforced defense cooperation. In October 2011, defense ministers of Japan and Vietnam signed a memorandum on defense cooperation, and agreed to promote high-level exchanges and regular dialogue at the vice-ministerial level. Japan also advanced security cooperation with India, reaching a ministerial agreement in November 2011 to carry out the first bilateral exercise between the Japan Maritime Self-Defense Force and the Indian navy. China’s strategic manipulation of economic linkages to attain security objectives encouraged its neighboring states to pursue strategies that combine economic and security means to balance against it.

Although the Sino-Japanese conflict has attracted most attention, the use of economic instruments to attain political and strategic objectives is seen in other conflicts in Asia. For instance, the supply of water from Malaysia’s Johor state to Singapore has often in the past been a source of diplomatic dispute, and the Malaysian government has tried to change Singapore’s policies by threatening to cut off water or drastically increase its pricing. In another linkage of economic instruments with security objectives, in August 2012 political confrontation between Japan and South Korea over the Dokdo/Takeshima Islands escalated as Korean president Lee Myung-bak made an unprecedented visit to the islands. In response to this visit, the Japanese government announced that it would freeze the planned purchase of Korean government bonds and delayed the extension of a bilateral currency swap agreement with South Korea.
In Asia, unsettled historical disputes including those driven by territorial issues often provoke political confrontation. Such confrontation has encouraged governments to use economic linkages as a tool of influence or pressure to obtain concessions from and change the behavior of the other party in a dispute.

29.4. Conclusion

This chapter has explored the implications of the economic-security nexus in Asian international relations by focusing on two aspects: how heightened economic interdependence influences the possibility of interstate conflict; and how states have wielded economic instruments to attain key political-security objectives. The examination of linkages between economic interdependence and possible interstate conflict in subregions of Asia reveal that enhanced economic interdependence has stimulated the creation of new institutions or the formalization of existing institutions. However, the influence of economic interdependence on alleviating political-security tensions and advancing security cooperation remains limited. As for a state’s instrumental use of economic statecraft, states in Asia have taken advantage of economic instruments such as trade, foreign aid, and commercial agreements for attaining their political-security goals. Lingering historical distrust and growing concern about energy security intensified the state’s aspirations to use economic statecraft for strategic purposes.

As this chapter indicates, the development of regional institutions and the effective use of them for creating regional stability are different matters. For the most part, Asian states have not used regional institutions effectively for the purpose of alleviating political and security disputes. The positive effects of economic interdependence that liberals posit have remained weak in Asia, where governments still attach primary importance to the maintenance of national interests and to resolving domestic political challenges. Besides, economic instruments have become critical tools of diplomatic manipulation in Asia. In addition to traditional security disputes over national borders, issues relating to maritime security and to energy security expand the likelihood that states will resort to economic instruments of statecraft to pursue strategic goals. In turn, this leads to the deterioration of mutual trust among government officials.

Asian states are often confronted with common nontraditional security threats such as natural disasters, infectious diseases, and environmental deterioration (see chapter 33). The reduction of these threats would help secure national interests and promote security. Effective responses to transboundary threats require joint initiatives and action by regional states. Perceiving such threats as part of a new comprehensive security agenda would necessitate that the measures to meet security challenges are considered broadly. These would include various economic dimensions that are critical to sustaining economic development, social stability, and the preservation of the environment. The effective use of economic measures in conjunction with other diplomatic
means in pursuit of comprehensive security might help to mitigate political and security tensions.

Notes

1. The ASEAN Economic Community would be a single market and production base with a free flow of goods, services, investment, and skilled labor. Unlike a normal common market, the AEC would have no plan to establish a common tariff rate applied to non-members and would restrict the flow of labor to skilled laborers.

2. While the regulative effects specify standards of proper behavior, the constitutive effects specify what actions will cause relevant others to recognize a particular identity (Katzenstein 1996, 5).

3. The ASEAN leaders declared the creation of the ASEAN Community in the Bali Concord II, agreed at the ninth summit in October 2003. The ASEAN Community comprises three pillars, the ASEAN Economic Community, the ASEAN Security Community—later changed into the ASEAN Political-Security Community—and the ASEAN Socio-Cultural Community. The Bali Concord II was a new ASEAN vision, twenty-seven years after the first Bali Concord signed by the original ASEAN members.

4. Engagements in the BIMSTEC (the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation) or the East Asia Community have become far more policy relevant and meaningful for India (Pattanaik 2006).

5. The Yoshida Doctrine, which was named after Prime Minister Shigeru Yoshida, asserted that Japan should concentrate on economic development while relying on the United States for its security (see also chapters by Solís and by Hughes in this volume).

6. China’s primary energy consumption increased from 1,038 million toe (tonne of oil equivalent) in 2000 to 2,432 million toe in 2010, accounting for 20.3 percent of the world total consumption.

7. The islands have been a source of conflict between Japan and China because both governments claim the sovereign right to the islands and surrounding waters. For details of historical conflicts over the islands, see Koo (2009).

8. Rare earth elements are a group of seventeen chemical elements comprising part of the family of lanthanides on the periodic table, with atomic numbers 57–71. They include neodymium, lanthanum, and cerium. Scandium and yttrium are grouped with the lanthanide family due to their similar properties. For one analysis that shows how complex it is to measure any suspension of these exports see Johnston (2013).

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