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**THESIS**

**TRIGGERS OF CHINESE ECONOMIC COERCION**

by

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**TRIGGERS OF CHINESE ECONOMIC COERCION**

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## **ABSTRACT**

This study considers the triggers that may cause China to use economic coercion in bilateral state disputes. The literature reviewed shows that economic statecraft and coercion is a viable policy tool for shaping an opposing state's behavior and the degree to which a state holds an asymmetrical economic advantage influences its ability to wield this tool. China's rising power has made the study and understanding of the conditions under which China will utilize economic coercion an imperative as more states become vulnerable to it. China has already revealed that it is willing to shape state behavior through economic "carrots" and "sticks." As demonstrated by the case studies explored in this thesis, China uses economic coercion to defend its territorial integrity and sovereignty and its understanding of the status quo. Where it holds an economically asymmetrical advantage, China has targeted specific sectors for coercion as a way to signal resolve. As Chinese economic power continues to rise relative to regional neighbors and the U.S., the feasibility of using economic coercion also increases, making the future employment of economic coercion likely wherever China perceives a threat to its interests that is cannot be solved with its increasing military might.

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## LIST OF ACRONYMS AND ABBREVIATIONS

ASEAN	Association of Southeastern Asian Nations
CCP	Chinese Communist Party
CFM	Chinese Foreign Ministry
CNOOC	China National Offshore Oil Corporation
CTA	Central Tibetan Administration
CPPCC	Chinese People’s Political Consultative Conference
DOC	Declaration on Conduct in the South China Sea
DPJ	Democratic Party of Japan
EEZ	economic exclusion zone
EU	European Union
FDI	foreign direct investment
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
JCG	Japanese Coast Guard
JMSU	Joint Marine Seismic Undertaking
LDP	Liberal Democratic Party
NDPO	National Defense Program Outline
PHP	Philippine peso
PLA	People’s Liberation Army
PRC	People’s Republic of China
REE	rare earth elements
SCS	South China Sea
UN	United Nations
UNCLOS	United Nations Convention on the Law of the Sea
U.S.	United States

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# I. ECONOMIC STATECRAFT AND CHINESE ECONOMIC COERCION

This chapter is intended to introduce the foundations of economic statecraft and coercion, look at the current literature that deals with China's use of it and possible causes. The literature review creates five hypotheses for potential triggers to be explored in the following chapters.

## A. INTRODUCTION

The economic and military rise of the People's Republic of China (PRC) has attracted worldwide attention, prompting conjecture among China-watchers as to how this growing power and influence will change the world. The PRC increasingly attempts to influence the policies of neighboring states through "carrots" and "sticks," economic measures that use rewards and punishments to elicit desired behavior from a target.<sup>1</sup> The two elements of economic statecraft are positive sanctions (carrots), such as most-favored-nation status and foreign direct investment (FDI), and negative sanctions (sticks), for example, trade embargoes and increased import inspections.<sup>2</sup>

In a bilateral relationship, how much influence one party can wield over the other is variable, but clearly the relative economic sizes and level of dependency matter.<sup>3</sup> Negative economic sanctions involve the withholding of gains from a targeted state, commonly through embargoes, tariffs, and boycotts.<sup>4</sup> Those sanctions escalate to coercion when the intention is to dictate the behavior of the state. In Southeast Asia, China offers neighboring states the positive sanction of economic assistance, primarily infrastructure projects and aid. As a negative sanction, China implemented a rare-earth element (REE) export ban following the Sino-Japanese conflict in the Senkaku Islands in 2010, banned the importation of Philippine bananas after an incident at Scarborough

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<sup>1</sup> James Reilly, *China's Economic Statecraft: Turning Wealth into Power* (Sydney: Lowy Institute for International Policy 2013): 30.

<sup>2</sup> David A. Baldwin, *Economic Statecraft* (Princeton, NJ: Princeton University Press, 1985), 41-42.

<sup>3</sup> Reilly, *China's Economic Statecraft*, 2.

<sup>4</sup> Baldwin, *Economic Statecraft*, 35-41.

Shoal in 2012, and cancelled high-level meetings after heads of state met with the Dalai Lama in Europe in 2010.<sup>5</sup> Other examples not covered by this thesis include the imposition of additional inspections on salmon from Norway following the awarding of a Nobel Peace Prize to the Chinese political dissident Lui Xiaobo and the imposition of luxury goods sanctions on North Korea after continued nuclear testing. The Chinese exercise the tactics of economic statecraft for political gain, not in retaliation for economic grievances.

This thesis discusses the use of negative economic sanctions generally and particularly those that are used coercively by China. Prominent international disputes that have featured economic sanctions include the U.S. sanctions against Cuba, beginning in 1960, the United Nations (UN) sanctions against Iraq from 1991–2002, and the current sanctions against North Korea. These actions were meant to signal strong disapproval. Economic coercion, by contrast, goes a step further, influencing policy makers as directly as possible. This is particularly effective in democracies, where leaders are vulnerable to popular pressure and economic fallout may force changes in foreign policy and acquiescence to international demands. With economic coercion used to signal resolve in political disputes, what are the conditions in which China will use economic coercion in conjunction with other methods as a means to shape opposing state behavior?

Researching the conditions that cause one state to employ economic coercion against another has useful implications for U.S. policymakers and business leaders. Accordingly, this chapter thesis presents a rationale for studying economic coercion, the current literature with respect to China's behavior, and hypotheses as to why the PRC chooses to act coercively by examining three case studies of Chinese coercion and their implications. These studies and the application of hypotheses to mini-cases suggest that China is apt to use economic coercion when it perceives threats to its territorial sovereignty, integrity, or the status quo under which international disputes are currently resolved.

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<sup>5</sup> The Japanese name for the islands is Senkaku, in Chinese they are referred to as Diaoyu, for simplicity the name of Senkaku will be used throughout the paper. The international name for the disputed reef in the South China Sea is Scarborough Shoal, the Philippines calls it Panatag Shoal and China calls it Huangyan Island. For simplicity, the reef will be referred to as Scarborough Shoal.

## B. WHY STUDY CHINESE ECONOMIC COERCION?

There are generally two perspectives on the rise of China and its implications internationally. First, experts have long argued that China's increasing integration into the international order and multilateral institutions will constrain its behavior.<sup>6</sup> More recently, experts have observed that the PRC is growing increasingly assertive in the region.<sup>7</sup> China's influence and ability to leverage carrots and sticks increases as its relative economic power increases, creating the conditions necessary for economic coercion. Nevertheless, China has used sticks sparingly and deliberately, in the heat of some disputes but not others. Economic coercion, as just one tool available to policy makers, has been frequently utilized as a means to shape another state's behavior, so the use of it to defend China's territorial interests is not surprising. The precise triggers that determine when China will resort to economic coercion remain unclear. By understanding the conditions under which coercion has been employed in the past, we may better predict those situations in which it is likely to occur again. As China's relative power increases and the state leaves larger footprints on the international stage, understanding the behavior of this economic giant, especially analyzing its intentions and motivations, grows more imperative.

For policy makers outside China, understanding which factors are likely to trigger sanctions, embargoes, and ruinous import inspections can help shape policies and actions. Knowing what is likely to provoke retaliation can help policy makers avoid crossing the line, or at least cross it forewarned. As the gap between the U.S. and Chinese economies narrows, it is more likely that China will use economic coercion to signal opposition to U.S. political decisions. PRC attempts of regional economic coercion while the U.S. is rebalancing to Asia puts the two states at odds, with each attempting to reshape the region

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6 Amitav Acharya, "Will Asia's Past Be Its Future?" *International Security* 28, No. 3 (2003): 150; Kai He, "China's Peaceful Rise and Multilateral Institutions: In Search of a Harmonious World," in *"Harmonious World" and China's New Foreign Policy*, ed. Sujian Guo and Jean-Marc F. Blanchard (Lanham, MD: Lexington Books, 2008), 78.

7 Bonnie S. Glaser, "China's Coercive Economic Diplomacy: A New and Worrying Trend," *Center for Strategic and International Studies*, last modified August 6, 2012. <http://csis.org/publication/china-coercive-economic-diplomacy-new-and-worrying-trend>; Adam Segal, "Chinese Economic Statecraft and the Political Economy of Asian Security," in *China's Rise and the Balance of Influence in Asia*, ed. William W. Keller and Thomas G. Rawski (Pittsburgh: University of Pittsburgh Press, 2007), 146.

in its interest, making Chinese economic coercion of U.S. concern. Cognizance of potential triggers will help policy makers identify those sectors on which coercion is likely to fall and prepare their responses. Like policy makers, business leaders must be able to prepare for punitive actions. In business, the risk of sanctions and other punishments can be particularly severe. Understanding triggers will allow industrial leaders to better mitigate risks and protect the global supply chain, which promotes stability at the national and international levels. To mitigate the risk of being targeted by economic coercion, diversification of raw material suppliers and market locations would alleviate some of the precursors and reduce reliance on one state, not only in the case of China but with any state holding an asymmetrical advantage in a sector.

### **C. HYPOTHESES**

The above literature review provides the foundation upon which the following hypotheses are built. Economic coercion as understood in this thesis is founded in Baldwin and Hirschman's works and is informed by the selected texts on China's core interests, economic assertiveness and nationalism. The research question, which the hypotheses attempt to answer, was developed after consulting the materials in the literature review. The question investigated is under what conditions China feels the need to protect its interests and when it can be expected to employ economic coercion to do so. The answers inevitably suggest what truly matters to China, by delineating those interests over which China is willing to risk its own economic growth, which is a major pillar of the Chinese Communist Party (CCP's) governing legitimacy. Regardless of proclamations by the ministry of foreign affairs as to what is or is not important to China, identifying what has historically triggered economic statecraft and might reasonably be expected to do so again is key. In deciding when to deploy economic coercion, it is doubtless that China juggles many considerations, from the individual preferences of the CCP members to long- and short-term background conditions and the relationships between China and the target country. To offset this complexity, the cases selected in this thesis occurred over the past seven years and involve different adversary states. The literature posits several explanations as to why the PRC may resort to economic statecraft, particularly to the use of "sticks." The five hypotheses are explored as potential

drivers of coercion. Because any decision to exercise economic statecraft is likely to be informed by factors at many levels, including domestic and international concerns, these hypotheses are by no means mutually exclusive. The hypotheses could, rather, interact with each other to increase the likelihood of economic coercion. For example, the rise in nationalism could harden Chinese foreign policy while economic dependency sets the conditions for economic coercion. Likewise a challenge to territorial integrity and sovereignty could also be a challenge to regime legitimacy depending on the context of the dispute.

### **1. H1: Territorial Integrity and Sovereignty**

Economic statecraft is more likely to be used in cases of infringement on territorial integrity, which China identifies as a core interest.<sup>8</sup> The Scarborough Shoal and Senkakus incidents are examples. In both cases, the opposing state was backed by the United States, making military escalation unlikely; the most powerful weapon China could field was therefore economic. Any fear of a proportional response from the target may be lessened, first, by China's position as the second-largest economy in the world, and, second, by the China's usual denial of the use of sanctions in political disputes and inevitable attempt to solve the issue diplomatically.<sup>9</sup>

### **2. H2: The Status Quo**

H2 states that economic statecraft is more likely when China perceives that the status quo, which has contributed to its prosperity, is being challenged by other state actors. China's understanding of the status quo is based on bilateral and multilateral agreements to which it is a signatory and de facto arrangements with neighboring states for the mediation of disputes.<sup>10</sup> Preservation of the status quo, particularly in territorial disputes, for economic progress was heralded by Deng Xiaoping in the 1980s and

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<sup>8</sup> Central People's Government of the People's Republic of China, "China's Peaceful Development," (September 2011), sec. 3, [http://english.gov.cn/official/2011-09/06/content\\_1941354.htm](http://english.gov.cn/official/2011-09/06/content_1941354.htm).

<sup>9</sup> Susan Shirk, *China: Fragile Superpower* (New York: Oxford University Press, 2007), 182; *Xinhua*, "Premier Wen's Speech at Sixth China-EU Business Summit," October 7, 2010, [http://news.xinhuanet.com/english2010/china/2010-10/07/c\\_13545683.htm](http://news.xinhuanet.com/english2010/china/2010-10/07/c_13545683.htm).

<sup>10</sup> Suisheng Zhao, "Foreign Policy Implications of Chinese Nationalism Revisited: The Strident Turn," *Journal of Contemporary China* 22, no. 82 (2013): 551.

continues to guide Chinese foreign policy.<sup>11</sup> Once again the 2010 Senkakus case is a good example. In this arrest of a Chinese fishing boat captain by the Japanese, China perceived a deviation from the present conduct of Sino–Japanese relations and escalated the dispute, possibly causing the subsequent ban on REE exports.

### **3. H3: Regime Legitimacy**

H3 states that any oppositional views that reach the international stage and are taken as being directed at the CCP or the legitimacy of its regime may precipitate economic coercion. Challenges to regime legitimacy are similar to the first hypotheses, but differ in that they do not necessarily involve territory. Regime legitimacy can be challenged economically or politically as well. Foreign recognition of Chinese dissidents is a prominent offense. Regime legitimacy in China has shifted from a historical foundation of elitism and class distinctions to an assertion that the CCP has brought economic progress to the people, creating a stable social and political system.<sup>12</sup> By identifying the party as critical to China’s transformation and defense, the CCP can condemn any threat to Chinese sovereignty and territorial integrity as being a threat to the regime. Defending the party’s core interests is therefore not only an enlightened response to the lingering shadow of the “century of humiliation,” but is fundamental to the CCP’s ability to act as the champion of China. By this characterization, the wielding of economic statecraft is justified as one of many defensive tools in PPC’s arsenal.

### **4. H4: Chinese Nationalism**

H4 hypothesizes rising nationalism may make the use of economic coercion more likely as the CCP experiences internal pressure to respond assertively to international incidents. As the Chinese multiply their use of social media, the regime must be more responsive to popular sentiment, including animus directed at neighboring states.<sup>13</sup> Economic coercion can result from public pressure to punish other states for their

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<sup>11</sup> “Set Aside Dispute and Pursue Joint Development,” Ministry of Foreign Affairs of the People’s Republic of China, accessed August 15, 2014, [http://www.fmprc.gov.cn/mfa\\_eng/ziliao\\_665539/3602\\_665543/3604\\_665547/t18023.shtml](http://www.fmprc.gov.cn/mfa_eng/ziliao_665539/3602_665543/3604_665547/t18023.shtml).

<sup>12</sup> Shirk, *China*, 53–54.

<sup>13</sup> *Ibid.*, 103.

offenses. Chinese nationalists are particularly sensitive to perceived slights from Japan, and a strong response by the PRC is demanded. Example transgressions are a Japanese textbook that glossed over Japanese atrocities in Manchuria, which caused widespread protests and a boycott on Japanese goods, requiring the regime to step in diplomatically—and the 2010 Senkakus dispute.<sup>14</sup> For hypothesis H4 to hold, the identity of the opposing state is important. Incidents involving states that are resented and provoke a strong nationalistic clamor would receive harsher treatment than would states with no history of infringing Chinese interests. China's economic coercion would start out as mild and then increase as public outcry increased, particularly toward states with which the Chinese population is most sensitive. Nationalism would have to drive the policy response of China. In sum, depending on the offending state, nationalism and pressure from the masses would force China's hand to respond more forcefully on the international stage than it might otherwise might done.

## **5. H5: Asymmetric Trade Advantages**

Hypothesis H5 states that to use economic coercion to signal resolve, China must enjoy an asymmetrical economic advantage over the intended target in one or more sectors. Having this advantage, whether overall or in a specific sector, will make economic coercion more likely.<sup>15</sup> In the 2010 embargo of REE to Japan, China held a near monopoly on the raw materials that Japanese industry required. This advantage allowed the PRC to exploit for gain a sector dependency in an unrelated dispute. China's monopoly on REE and the lack of other suppliers made economic coercion more costly for Japan than for China and allowed China to influence Japanese industrialists and possibly create domestic pressure for acceding to Chinese demands vis-à-vis the Senkaku Islands. A lopsided relationship with the target makes economic coercion an easier choice for the PRC and thus more likely to be deployed. While not be a stand-alone trigger for the use of sticks, this asymmetry may encourage targeted sanctions upon certain sectors.

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<sup>14</sup> Michael Yahuda, *Sino-Japanese Relations after the Cold War: Two Tigers Sharing a Mountain* (New York: Routledge, 2014), 45.

<sup>15</sup> Albert Hirschman, *National Power and the Structure of Foreign Trade* (Berkeley: University of California Press, 1980), 30-31.

The three case studies selected assist in the development of the hypotheses by introducing different instances, spanning a five-year period, in which China has been charged with economic coercion. Two of the cases, the Senkaku Islands and Scarborough Shoal case involve disputes over territory while the Dalai Lama case study involves a challenge to regime legitimacy, since the states involved do not dispute the territorial claim China has to Tibet. The Dalai Lama case study is more of a political challenge than a territorial one. All cases include aspects of economic asymmetry, Chinese nationalism, and challenges to the status quo. The wide range of targeted states, from neighboring Japan and the Philippines, to France and Germany help reduce the chance that China only targets one or two states.

#### **D. LITERATURE REVIEW**

China's wielding of economic statecraft has stirred much discussion in recent years. The literature is mostly agrees that China's assertiveness is rising and that the PRC is using both positive and negative aspects of economic statecraft more often, with negative sanctions being the primary focus of discussion. Generally, a perceived need to defend the PRC's core interests is discussed as a potential trigger for sticks, with the CCP's increased responsiveness to popular nationalistic groundswells also key.

##### **1. Economic Statecraft**

The work of David A. Baldwin provides a framework for the concepts explored in this thesis. Baldwin defines economic statecraft as one government's attempt to influence another through the use of market mechanisms and resources.<sup>16</sup> As one aspect of economic statecraft, economic coercion is the attempt to compel another state to conform to actions considered preferable by the initiating state. By contrast, positive economic statecraft may employ incentives such as a favorable trade status, subsidies, or the relaxation of tariffs.<sup>17</sup> Baldwin cites five methods of economic coercion, four of which involve both punishment and reward, whether threatened or actually implemented. The last of these methods is the promulgation of misinformation in an effort to cause a target

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<sup>16</sup> Baldwin, *Economic Statecraft*, 30.

<sup>17</sup> *Ibid.*, 42.

state to miscalculate the costs and benefits of its actions.<sup>18</sup> Constraining the choice of options available to a target through positive or negative manipulation is an important part of coercion.<sup>19</sup> Examples of these types of coercive mechanisms are the use of sanctions and embargoes (negative), or the use of aid and favorable trade policies (positive).<sup>20</sup> By analyzing past instances of economic statecraft, Baldwin makes the case for the exploitation of asymmetrical power as an essential component of economic coercion and asserts that, from the perspective of the stronger state, it is easier to influence a weaker neighboring state. Thus economic statecraft is just one more weapon in state-to-state power plays.<sup>21</sup> Decrying the tendency to generalize about the success of economic statecraft, Baldwin notes that tactics are often subtle and take different paths to signal resolve to the opposing state.<sup>22</sup>

Albert Hirschman also emphasizes the role of asymmetrical trade relations by arguing that states seeking influence over neighboring states can do so through economic statecraft. He points out that trade is a key part of a state's power base, and control over trade can lead to an advantageous balance of power:<sup>23</sup> First, because military might can be compounded by economic means, increasing the threat level perceived by the targeted state, and second, because trade itself may become a source of power over another state, providing options for coercion short of war.<sup>24</sup> In an asymmetrical relationship, the smaller partner depends more heavily on bilateral trade, making disruptions more costly to the state. As a result, the larger partner can afford to compel desired behavior by threat or enforcement of coercive measures.<sup>25</sup> The use of economics as an instrument of national power has been known throughout history as an alternative to military force, and in these situations both size and sector-specific advantages matter.

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18 Baldwin, *Economic Statecraft*, 38.

19 Ibid., 38.

20 Ibid., 41–42.

21 Ibid., 20.

22 Ibid., 370–371.

23 Hirschman, *National Power and the Structure of Foreign Trade*, 13.

24 Ibid., 14–15.

25 Hirschman, *National Power and the Structure of Foreign Trade*, 30–31.

## 2. China's Core Interests

China's core interests boil down to five main points: "state sovereignty, national security, territorial integrity and national unification, China's political system established by the constitution and overall social stability, and the basic safeguards for ensuring economic and social development."<sup>26</sup> Concerning state sovereignty, after the Chinese "century of humiliation," the period of foreign interference from 1839–1949, it is understandable that China would be preoccupied with thwarting further meddling. A constant theme in foreign affairs, the imperative of protecting state sovereignty has been pushed by China in defense of itself and others since the development of the "five principles of peaceful coexistence," five years after the PRC was established. This trend continues with PRC rhetoric about the rise of the modern Chinese state and its ability to ascend peacefully. Second, national security is a concern for any state, and especially for one that has faced off against major world powers within the last century. The third Chinese core interest is territorial integrity and reunification. The latter clearly refers to Taiwan as the main issue, but also applies to the ownership of small islands claimed in defiance of Japan, Vietnam, South Korea, and the Philippines. The PRC asserts that not until Taiwan and the disputed islands are returned will China regain its territorial integrity. Fourth, social stability and the maintenance of CCP power are of utmost concern. China's vaunted rise is the principal pillar of CCP legitimacy, one that could crumble in an economic downturn. In such an event, the responsibility for maintaining social order and regime stability would fall squarely on the regime's shoulders as the defender of China against exploitation from other powers. Social instability would threaten the party enough that it might turn to aggressive behavior domestically and abroad. Finally, the fifth core interest of the Chinese is a stable environment in which to achieve further economic and social progress. China's population has become more affluent, and the PRC is providing better for the citizenry. Cracks in the social order could undermine this progress. The iron thread connecting these interests is a combination of maintaining the status quo internationally and resolving outstanding issues in a manner favorable to China without delegitimizing the party.

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<sup>26</sup> Central People's Government of the People's Republic of China, "China's Peaceful Development."

On the international stage, the PRC is intractable in defense of its core interests—Taiwan is a good example of how Chinese reunification and territorial integrity must not be questioned. Taiwan has been a sticking point between the U.S. and the PRC since the normalizing of relations in 1972. The Taiwan issue also involves the Chinese core interests of social stability and regime furtherance. Were Taiwan to declare independence from the mainland, the PRC would feel immense domestic pressure to react, or be forced from power.<sup>27</sup> The PRC is thus unwilling to consider any outcome other than reunification. China has taken economic and military action to quash pro-independence actors in Taiwan, as in the 1995–1996 Taiwan Straits crisis and the PRC response to the election of Taiwanese president Chen Shui-bian in 2000.<sup>28</sup> China’s insistence on reunification leaves the PRC unwilling to negotiate Taiwan’s future and unwilling to state publicly that reunification will not occur without the use of force.

### **3. Chinese Economic Assertiveness**

The rise of an economically strong China is exacerbating tensions across the region. Bonnie Glaser points to potential flashpoints in the region and provides a thorough historical background of the security challenges China faces.<sup>29</sup> She identifies issues that could encroach on China’s stable relationships with the U.S., Japan, Mongolia, Korea, Taiwan, the Spratly Islands, and India. The push for economic growth is a moderating factor on China’s foreign policy, but in the meantime, China will continue to increase military power and assert its territorial claims.<sup>30</sup> With so many potential areas of conflict in the region, a Chinese military that is still catching up to the West, and an array of world powers with vested interests in Asia, China may increasingly use economic statecraft to avoid military entanglements. Glaser looks at the growing use of sticks and carrots in the PRC and argues that China is shaping Southeast Asian national policies through aid and coercion.<sup>31</sup> A recent example is the Scarborough Shoal affair, in which

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27 Shirk, *China*, 182.

28 *Ibid.*, 188–195.

29 Bonnie S. Glaser, “China’s Security Perceptions,” *Asian Survey* 33, no. 3 (March 1993): 253.

30 *Ibid.*, 270–271.

31 Glaser, “China’s Coercive Economic Diplomacy: A New and Worrying Trend.”

Chinese punitive measures prompted Philippine business leaders urge capitulation, the embargo of REE to Japan in the Senkaku Islands dispute, and China's more stringent inspections of Norwegian salmon after the 2010 Nobel Peace Prize was awarded to political dissident Liu Xiaobo.<sup>32</sup>

James Reilly agrees with Glaser that China is increasingly assertive, but argues that China's economic statecraft is not necessarily punitive in all cases and that China appears to prefer using carrots to persuade neighboring states.<sup>33</sup> In most cases of economic enticement, aid or loans are given to improve the infrastructure of a smaller state. These carrots have been more successful for China than sticks, with the sticks proving mostly ineffective and costly, particularly in maritime disputes.<sup>34</sup> Acknowledging the REE embargo, Scarborough Shoal, and the suspension of an Airbus contract after a meeting between the Dalai Lama and French president Nicolas Sarkozy,<sup>35</sup> Reilly nevertheless asserts that that while a mixture of statecraft tactics will continue, carrots are the first weapon of choice for China and sticks are applied only as needed.

China uses its growing economic strength in ways that have raised suspicions among neighboring states and potential adversaries. Its rise in wealth is funding a military modernization program, and this growing military strength is being used to influence other states.<sup>36</sup> Adam Segal argues that while other states typically avoid conflict to ensure economic stability, China, as the center of the world market, need not subjugate its economy to security concerns: China is in a position to pursue both.<sup>37</sup> By strengthening economic ties with the U.S. and Asia, the PRC is increasing its security through economic interdependence, making it increasingly costly for any state to turn adversarial. This gain in power and influence is making China the largest player in the region—one that other states may wish to confer with before making decisions that could jeopardize

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32 Glaser, "China's Economic Coercive Diplomacy."

33 Reilly, "China's Economic Statecraft," 5.

34 Ibid., 10.

35 Ibid., 5–8.

36 Segal, "Chinese Economic Statecraft and the Political Economy of Asian Security," 146.

37 Ibid., 147.

relations, thus allowing China a voice in their policy making.<sup>38</sup> As the perceived need for China to weigh in with neighboring states becomes normalized, China may not have to continue economic coercion, having the ability to influence neighboring states' decision making processes. This trend is exacerbated by the asymmetry of states that are too small to defend themselves against Chinese hegemony.<sup>39</sup> Robert Ross notes that South Korea and Taiwan are now economically dependent on China, making them vulnerable to coercion, while Japanese and Philippine dependence on China is limited, rendering them less vulnerable.<sup>40</sup> Counter-intuitively, South Korea and Taiwan's dependency may not necessarily make coercive measures more likely. Disputes between China and dependent states may end in threats that never materialize as actions. Extrapolating that logic, economic coercion against states that are not conforming to China's wishes and unlikely to bend to threats might be more likely than military action.

Amitav Acharya argues that China will not revert to being the isolated Middle Kingdom of the past, due to its entanglements in international institutions, economic interdependency with outsiders, and multiple institutional linkages.<sup>41</sup> These factors will help mitigate a potential security dilemma in the region. As of now, there is no Asian bandwagoning with China, and to allow such, the U.S. influence would have to be removed.<sup>42</sup> Extending his argument on the moderating effect of institutions through the internalizing of norms, Acharya claims that as China embeds itself further with international organizations, it will be constrained from acting outside the norms of those institutions—meaning that while China may act aggressively from time to time, these instances will become fewer as China becomes more multilateral.

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38 Segal, "Chinese Economic Statecraft and the Political Economy of Asian Security," 153.

39 Robert S. Ross, "Balance of Power Politics and the Rise of China: Accommodation and Balancing in East Asia," in *China's Rise and the Balance of Influence in Asia*, ed. William W. Keller and Thomas G. Rawski (Pittsburgh: University of Pittsburgh Press, 2007), 122.

40 Ibid., 130–132.

41 Acharya, "Will Asia's Past Be Its Future?" 150.

42 Ibid., 155.

#### 4. The Role of Nationalism

Erica Downs and Phillip Saunders foresee China's negative economic actions as more limited in the future due to nationalism, which is currently checked by the economic aspirations of the regime, diminishing the role public sentiment plays in foreign and economic relations.<sup>43</sup> Concerns about China's aggressiveness are overblown according to these experts, because China is already cooperating within the system.<sup>44</sup> Since their writings in 1998, China has continued to become more involved internationally and, therefore, would have less incentive to respond to domestic nationalism. Michael Yahuda agrees that China is more worried about sustaining economic growth in order to quell domestic problems than about encroaching on neighboring states. Yahuda asserts that China seeks peaceful resolutions to neighborhood conflicts, with better relations and minimized fears,<sup>45</sup> and that the real challenge China faces is not international, but domestic.<sup>46</sup> Relying on economics and nationalist fervor for its legitimacy, the PRC may be hesitant to undermine its standing by instigating conflicts over territory and markets.

Susan Shirk departs from Downs and Saunders, stressing that increases in nationalism and domestic unrest can cause the state to act more assertively in the international system. To maintain global stability, the leaders of the PRC need to check domestic pressures that may push them into taking negative steps toward states like Japan, against whose perceived slights the public is highly reactive.<sup>47</sup> Extending this argument, China might not have used economic statecraft against Japan in 2010 if the people had not protested and forced the CCP's hand.

Peter Gries touches on China's diplomatic relationship with Japan and how, due to the Internet, the expression of popular political opinion is thriving, particularly when it

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43 Erica Strecker Downs and Phillip C. Saunders, "Legitimacy and the Limits of Nationalism," *International Security* 23, no. 2 (Winter 1998–1999): 144.

44 *Ibid.*, 116.

45 Michael Yahuda, *The International Politics of the Asia-Pacific*, 2nd ed. (New York: RoutledgeCurzon, 2004), 283.

46 *Ibid.*, 310.

47 Shirk, *China*, 85.

comes to airing grievances against Japan. Rising nationalism and enmity is causing fervor reminiscent of the Cultural Revolution.<sup>48</sup> While this nationalism feeds the short-term goals of the government, there is a long-term risk that massive unrest could turn against the CCP.<sup>49</sup> Heated nationalism limits China's ability to conduct foreign affairs pragmatically and arouses fear in Japan. Yahuda outlines the relationships in the region, focusing mainly on Sino–Japanese relations, but also touching on Chinese relations with the Association of Southeastern Asian Nations (ASEAN) states. Like Shirk, Yahuda notes that while the Chinese exude self-confidence on the international stage, they are quite vulnerable at home, which affects their foreign policy.<sup>50</sup> Explicitly detailing the Senkaku Island dispute, he also analyzes the Dalai Lama contretemps<sup>51</sup> and argues that the Chinese tend to tie economic relations directly to how harmonious the diplomatic arena is in dyadic relationships, with economic disputes often infringing on diplomacy.<sup>52</sup> Yahuda suggests, meanwhile, that the Senkakus dispute did not have a lasting effect on Sino–Japanese relations.<sup>53</sup> In its relations within ASEAN, China is using multilateral institutions to attach neighboring states to itself economically, ensuring that they cannot challenge its territorial integrity without incurring costs.<sup>54</sup> Despite this, China is overcoming the mistrust that characterizes ASEAN and agreeing to shelve disputes for now.<sup>55</sup>

With domestic challenges being a paramount concern for the CCP, the rise in nationalism could increase popular demand that the regime to respond to public opinion. As responsiveness increases and the public becomes more involved in decisions, the

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48 Peter Gries, “China’s ‘New Thinking’ on Japan,” *The China Quarterly*, no 184 (December 2005): 847.

49 Ibid., 846.

50 Yahuda, *Sino-Japanese Relations after the Cold War*, 39; Shirk, *China*, 10.

51 Yahuda, *Sino-Japanese Relations after the Cold War*, 55.

52 Ibid., 77.

53 Ibid., 78.

54 Ibid., 83.

55 Ibid., 89.

choices available to decision makers becomes narrower, potentially hardening their stance toward opposing states and possibly leading to an increase in economic statecraft.

## **E. ANALYTICAL METHODOLOGY**

This thesis uses comparative case studies to identify potential triggers that drive the use of economic coercion by the Chinese. The hypotheses presented suggest that these triggers may stem from territorial infringement, threats to the status quo and the political regime, nationalism, and economic dependency. This thesis examines three major cases in which China used economic coercion against other countries: the 2010 conflict over the Senkaku Islands with Japan, the 2012 dispute over Scarborough Shoal with the Philippines, and the visits of the Dalai Lama to Germany in 2007 and France in 2008. Three mini-cases that receive more cursory treatment in the final chapter are recent developments in the Senkaku Islands, the Second Thomas Shoal controversy in the Philippines, the positioning of oil rig HD-981 near Vietnam in 2014, and the meetings of the Dalai Lama with Prime Minister David Cameron in 2012 and President Obama in 2014.

To analyze economic coercion in these cases, the first step is to discover common conditions. The case studies are structured so as to look only at China and the target state involved. Because selecting on the dependent variable can introduce issues of narrowed research scope, the cases selected should help discover those conditions that have triggered China's use of coercion. A definitive survey of all instances in which the conditions for economic coercion were present and were or were not utilized is outside the scope of this thesis and is suggested for further study. The selection of cases in which economic coercion is alleged, considered without the analyzing contrasting case studies, may introduce bias that might inflate the results. A longer study might remove much of this bias through a more thorough examination of cases in which China refrained from using economic coercion under similar circumstances. While this approach does not yield definitive numerical data to predict relative likelihood, trends are shown that indicate those conditions in which economic statecraft is more likely to be used.

## **F. THESIS OVERVIEW**

The main problem or question addressed throughout these case studies is whether there is a handful of disputes or policies that China perceives important enough that economic statecraft must be invoked—in other words, issues so vital that the will of China must be enforced and other states must be coerced. The findings of the study suggest that economic coercion is more likely in cases where China perceives that its territorial integrity and sovereignty (H1) and the status quo (H2) are being challenged. H3, regime legitimacy, is only partially supported in the Dalai Lama case, through the assumption that undermining CCP rule in Tibet could challenge the regime. Asymmetric trade dependency appears to be a precursor to the use of economic coercion, and not necessarily a trigger. The use of sector specific sanctions, which were utilized in the Senkaku Islands and Scarborough Shoal disputes, require an asymmetric relationship in favor of China, but the dispute appears to be the trigger, not trade dependency. The rise of nationalism (H4) does play a small role in China's foreign policy, but like H5, the research suggest that it is a secondary condition and does not make economic coercion more likely.

The organization of the remaining thesis is setup to present the case studies, summarize and test the findings, and discuss possible implications. Chapter II contains the first case to be analyzed, the 2010 Senkaku Islands affair and the retaliatory REE clampdown. Chapter III analyzes, the 2012 dispute over Scarborough Shoal and punitive measures against the Philippines. Chapter IV investigates the PRC reaction to meetings between the Dalai Lama and Western leaders in 2007 and 2008. Employing the analysis gleaned from the case studies, this thesis proposes a list of interests that China will defend with economic statecraft. In conclusion, the hypotheses of this research are tested against historical data and applied to recent cases for assessment, implications for the U.S. Department of State and U.S. Navy are analyzed, research findings are summarized, and recommendations are made for further research.

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## II. THE SENKAKUS INCIDENT, 2010

The first case study to be explored, China has been accused of using economic coercion against Japan over a territorial dispute in the Senkaku Islands in 2010. Chapter II explores the origins of the dispute, the incidents that occurred and which hypotheses appear to be supported by this case study.

### A. INTRODUCTION

On September 7, 2010, the Chinese fishing trawler *Minjinyu 5179* collided with two Japanese coast guard (JCG) vessels near the Senkaku Islands (see Figure 1). The vessel and crew were quickly taken into custody by Japanese authorities and the captain was charged under Japanese law, as outlined in Section D of this chapter. For Japan, damage to coast-guard vessels in an area under Japanese administrative control was serious enough to elicit filing of charges. From China's perspective, Japan violated the status-quo procedure of turning over the captain and crew to the Chinese, which has been set by a series of agreements in the preceding 15 years. Both parties have an interest in the economic exploitation of the area, both for its fisheries and energy resources, and a common understanding that escalation in the area could threaten interests on either side. Complicating the diplomacy was the fact that China's ascendant economic power has shifted the balance of power in the region.

In 2010, China surpassed Japan as the world's second largest economy, second only to the U.S.<sup>56</sup> China's advance has had two dramatic impacts on foreign relations within the region. First, China has become a dominant economic player that is able to impose high costs on targeted states by applying coercion in bilateral disputes—and it is becoming more aggressive in doing so.<sup>57</sup> Second, China has invested in a modernized military that is able to back up its use of economic statecraft. In the Senkakus dispute, in which territorial integrity was challenged and China chose not to retaliate militarily or

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<sup>56</sup> Chester Dawson and Jason Dean, "Rising China Bests a Shrinking Japan," *Wall Street Journal*, February 14, 2011, <http://online.wsj.com/news/articles/SB10001424052748704593604576140912411499184>.

<sup>57</sup> Reilly, *China's Economic Statecraft: Turning Wealth into Power*, 2.

diplomatically (due to the U.S. protections), the PRC resorted to economic coercion to force a desired behavior. China exploited Japanese dependencies within a key economic sector by cutting off the supply of rare-earth elements (REE) needed by Japanese industry. China also used law-enforcement vessels to secure its interests in the disputed territory.

In Sino–Japanese relations, the change in relative power has been stark and swift, as seen in those sectors where China holds the lion’s share of a natural resources such as the REEs needed by Japan for higher value-added goods production. China’s control over the REE market climbed from 27 percent of the world’s supply in 1990 to 90 percent in 2008.<sup>58</sup> Diplomatically, Sino–Japanese relations were improving until 2005, when the relationship began to slip due to several incidents, including the 2010 Senkakus dispute. Japan’s perceived affront to China’s territorial integrity resulted in a sector-specific asymmetrical relationship’s being used as a weapon; lacking alternative means of enforcement, China deployed economic coercion.

Examination of the Senkakus case study suggests that the first hypothesis, H1, is supported: China uses economic statecraft when territorial integrity and sovereignty are challenged. The second hypothesis, H2, stating that attempts to change the status quo become triggers, is also supported; however, the third hypothesis, H3, stating that challenges to regime legitimacy are triggers, is not and H4, that nationalist behavior leads to limited diplomacy, is partially supported. Nationalism may have led to the continuation of the ban after the release of the entirety of the fishing boat crew. Finally, H5, that China uses economic coercion where it has an asymmetrical advantage, is supported.

This chapter discusses China and Japan’s claims to the Senkaku Islands, looks at the state of their economic and diplomatic relations before the dispute, lays out key events, and finishes with a discussion of how the incident was viewed by each state and the coercion used by the Chinese to signal resolve in the matter.

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<sup>58</sup> Tse Pui-Kwan, “China’s Rare-earth Industry,” *U.S. Geological Survey Open-File Report 1042* (2011): 2, <http://pubs.usgs.gov/of/2011/1042/of2011-1042.pdf>.



Figure 1. The Senkaku Islands<sup>59</sup>

## B. CLAIMS ON SENKAKU ISLANDS

Both China and Japan claim the Senkaku Islands, and Japan currently administers them. Japan asserts that it found the islands uninhabited in 1885 and incorporated them in 1895.<sup>60</sup> China claims records of the islands from 1403 and having used the islands for coastal defense since 1561.<sup>61</sup>

### 1. Japanese Claims

The dispute over the Senkaku Islands began at the end of World War II, with China insisting that the islands belonged among territories taken after the Sino-Japanese war of 1895 and that they should be returned in accordance with the Cairo and Potsdam

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<sup>59</sup> “Japan Deports Pro-China Activists,” *Al Jazeera*, August 18, 2012, <http://www.aljazeera.com/news/asia/2012/08/2012817154256383622.html>.

<sup>60</sup> “The Basic View on the Sovereignty over the Senkaku Islands,” Ministry of Foreign Affairs of Japan, last modified May 8, 2013, [http://www.mofa.go.jp/region/asia-paci/senkaku/basic\\_view.html](http://www.mofa.go.jp/region/asia-paci/senkaku/basic_view.html).

<sup>61</sup> Information Office of the State Council of the People’s Republic of China, *Diaoyu Dao, An Inherent Territory of China*, (Beijing: Information Office of the State Council, 2012), article 1.

declarations. Japan states simply that no dispute exists—that in 1885, the government conducted a survey of the uninhabited islands and found no trace that they had ever been occupied. Japan claimed the islands through a cabinet decision in 1895, during the Sino-Japanese War, erected markers on them, and occupied them for the next 45 years. The islands were not ceded by China in the Treaty of Shimonoseki, which ended the Sino-Japanese War; the accession was done separately, through the cabinet decision. In addition, Japan points out that the islands were not included in the territories it renounced in the 1951 San Francisco Treaty at the end of World War II.<sup>62</sup> This treaty stated that the Japanese “renounced all right, title, and claim to Formosa and the Pescadores,” and that the United States would act as an administrator to the islands “south of 29° north latitude (including the Ryukyu Islands and Daito Islands).”<sup>63</sup> Japan argues that the islands are not a part of the Formosa–Pescadores island groupings and, as a result, were rightly administered by the U.S. before being turned over to Japanese administration under the Agreement Between Japan and the United States of America Concerning the Ryukyu Islands and the Daito Islands in 1972.<sup>64</sup> Therefore, based on the principle of *terra nullius*, the Japanese claim that a territorial dispute does not exist. The islands were not taken in the Treaty of Shimonoseki, and they have been Japanese since their discovery in 1885 and claim by cabinet decision in 1895.

## 2. Chinese Claims

China’s insistence on its territorial claim over the islands and subsequent use of economic coercion to defend them supports hypothesis H1. China claims that the earliest records of the Senkaku Islands under their current Chinese name, Diaoyu, appeared in 1403, when the king of the Ryukyu Islands started paying tribute to the Ming dynasty and both the Ming and Qing dynasties sent envoys to the Ryukyus, passing by the Senkaku Islands and recording their presence. In 1650, the islands were recorded as Chinese territory in the *Annals of Chong-shan*, which stated that everything east of Chiwei Yu

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<sup>62</sup> “The Basic View on the Sovereignty over the Senkaku Islands.”

<sup>63</sup> *Treaty of Peace with Japan (with Two Declarations)*, San Francisco, September 8, 1951, *United Nations Treaty Series*, No. 1832, 48–50.

<sup>64</sup> “The Basic View on the Sovereignty over the Senkaku Islands.”

belonged to the Ryukyu chain and everything west belonged to China. Administratively, China began jurisdiction of the islands in 1561, under the Ming, by incorporating the Senkakus into the Chinese coastal-defense system. From that point on, until the Japanese claimed it in the Sino-Japanese War, the islands were administered by China.<sup>65</sup> The Treaty of Shimonoseki, which ended the Sino-Japanese War, stated that China surrendered all islands pertaining to the island of Formosa.<sup>66</sup> China considers the Senkaku Islands among those islands that were taken over by Japan under the treaty.<sup>67</sup> Citing the Potsdam Declaration, which reaffirmed the Cairo Declaration, China claims that after World War II, the islands should have once again been administered by China. The Cairo Declaration states, “all the territories Japan has stolen from the Chinese, such as Manchuria, Formosa, and the Pescadores, shall be restored to the Republic of China. Japan will also be expelled from all other territories which she has taken by violence and greed.”<sup>68</sup> The Potsdam Declaration later maintained this view, stating, “The terms of the Cairo Declaration shall be carried out and Japanese sovereignty shall be limited to the islands of Honshu, Hokkaido, Kyushu, Shikoku, and such minor islands as we determine.”<sup>69</sup> The Chinese claim is based on the belief that the islands were seized by Japanese aggressors during the Sino-Japanese War and that the transfer of administration from the U.S. to Japan is invalid, since the islands should have been returned following World War II, consequent to their affiliation with Taiwan.<sup>70</sup>

### **3. The Importance of the Senkaku Islands**

Further complicating the dispute are oil deposits, which were found in the 1960s during a geological survey by the U.N. Economic Commission for Asia and the Far

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<sup>65</sup> Information Office of the State Council of the People’s Republic of China, *Diaoyu Dao*, article 1.

<sup>66</sup> *Treaty of Shimonoseki*, Shimonoseki, April 17, 1895, article 2.

<sup>67</sup> Information Office of the State Council of the People’s Republic of China, *Diaoyu Dao*, article 2.

<sup>68</sup> “Cairo Communiqué,” National Diet Library, December 1, 1943, accessed August 2, 2012, [http://www.ndl.go.jp/constitution/e/shiryo/01/002\\_46/002\\_46tx.html](http://www.ndl.go.jp/constitution/e/shiryo/01/002_46/002_46tx.html).

<sup>69</sup> “Potsdam Declaration,” National Diet Library, July 26, 1945, accessed August 2, 2012, <http://www.ndl.go.jp/constitution/e/etc/c06.html>.

<sup>70</sup> Information Office of the State Council of the People’s Republic of China, *Diaoyu Dao*, article 2-3.

East.<sup>71</sup> Oil reserves in the East China Sea are estimated at 60–100 million barrels, with 1–2 trillion cubic feet of natural-gas deposits, making the area important for the second- and third-largest oil importers, China and Japan, respectively.<sup>72</sup> While not a large find in terms of global production, these oil deposits would bring proven Japanese reserves from 44.1 million (as estimated in 2013) to 104.1 million barrels (adding the low end of the estimate)—more than doubling Japan’s oil in reserve.<sup>73</sup> Likewise, Japanese natural-gas reserves would increase from .738 trillion cubic feet to 1.738 trillion, nearly doubling the reserve.<sup>74</sup> China, by contrast, would not increase its reserves so drastically, as it already has proven oil reserves, to the extent of 23.7 billion barrels, and natural gas reserves of 141.2 trillion cubic feet in 2013.<sup>75</sup> These figures suggest that the oil deposits would make a larger difference to Japan than China, but both states are concerned with the allocation of energy resources in the future. In addition to oil and natural gas, the East China Sea is also home to abundant sea life, making access to its fishing grounds important. Strategically, the East China Sea contains a series of important sea-lanes to China, Korea, and Japan, whose control and protection is vital to surrounding economies. Both states have instructed their populations that they have sovereignty over the islands, complicating the chances of negotiation on either side. Japan writes its unqualified claims into textbooks, and China is looking at revisiting classical texts to prove its case.<sup>76</sup> Clearly, both China and Japan have nationalistic sentiments and economic concerns invested in the islands.

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<sup>71</sup> Tadashi Ikeda, “Getting Senkaku History Right,” *The Diplomat*, November 26, 2013, <http://thediplomat.com/2013/11/getting-senkaku-history-right/?allpages=yes>.

<sup>72</sup> “East China Sea,” U.S. Energy Information Administration, last modified September 25, 2012, 2–3, [http://www.eia.gov/countries/analysisbriefs/east\\_china\\_sea/east\\_china\\_sea.pdf](http://www.eia.gov/countries/analysisbriefs/east_china_sea/east_china_sea.pdf).

<sup>73</sup> “Country Overview/Data: Japan, U.S. Energy Information Administration,” U.S. Energy Information Administration, accessed August 2, 2014, <http://www.eia.gov/countries/country-data.cfm?fips=JA#ng>.

<sup>74</sup> Ibid.

<sup>75</sup> “Country Overview/Data: China, U.S. Energy Information Administration,” U.S. Energy Information Administration, accessed August 2, 2014, <http://www.eia.gov/countries/country-data.cfm?fips=CH#ng>.

<sup>76</sup> Michelle FlorCruz, “Chinese and Japanese Scholars Take Diaoyu/Senkaku Territorial Disputes to Textbooks,” *International Business Times*, April 7, 2014, <http://www.ibtimes.com/chinese-japanese-scholars-take-diaoyu-senkaku-territorial-disputes-textbooks-1568409>.

## C. SINO-JAPANESE DIPLOMATIC AND ECONOMIC RELATIONS

Diplomatic relations between China and Japan improved from 1972 through 2005. In 2005, diplomatic relations took a hit due to several events that increased friction; economically, however, relations have improved steadily, despite the downturn in diplomacy.

### 1. Diplomatic Relations

Following U.S. and PRC rapprochement and the release of the Shanghai Communiqué, Japan recognized the PRC in 1972, one of the first states to do so, despite mostly negative interactions over the previous century. From 1972–2005, relations continued to improve, with both economies growing through most of the period due to many areas of mutual cooperation.<sup>77</sup> However, as China began the second phase of its military modernization program in the 1990s, tensions began to rise. Chinese modernization, aimed at accomplishing the PRC's second core interest of national security, aroused concerns in Tokyo as to motivations.<sup>78</sup> China's growing military might, combined with an economic downturn and stagnation in Japan, began to provoke security concerns in Japan.<sup>79</sup>

While the security situation was causing apprehension, diplomatically, tensions reached fever pitch in 2005, with former prime minister Junichiro Koizumi's visits to the Yasukuni Shrine, which memorializes Japan's military casualties—including some war criminals; the release of a new textbook that glossed over Japanese atrocities in World War II, most outrageously those committed in China; and Japan's attempt to become a permanent member of the U.N. Security Council.<sup>80</sup> These events put domestic pressure on the CCP to retort in a meaningful and unyielding way. With protests and riots ongoing, the two states could no longer cooperate as before, and Japanese aid to China

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<sup>77</sup> Richard C. Bush, *The Perils of Proximity: China-Japan Security Relations* (Washington, DC: Brookings Institute Press, 2010), 12.

<sup>78</sup> *Ibid.*, 17; Central People's Government of the People's Republic of China, "China's Peaceful Development," sec. 3.

<sup>79</sup> Yahuda, *Sino-Japanese Relations after the Cold War*, 39.

<sup>80</sup> *Ibid.*, 45.

was cut off.<sup>81</sup> After the turmoil subsided and Abe Shinzo took over as prime minister in 2006, relations began to recover, partly due to Abe's promises not to visit the Yasukuni Shrine or support Taiwanese independence.<sup>82</sup> Abe's successor, Yasuo Fukuda, continued to mend relations with China, promoting a joint-development agreement for the East China Sea in 2008.<sup>83</sup> Intended to increased cooperation, the agreement was not carried through to completion.

Despite the efforts of Abe and Fukuda, both of whom were Liberal Democratic Party (LDP) members, and attempts to warm relations between the neighboring states, issues remained. In 2007, Abe announced that he intended to create an "arc of freedom" that excluded China and that Beijing interpreted as an insult.<sup>84</sup> Second, Japan and China remained divided over the disputed islands in the East China Sea and could not reach a settlement despite a 2008 joint-development agreement. Third, a shipment of poisoned dumplings from China to Japan in 2008 brought no meaningful apology from China.<sup>85</sup> These ongoing conflicts continued to divide the two governments before the dispute of 2010.

In 2009, the Democratic Party of Japan (DPJ) took over the diet and elected Yukio Hatoyama as prime minister. Hatoyama pushed for closer cooperation between the two states, called for a "sea of fraternity" within Asia, and advocated the installation of a hotline with Chinese premier Wen Jiabao to help with diplomatic issues.<sup>86</sup> The Senkaku Islands incident occurred a few months later, and regrettably the hotline appeared to have little effect in solving the issue diplomatically. Some of the lack of cooperation over the Senkaku Islands has been attributed to the DPJ's ignorance of a "secret deal" with the

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<sup>81</sup> Bush, *The Perils of Proximity*, 21.

<sup>82</sup> *Ibid.*, 21–22.

<sup>83</sup> Yahuda, *Sino-Japanese Relations after the Cold War*, 52; *Xinhua*, "China, Japan Reach Principled Consensus on East China Sea Issue," June 18, 2008, [http://news.xinhuanet.com/english/2008-06/18/content\\_8394206.htm](http://news.xinhuanet.com/english/2008-06/18/content_8394206.htm).

<sup>84</sup> Yahuda, *Sino-Japanese Relations after the Cold War*, 49.

<sup>85</sup> *Ibid.*, 52.

<sup>86</sup> Yukio Hatoyama, "Japan's New Commitment to Asia: Toward the Realization of an East Asian Community" (speech, Singapore, November 15, 2009), [http://japan.kantei.go.jp/hatoyama/statement/200911/15singapore\\_e.html](http://japan.kantei.go.jp/hatoyama/statement/200911/15singapore_e.html); *Xinhua*, "China, Japan Agree to Reestablish Hotline between Premiers," *People's Daily*, May 31, 2010, <http://english.people.com.cn/90001/90776/90883/7005884.html>.

LDP on the handling of Chinese citizens in the vicinity of the islands.<sup>87</sup> The agreement backed up the 1997 China–Japan Fisheries Agreement in which both states agreed to handle vessels according to the rules of the flagged state, and under the deal, Japan allegedly agreed to send Chinese citizens back to China.<sup>88</sup> At the time of the incident, Naoto Kan, a member of the DPJ, had succeeded Hatoyama as prime minister but was apparently unaware of the arrangement. Kan remained in power until a year after the Senkakus events. China’s reaction to the breaking of the deal and the fisheries agreement supports the second hypothesis of this research, H2.

## 2. Economic Relations

Economic interdependence between Japan and China increased as China opened up to the world and began its climb. China’s gross domestic product (GDP) prior to Deng Xiaoping’s economic reforms was growing at 6.0 percent; once the reforms were enacted, the GDP growth shot to an average of 9.6 percent.<sup>89</sup> Regionally, China’s rise translated into increasingly dependency on China for resources and as a market for exported goods, to include the Japanese economy.<sup>90</sup> Japan initially grew in a similar fashion following World War II, becoming the first Asian miracle, but began to stagnate in the 1990s. In 1990, trade between Japan and China was at \$18.2 billion, eventually reaching \$267.0 billion in 2005 (see Table 1)<sup>91</sup>. In addition, Japanese investment in China increased to 20 times its size before 1990, and Japan became the largest importer of Chinese goods.<sup>92</sup>

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<sup>87</sup> Jeff J. Sutherland, “Violation of ‘Secret Deal’ May Be at Root of China-Japan Dispute,” *The Two-Way*, National Public Radio, October 19, 2010, <http://www.npr.org/blogs/thetwo-way/2010/10/19/130668119/violation-of-secret-deal-may-be-at-root-of-china-japan-dispute>.

<sup>88</sup> Zhao, “Foreign Policy Implications of Chinese Nationalism Revisited,” 551.

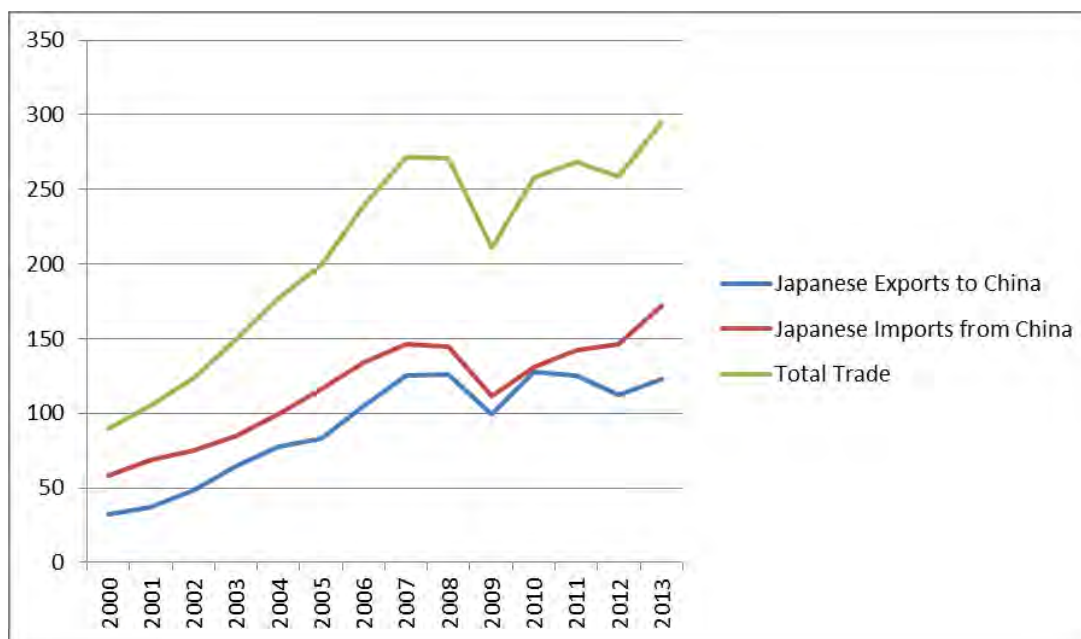
<sup>89</sup> Barry Naughton, *The Chinese Economy: Transitions and Growth* (Cambridge, MA: Massachusetts Institute of Technology, 2007), 140.

<sup>90</sup> Segal, “Chinese Economic Statecraft and the Political Economy of Asian Security,” 146.

<sup>91</sup> “Trade Statistics of Japan,” Ministry of Finance, accessed August 1, 2014, <http://www.customs.go.jp/toukei/srch/indexe.htm>.

<sup>92</sup> Bush, *The Perils of Proximity*, 16.

Table 1. Sino-Japanese trade in billions of USD<sup>93</sup>



The Japanese economy had already moved past the exportation of raw materials to the production of higher value-added goods such as electronics. Crucial to the creation of these goods was steady access to the rare-earth elements used in computers, hybrid-car batteries, and wind turbines.<sup>94</sup> China’s production of REEs increased greatly over the past quarter century: production went from 16,000 metric tons in 1990 to 129,000 metric tons in 2009.<sup>95</sup> What is critical is that world production levels were at 132,000 metric tons in 2009, meaning that outside of China, only 3,000 metric tons of REE were produced.<sup>96</sup> At the time of the 2010 incident, China held 90 percent of the global REE supply<sup>97</sup> and Japan relied on China to provide 80–90 percent of its REEs (see Table 2).<sup>98</sup> Japanese

<sup>93</sup> “Trade Statistics of Japan,” Ministry of Finance.

<sup>94</sup> Lee Levkowitz, “China’s Rare Earths Industry and its Role in the International Market,” *U.S.-China Economic and Security Review Commission Staff Background Paper*, November 3, 2010, <http://www.uscc.gov/Research/china%E2%80%99s-rare-earths-industry-and-its-role-international-market>

<sup>95</sup> Pui-Kwan, “China’s Rare-earth Industry,” 2

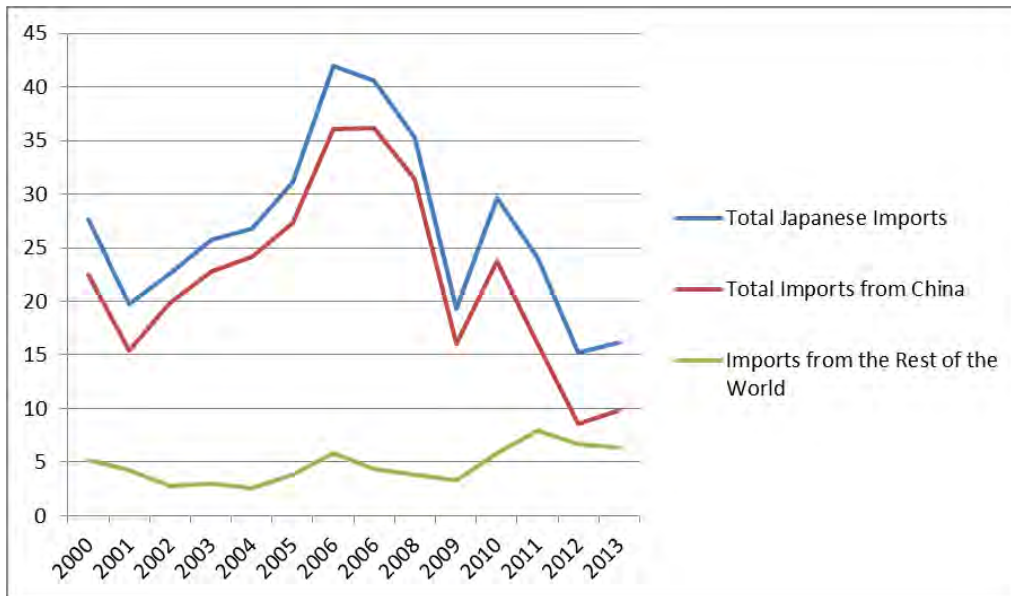
<sup>96</sup> Ibid.

<sup>97</sup> Elliot Brennan, “The Next Oil? Rare Earth Metals,” *The Diplomat*, January 10, 2013, <http://thediplomat.com/2013/01/the-new-prize-china-and-indias-rare-earth-scramble>.

<sup>98</sup> Hiroko Tabuchi, “The Hunt for Rare Earths,” *The New York Times*, November 25, 2010.

reliance on REE imports (commodity codes 2846, 280530, and 360690) from China averaged 86 percent of its total REE imports from 2000–2009.<sup>99</sup> Owing to the embargo, imports dropped slightly in 2010 to 80 percent of all REEs imported.<sup>100</sup> Once Japan began to pursue other resources domestically and abroad, its sector vulnerability decreased, averaging 61 percent of all imports coming from China from 2011–2013.<sup>101</sup> While China was not the only source of REE, it held a virtual monopoly, leaving not only Japan, but advanced industrial nations around the globe reliant on the stability of these imports. The economic relationship and trade between the two countries, which might have stabilized the relationship before to the downturn in foreign relations in 2005, did little to prevent confrontation.

Table 2. Japanese REE Commodity Imports (Commodity Codes 2846, 280530, 360690) in Hundreds of Metric Tons<sup>102</sup>



<sup>99</sup> “Trade Statistics of Japan,” Ministry of Finance.

<sup>100</sup> Ibid.

<sup>101</sup> Ibid.

<sup>102</sup> Ibid.

#### D. THE 2010 SENKAKUS INCIDENT

On September 7, 2010, the Chinese fishing trawler *Minjinyu 5179*, captained by Zhan Qixiong, was operating approximately 7.45 miles off the Senkaku Islands when it was spotted by a JCG vessel.<sup>103</sup> The JCG consists of 120 patrol vessels and is overseen by the Japanese ministry of land, infrastructure, transportation and tourism.<sup>104</sup> Upon the JCG's intercepting the vessel and demanding to board, the *Minjinyu 5179* collided with a JCG Hateruma-class vessel, the *Yonakuni*, and attempted to flee. The *Yonakuni* gave chase, and during the pursuit another JCG patrol vessel, the *Mizuki*, joined; the *Minjinyu 5179* then collided with the *Mizuki*, less than an hour after the first collision. Stopping the trawler at that point, the JCG boarded and arrested Zhan and 14 crewmembers. A few hours later, Zhan was charged with "obstruction of official duties" and "illegal fishing."<sup>105</sup> Upon his release on September 24, 2010, the PRC protested and Japan responded by stating that it was handling a domestic issue according to domestic law.

Chinese foreign-ministry (CMF) spokesperson Jiang Yu was quoted as calling the behavior of Japanese authorities "absurd, illegal, and invalid."<sup>106</sup> Shortly after the arrest of Zhan, Jiang stated that the Chinese government "demand Japanese patrol boats refrain from so-called law-enforcement activities in waters off the Diaoyu islands and actions that would threaten the safety of Chinese fishing boats and their crew."<sup>107</sup> China saw the arrest and charging of Zhan as a violation of the tacit agreement to release and return prisoners and as a defiance of the 1997 fisheries agreement. In China's eyes, a provocation had occurred and Chinese interests had been challenged. According to Lin Xiaoguang, a professor at the CCP Central Committee Party School, "the Japanese side

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<sup>103</sup> *Xinhua*, "Japan Arrests Chinese Captain near Diaoyu Island Despite China's Protest," September 8, 2010, [http://news.xinhuanet.com/english2010/china/2010-09/08/c\\_13484318\\_2.htm](http://news.xinhuanet.com/english2010/china/2010-09/08/c_13484318_2.htm).

<sup>104</sup> "Japan Coast Guard Pamphlet," Japan Coast Guard, March 2014, <http://www.kaiho.mlit.go.jp/e/pamphlet.pdf>.

<sup>105</sup> Linus Hagstom, "'Power Shift' in East Asia? A Critical Reappraisal of Narratives on the Diaoyu/Senkaku Islands Incident in 2010," *The Chinese Journal of International Politics*, vol. 5 (2012), 272.

<sup>106</sup> "China Opposes Japan's Handling of Chinese Fishing Boat," *Global Times*, September 9, 2010, <http://www.globaltimes.cn/content/571755.shtml>.

<sup>107</sup> *Xinhua*, "Japan Arrests Chinese Captain near Diaoyu Island Despite China's Protest."

has ignored the goodwill of the Chinese side and quietly played many little tricks on the Diaoyu [Senkaku] Island issue.”<sup>108</sup> Over the next several days, the PRC summoned the Japanese ambassador, Niwa Uichiro, for discussions on the matter, and on September 12 demanded the release of the crew and boat. Japan responded by refusing to acknowledge the existence of a territorial dispute and confirming that it would continue to administer the islands. Japanese chief-cabinet-secretary Yoshito Sengoku stated two days after the event that “no special diplomatic consideration was given. Procedures were carried out in an orderly manner. The matter was handled according to domestic Japanese law because Japan’s position has always been that no territorial issue exists over the Senkaku Islands.”<sup>109</sup>

Nevertheless, on September 13, the 14 crewmembers and the *Minjinyu 5179* were released. Zhan remained in custody until September 24. The PRC immediately demanded reparations and an apology for the unlawful detention of a Chinese citizen, which was rejected by Tokyo. CMF spokeswoman Jiang Yu stated, “If Japan takes its ties with China seriously, Japan should take practical measures to remove the negative effects of the incident and mend bilateral relations.”<sup>110</sup> In return, Japan wanted China to pay for damages to the JCG vessels.<sup>111</sup>

Immediately following the incident, China suspended all intergovernmental meetings and negotiations, including talks on joint exploration of the Chunxiao gas fields, and reduced Chinese tourism to Japan. Most official and unofficial exchanges between the two states were cancelled.<sup>112</sup> Most notably, from September 23 to November 19 the PRC suspended the shipment of REEs to Japan, drying up the supply of raw materials for Japanese industry,<sup>113</sup> though China denied the suspension. At the 6th China-EU Business

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<sup>108</sup> Lin Xiaoguang, “Bring the Diaoyu Dao Issue into the Orbit of Diplomatic Negotiations,” *Guoji Xianqu Daobao*, September 20, 2010, Open Source Center (CPP20100921671001).

<sup>109</sup> “Fallout Seen in Arrest of Chinese Trawler Captain,” *Asahi Shimbun Online*, September 9, 2010, Open Source Center (JPP2010090969008).

<sup>110</sup> *Xinhua*, “China Demands Japan Act to Repair Ties Following Trawler Row,” September 28, 2010, [http://news.xinhuanet.com/english2010/china/2010-09/28/c\\_13534141.htm](http://news.xinhuanet.com/english2010/china/2010-09/28/c_13534141.htm).

<sup>111</sup> Hagstom, “‘Power Shift’ in East Asia?,” 272.

<sup>112</sup> *Ibid.*, 273; Zhao, “Foreign Policy Implications of Chinese Nationalism Revisited,” 551.

<sup>113</sup> Hagstom, “‘Power Shift’ in East Asia?” 274.

Summit on October, 6, 2010, Wen Jiabao stated, “We haven’t imposed, and will not, impose an embargo on the industry.... China is not using rare earth as a bargaining chip.”<sup>114</sup> However, in the eight months before to the suspension, Chinese exports of REE averaged around 1,780 metric tons per month.<sup>115</sup> In September, the numbers remained high due to the late imposition of the embargo, but in October and November, REE exports to Japan plummeted to 200–300 metric tons a month before spiking again in December.<sup>116</sup>

China’s actions were labeled by Japan and the media as aggressive and nationalistic, feeding a growing apprehension about China’s rise.<sup>117</sup> The Japanese foreign minister, Katsuya Okada, felt that the incident was being characterized in Chinese media as a deliberate provocation by Japan, thus complicating the negotiations. Stating that “such reports are not true and extremely regrettable,” Okada urged China to proceed “calmly and carefully.”<sup>118</sup> In the *Yomiuri Shimbun*, an October 6 article described the Japanese perception of China’s approach: “China’s hard-nosed diplomacy gave the impression to the international community that the country is aggressive.”<sup>119</sup> An editorial in the *Asahi Shimbun* stated, “China is far from a ‘sensible major power’ that respects the rules shared by the international community,” and quoted an unnamed senior official in the Japanese ministry of foreign affairs as stating, “China practiced diplomacy in a rude manner by pushing demands with force.”<sup>120</sup> Japan saw the China’s reaction as an overreaction, since, in its view, Japan was upholding the rightful application of law in the Senkakus.

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<sup>114</sup> *Xinhua*, “Premier Wen’s Speech at Sixth China-EU Business Summit.”

<sup>115</sup> Wayne M. Morrison and Rachel Tang, *China’s Rare Earth Industry and Export Regime: Economic and Trade Implications for the United States*, CRS Report R42510 (Washington, DC: Congressional Research Service, 2012), 32.

<sup>116</sup> Morrison and Tang, *China’s Rare Earth Industry and Export Regime: Economic and Trade Implications for the United States*, 32.

<sup>117</sup> Hagstrom, “‘Power Shift’ in East Asia?” 274; Glaser, “China’s Coercive Economic Diplomacy.”

<sup>118</sup> “Japanese FM Okada Regrets PRC Reports Saying Ship Collision ‘Deliberate,’” *Kyodo World Service*, September 10, 2010, Open Source Center (JPP20100910969110).

<sup>119</sup> “Kan Must Take Firm Line on Chinese Aggression,” *Yomiuri Shimbun*, October 6, 2010, Open Source Center (JPP20101006969120).

<sup>120</sup> Katsuyuki Yakushiji, “Visible High-handed Stance; Diplomacy With China Becoming Difficult,” *Asahi Shimbun*, September 25, 2010, Open Source Center (JPP20100927164007).

While both sides experienced public outcry, protests were far more prevalent in China. In October, in response to a planned Japanese protest outside the Chinese embassy in Tokyo, thousands of Chinese college students marched to show their outrage: *Xinhua* reported 2,000 in Chengdu, 7,000 in Xi'an, and an additional protest in Zhengzhou with an unreported number of students. The protesters shouted slogans such as “defend the Diaoyu Islands,” and “fight Japan,” burned Japanese flags, and vandalized a Japanese shop.<sup>121</sup> These large protests occurred after the assumption of economic sanctions on REE, thus making it likely that a nationalist outcry could have been predicted by the CCP and may have influence the decision making, but not the trigger. Foreign-ministry spokesman Ma Zhaoxu stated it was “understandable that some people expressed their outrage over the Japanese words and deeds, but patriotism should be expressed rationally and in accordance with the law.”<sup>122</sup> Protests occurred throughout China in September and October. As the incident died down, tensions abated, but the conflict had reinforced the growing divide between the two states, and the dispute over the Senkakus was far from over. Another incident occurred in 2012, with the Japanese government attempting to purchase the islands. As Richard Bush pointed out, frequent contact can ameliorate some issues, but as neighboring states with an unfriendly history, Japan and China’s recurring confrontations kept problems stewing.<sup>123</sup> While the Chinese protests would tend to indicate support of hypothesis H4 of this research, the steps that China took, namely economic coercion and increased law-enforcement patrols, were not limited to dealings with Japan, a state that invokes a highly nationalist response—they are the same steps taken in the case with the Philippines, albeit different industries were targeted. Nationalism expressed on social media and editorials may have played a role in China’s response, but with the largest protests occurring in October, after the export ban on REE, they appear not to be the trigger of economic coercion. The October protests may have been a reason that the ban on exports of REE continued until November.

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<sup>121</sup> *Xinhua*, “Chinese Protest against Japan over Diaoyu Islands Issue,” October 16, 2010, [http://news.xinhuanet.com/english2010/china/2010-10/16/c\\_13560499.htm](http://news.xinhuanet.com/english2010/china/2010-10/16/c_13560499.htm).

<sup>122</sup> “Protests over Diaoyu Islands Erupt,” *China Daily*, October, 18, 2010, [http://www.chinadaily.com.cn/china/2010-10/18/content\\_11420663.htm](http://www.chinadaily.com.cn/china/2010-10/18/content_11420663.htm).

<sup>123</sup> Bush, *The Perils of Proximity*, 16.

## E. ANALYSIS OF THE INCIDENT

The outrage exhibited by China and the REE embargo can be looked at from several different levels. First, at the domestic level, the Chinese population is extremely sensitive to perceived slights from Japan.<sup>124</sup> Any incident seen as challenging Chinese interests will likely result in a popular demand for strong official responses, particularly if the incident involves Japan. In the Senkakus clash, this pattern held true. It would not be accurate to say that the PRC was at the mercy of these protests; the government is adept at shutting down or instigating protest when it serves foreign-policy needs. In 2005, protests against the Japanese textbooks were tolerated for three weeks, until the regime determined it was time to end them, which it did effectively.<sup>125</sup> China has been able to exploit nationalism without allowing it to bleed too far into policy.<sup>126</sup> Using nationalism at the bargaining table can be a useful tactic for the PRC if closely monitored by the regime. It appears that as in the 2010 incident, the CCP had control over how far the protests went, and manipulated them to signal disapproval to Japan.

Second, at the international level, maintaining the status quo in territorial disputes is the second-most-important foreign-policy objective of the PRC.<sup>127</sup> For example, China has expressed a desire to shelve its territorial disputes with other Southeast Asian states to enhance stability within the region. When perceived affronts occur, China may respond with economic coercion, as in the Scarborough Shoal incident.<sup>128</sup> However, China does not always respond economically to states that challenge the status quo, as evident in the 2007 clash between China and Vietnam over the Paracel Islands. China's response to Vietnamese challenges was the use of military force to cement its position. Patrolling the area, Chinese naval vessels began detaining Vietnamese trawlers and even shot at one,

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<sup>124</sup> Shirk, *China*, 144.

<sup>125</sup> *Ibid.*, 143.

<sup>126</sup> Segal, "Chinese Economic Statecraft and the Political Economy of Asian Security," 156.

<sup>127</sup> Wu Xinbo and Michael Green, "Regional Security Roles and Challenges," in *Debating China: The U.S.-China Relationship in Ten Conversations*, ed. Nina Hachigian (New York: Oxford University Press, 2014), 200.

<sup>128</sup> Glaser, "China's Coercive Economic Diplomacy."

killing a sailor.<sup>129</sup> China dispatched an unnamed number of ships to the Senkaku Islands in response to the 2010 incident, but those vessels, from the fisheries law-enforcement command, not from the People's Liberation Army Navy (PLAN), have strictly maintained the status quo, not opening fire as against the Vietnamese.<sup>130</sup> Clearly, the PRC does not regard economic coercion as a sole alternative, but will change its response based on the state it is squaring off against. With Vietnam not being democratic, it was not subject to similar domestic pressures that economic coercion can raise.<sup>131</sup> As Hirschman notes, economic statecraft is more likely to be used in cases where the targeting state holds an asymmetrical trade advantage, whether across the economy or sector specific.<sup>132</sup> Baldwin expounds on these ideas by arguing that not only is an asymmetrical relationship important, but economic statecraft is used at the international level to shape actor behaviors.<sup>133</sup> These three conditions make the use of negative economic sanctions more likely when a strong state desires to constrain the behavior of a weaker state. Where these conditions do not exist, the use of other means to influence the target is more likely.

## F. THE USE OF ECONOMIC COERCION

Diplomatic relations in 2010 were not as friendly as they had been, limiting the ability to resolve the Senkakus dispute diplomatically. With little diplomatic bargaining power due to Japan's control of the islands, China took a tough stance, refusing to negotiate on the status of the islands and perceived an alteration of the status quo.

Militarily, China had no ability to challenge Japan over the islands. While small, the Japanese maritime self-defense force is well equipped and capable. Much of its

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<sup>129</sup> Bonnie S. Glaser, "Tensions Flare in the South China Sea," Center for Strategic Studies, 2011, 1-2, <http://csis.org/publication/tensions-flare-south-china-sea>.

<sup>130</sup> *Xinhua*, "China's Patrol Missions near Diaoyu Islands Dispatched According to Its Law and Needs," October 21, 2010, [http://news.xinhuanet/english2010/china/2010-10/21/c\\_13569044.htm](http://news.xinhuanet/english2010/china/2010-10/21/c_13569044.htm)

<sup>131</sup> Madhu Sudan Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes: A Comparative Study of the Philippines and Vietnam," *Journal of Current Southeast Asian Affairs*, no. 3 (2012): 121.

<sup>132</sup> Hirschman, *National Power and the Structure of Foreign Trade*, 13.

<sup>133</sup> Baldwin, *Economic Statecraft*, 38.

technology and equipment was purchased from the U.S. and has been improving since the implementation of the 1996 National Defense Program Outline (NDPO).<sup>134</sup> The 2010 NDPO has increased Japanese military modernization to keep pace with China's modernization program.<sup>135</sup> As Chinese modernization focuses on the PLAN, so too does the 2010 NDPO, increasing the number of destroyers and equipment while reducing the number of ground forces, artillery, and battle tanks. Unlike the Philippines, Japan is in a good position to counter any military action China may undertake in a territorial dispute, even without U.S. support, which, however, was available had the dispute over the Senkaku Islands become militarized. The U.S. has included the islands under the U.S.–Japanese Treaty of Mutual Cooperation and Security since 1960, which enjoins U.S. intervention if Japan is attacked while defending the islands.<sup>136</sup> The U.S. reiterated this stance in 2012 and 2014.<sup>137</sup> The American backing of Japan made the pursuit of military action too costly for China, which was loath to risk war with either party. To protect Chinese fishermen, the fisheries law-enforcement command, which was later merged with other agencies to form the Chinese coast guard under the state oceanic administration, dispatched additional vessels to patrol the area.<sup>138</sup> The combination of law-enforcement vessels to physically secure Chinese interests and economic statecraft to signal resolve proved sufficient to secure the release of Zhan and shore up China's position without military force.

Diplomacy succeeded in getting the crew and trawler released on September 13, 2010, but China had to signal further resolve to release the captain, Zhan Qixiong. Thus,

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<sup>134</sup> Christopher W. Hughes, "China's Military Modernization, U.S. Partners and Allies in Northeast Asia," in *Strategic Asia 2012-13: China's Military Challenge*, ed. Ashley J. Tellis and Travis Tanner (Seattle, WA: National Bureau of Asian Research, 2012), 206-207.

<sup>135</sup> *Ibid.*, 209.

<sup>136</sup> *Dangerous Waters: China Japan Relations on the Rocks* (Brussels: International Crisis Group, 2013), 23, <http://www.crisisgroup.org/en/regions/asia/north-east-asia/china/245-dangerous-waters-china-japan-relations-on-the-rocks.aspx>

<sup>137</sup> Takashi Oshima and Kenji Minemura, "Panetta Tell China the Senkakus under U.S.-Japan Security Treaty," *Asahi Shimbun*, September 21, 2012, <http://ajw.asahi.com/article/asia/china/AJ201209210061>; Justin McCurry and Tania Branigan, "Obama Says U.S. Will Defend Japan in Island Dispute with China," *The Guardian*, April 24, 2014, <http://www.theguardian.com/world/2014/apr/24/obama-in-japan-backs-status-quo-in-island-dispute-with-china>.

<sup>138</sup> *Xinhua*, "China's Patrol Missions near Diaoyu Islands."

China turned to sticks. There are two key aspects in the use of economic coercion by the PRC. First, it must have the ability to do so, either because China is dealing with a weak partner with whom it has strong economic ties or a strong partner with which China has an asymmetrical advantage, as in REE exports,<sup>139</sup> a sector in which China could unilaterally manipulate and disrupt Japanese industry, wielding substantial coercive power. China, as the provider of a required raw material, could have slowed the production of Japanese goods by keeping ships carrying REE from heading to Japanese ports. This in turn, would create great domestic pressure for the Japanese to meet Chinese demands as the vital supply decreased to a drip. China's near monopoly allowed it to target a specific sector, instead of utilizing more general sanctions to signal its displeasure. Second, Japan had few quick options for getting this essential resource. Its overwhelming percentage of the world market allowed China to effectively control the natural resource. The Chinese ban on REE allegedly went into effect on September 23, 2010; Zhan was released the next day, on September 24th.<sup>140</sup> While the ban may have led to the release of Zhan, its continuation through October and November showed that China's ultimate aim was to show adamancy in the protection of its interests, supporting the fifth hypothesis of this research. By using an essential resource as a pawn and exploiting a virtual monopoly, China successfully threatened Japanese industry and, by extension, the Japanese government.

## **G. CONCLUSION**

Although steady economic progress legitimizes the CCP, China is willing to look beyond economic growth when it perceives that territorial integrity and sovereignty are threatened. The Senkakus example is one in which China had an overwhelming advantage in the production of REE and could harm Japanese industry through a ban on exportation. Table 2 shows the amount of REE shipped from China to Japan in the period of concern, with the Chinese market share dropping from a high of 90 percent of total

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<sup>139</sup> Brennan, "The Next Oil? Rare Earth Metals."

<sup>140</sup> Hagstom, "'Power Shift' in East Asia?" 274.

Japanese imports to 61 percent in 2013.<sup>141</sup> At its peak in 2007, China exported 36, 072 metric tons of the selected REEs used.<sup>142</sup> The REE ban led Japan to search for other sources, including domestic, and Chinese exports to Japan dropped to 9, 838 metric tons last year (see Table 2).<sup>143</sup> In other words, Japan was shown its vulnerability and has taken steps to reduce it since 2010. As noted earlier, the Japanese importation of Chinese REE plummeted in October and November of 2010, enough to motivate Japan to search for other sources, which led to an overall decline in the use of Chinese REE. The employment of economic statecraft worked well for China, in that it maintained a desired status quo.

The first and second hypotheses (H1&H2) are supported by this case study—economic statecraft was used when China felt it necessary to signal resolve to prevent challenges to the status quo and territorial integrity. H5 is also supported: China used its asymmetrical advantage in the REE industry to impose costs and signal resolve to Japan. H3 is not supported; Japan did not attempt to challenge the legitimacy of the CCP, and H4 is only partially supported, nationalistic protests did not trigger the economic coercion but may have increased its longevity. Economic statecraft as defined uses positive or negative sanctions to influence the behavior of another actor; China’s deployment in 2010 worked well due to Japanese dependency. China’s behavior followed Baldwin’s three aspects of economic statecraft: it exploited an economic advantage at the international level to shape the behavior of another actor. China had the means and desire to defend its territorial integrity and the status quo through economic coercion.

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<sup>141</sup> “Trade Statistics of Japan,” Ministry of Finance.

<sup>142</sup> Ibid.

<sup>143</sup> Ibid.

### III. SCARBOROUGH SHOAL INCIDENT 2012

The Scarborough Shoal Incident is the second case study to be examined and, like Chapter II, investigates the use of economic coercion in a territorial dispute. The chapter is organized to give background on the dispute, the events that occurred, and the possible triggers of Chinese economic coercion.

#### A. INTRODUCTION

Two years after the 2010 Senkakus dispute, a political row occurred over a disputed set of islands 124 nautical miles off of the coast of the Philippines in the South China Sea (see Figure 2). Like other disputed areas in the South China Sea (SCS), the shoal has different names: the Philippines call it Panatag Shoal or Bajo de Masinloc, and China calls it Huangyan Island. China and the Philippines entered a two-month standoff in April 2012 over an attempted Philippine arrest of Chinese fishermen. Both sides perceived an affront to their territorial sovereignty, the Philippines believing that the fishermen were operating illegally within its exclusive economic zone and China believing that the attempted arrest of its citizens, particularly by a Philippine naval vessel, was a departure from the status quo in a territory that was part of China. The Philippine foreign secretary, Albert del Rosario, stated on April 11, “we have sovereignty and sovereign rights over the Scarborough Shoal and finally I mentioned that if the Philippines is challenged, we are prepared to secure our sovereignty.”<sup>144</sup> As for China, the embassy in Manila released a statement that “urged the Philippine side to stop immediately their illegal activities and leave the area.”<sup>145</sup> As a result, China once again capitalized on its economic dominance over a neighboring state, this time by imposing new import and travel restrictions.<sup>146</sup> The standoff concluded with China’s retaining a presence near Scarborough Shoal to protect its fishing interests, following an initial

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<sup>144</sup> Kim Tan and Anita O. Legaspi, “PHL Says It Will ‘Secure Sovereignty’ if Challenged by China,” *GMA News Online*, April 11, 2012, Open Source Center (FEA20120411027598).

<sup>145</sup> *Xinhua*, “Chinese Embassy Urges Philippines to Stop Illegal Activities in China’s Territory,” April 11, 2012, Open Source Center (CPP20120411968100).

<sup>146</sup> Zhao, “Foreign Policy Implications of Chinese Nationalism Revisited,” 549.

withdrawal of ships for a passing storm and an unchallenged return to control the area with maritime surveillance vessels.

As noted in Chapter II, China may turn to sticks when it lacks military or diplomatic options to settle a dispute, has an asymmetrical economic relationship with the targeted state, or feels its territorial integrity has been challenged. In the case of the Scarborough Shoal, China used economic statecraft as part of a twofold strategy to show force by sending civilian surveillance vessels and by imposing costs on the democratic Philippine government to demonstrate resolve. The Scarborough Shoal case supports two of the hypotheses presented earlier, rejects two others, and supports H5 partially. In this case, economic statecraft was used to counter a perceived affront to the territorial integrity of China. H1 supports coercion to prevent changes to the status quo, particularly in the arrest and seizure of Chinese citizens and their property (H2). The hypotheses not supported are that economic coercion will be used when the CCP feels its legitimacy is challenged (H3) and that nationalism leads to more assertive foreign policy decisions (H4). Partially supported is the use of economic coercion in cases where China holds a bilateral trade advantage (H5). Coercion was used in two sectors in which China did indeed hold a wide margin of advantage, but the Chinese economy as a whole was important to the economic health of the Philippines, and China did not use wider negative sanctions to signal its resolve.

Before discussing the use of economic coercion by the Chinese as directed against two sectors of the Philippine economy, some background on the standoff is presented.



Figure 2. Scarborough Shoal<sup>147</sup>

## B. CLAIMS ON SCARBOROUGH SHOAL

Both the Philippines and China lay claim to the Scarborough Shoal. Philippine claims date to the fifteenth century; the shoal lies 124 miles from the closest recognized Philippine territory.<sup>148</sup> China claims the reef as a traditional fishing ground, illustrated on Chinese maps since the Yuan Dynasty.<sup>149</sup>

### 1. The Philippine Claim

The Philippine claim became active in the 1950s, when it was discovered uninhabited. This claim is supported by two arguments. First, the shoal is within the Philippine economic exclusion zone (EEZ) by 76 miles and is much closer to the

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<sup>147</sup> Marga Ortigas, “Scarborough Shoal Stand-off Sparks Protests,” *Al Jazeera*, May 13, 2012, <http://www.aljazeera.com/indepth/features/2012/05/2012512191343212584.html>

<sup>148</sup> Matikas Santos, “Lacierda: Aquino Won’t Give Up Scarborough Shoal,” *Inquirer Global Nation*, July 23, 2012, <http://globalnation.inquirer.net/45205/lacierda-aquino-wont-give-up-scarborough-shoal>.

<sup>149</sup> Luo Zheng, “Six Irrefutable Evidence: Huangyan Island Belongs to Chins,” *China Military Online – PLA Daily*, May 10, 2012, [http://chn.chinamil.com.cn/wy/2012-05/10/content\\_4857184.htm](http://chn.chinamil.com.cn/wy/2012-05/10/content_4857184.htm).

Philippines than China.<sup>150</sup> Second, the government claims the shoal has been under its control since Philippine independence in 1946 and administers it as a part of the province of Zambales. Under the United Nations Law of the Sea Archipelagic Baselines Law, the Philippines filed to include Scarborough Shoal as its territory in 2009.<sup>151</sup> These angles represent a case for the shoal that is based on legal foundations and simple enough for Filipinos to rally behind.

## 2. The Chinese Claim

China's claims to the shoal go back further in history and center on the historical use of the area. China claims the reef as a traditional fishing ground for the southern provinces and claims that it was first discovered 2,000 years ago, asserting that the island was included on early Chinese maps and China has exercised administrative control since the Yuan dynasty. By contrast, Philippine maps did not include the shoal until recently.<sup>152</sup> In addition to the historical claim, China has also produced a map outlining its claims, which includes the "nine-dash line" used as evidence in nearly every territorial dispute China is involved in. The map has been submitted to the United Nations Commission on the Limits of the Continental Shelf. The nine-dash-line map has been used since the Kuomintang government in 1947 to substantiate claims on all exposed rocks between the line and the mainland. From east of Taiwan, the line extends south to just off the west coast of the Philippines and Malaysia, before turning north toward Vietnam. This large area includes many disputed islands—not only Scarborough Shoal, but the Paracel and Spratly chains as well, to which China claims historical rights.<sup>153</sup> The Chinese claim over the island, combined with the PRC's core interest in territorial integrity, support H1: China uses economic statecraft in the case of territorial infringement, as seen in the review of the shoal incident below. China considers that violations of its territorial

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<sup>150</sup> Santos, "Lacierda: Aquino Won't Give Up Scarborough Shoal."

<sup>151</sup> "PH Sovereignty Based on UNCLOS, Principle of International Law," *Inquirer Global Nation*, April, 20, 2012, <http://globalnation.inquirer.net/34031/ph-sovereignty-based-on-unclos-principles-of-international-law>.

<sup>152</sup> Zheng, "Six Irrefutable Evidence: Huangyan Island Belongs to China."

<sup>153</sup> *Stirring Up the South China Sea (I)* (Brussels: International Crisis Group, 2012), 3, <http://www.crisisgroup.org/en/regions/asia/north-east-asia/china/223-stirring-up-the-south-china-sea-i.aspx>

integrity and sovereignty, such as attempted law enforcement within its territories, must be met with a strong response. In the case of the Scarborough Shoals, economic coercion was part of China's countermove.

### **3. The Economic Impact of the Scarborough Shoal**

At the lowest tide, Scarborough Shoal is five rocks, unable to support human life, protruding from the SCS. The U.N. Convention on the Law of the Sea (UNCLOS) notes that "rocks which cannot sustain human habitation or economic life of their own shall have no EEZ or continental shelf."<sup>154</sup> Therefore, Scarborough Shoal does not qualify as a habitable island, and thus has no EEZ, but it does qualify for 12 nautical miles of territorial waters, according to UNCLOS Article 6.<sup>155</sup> The region is strategically important for its resources and proximity to a major shipping lane. Ten percent of the world's fishing catch comes from the South China Sea, making the shoals economically viable,<sup>156</sup> because sovereignty over the shoal would effect a territorial outcropping in the SCS for either the Philippines or China and potentially strengthen China's claims to other disputed territories, allowing China more territorial waters to control and a larger percentage of the global fisheries catch. But the pockets of territorial waters surrounding the Scarborough Shoal and other SCS territories not only offer a larger share of the fishery, they also open the gateway for unilateral oil exploration of the region. Although exact numbers are not available due to the lack of detailed surveys, it is estimated that the SCS could hold major oil and natural gas reserves possibly equaling 80 percent of the reserves in Saudi Arabia.<sup>157</sup> For both states, but particularly for China, with its rapidly expanding metropolitan population and industry to support, gaining control of the shoal would be extremely valuable.

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<sup>154</sup> UN General Assembly, *Convention on the Law of the Sea*, December 10, 1982, Article 121, [http://www.un.org/depts/los/convention\\_agreements/texts/unclos/part8.htm](http://www.un.org/depts/los/convention_agreements/texts/unclos/part8.htm)

<sup>155</sup> UN General Assembly, *Convention on the Law of the Sea*, Article 121.

<sup>156</sup> Alistair D. B. Cook, "Unpacking the Scarborough Shoal Dispute," *East Asian Policy* 4, no. 46 (2012): 48.

<sup>157</sup> *Ibid.*, 48.

As for shipping, a quarter of the world's shipping traffic goes through the SCS, including 65 percent of vessels supplying China's energy needs.<sup>158</sup> Control of Scarborough Shoal and a 12 nm periphery would subject commercial vessels to the owner of the outcroppings and restrict the navigation of military vessels, particularly those of the U.S. and regional states. As a growing economic power that has been a net importer of oil and natural gas since 1993, China sees that it may be vulnerable to an external state's control over its energy resources. If China were to gain sovereignty over Scarborough Shoal, it would control a pocket of territorial sea inside the Philippine EEZ. Control of even a small part of the SCS would expand a state's ability to extract resources from that portion of the sea and legitimate its claims to other disputed chains. As a matter of routine, both China and the Philippines are quick to respond to any challenges to their sovereignty and will officially denounce statements by the opposing side so as not to imply that their position is weakening.<sup>159</sup>

### **C. SINO-PHILIPPINE DIPLOMATIC AND ECONOMIC RELATIONS**

Diplomatic cooperation between China and the Philippines improved from 1990 until 2009, declining after the passage of Republic Act No. 9522 in the Philippines and the election of a hardline president, Benigno Aquino III, in 2010.<sup>160</sup> Economic relations have continued to improve since 1997, with trade growing at over 140 percent.<sup>161</sup>

#### **1. Diplomatic Relations**

The Philippines and China have steadily increased their diplomatic cooperation since the 1990s. The number of Chinese living in the Philippines, and vice versa, has increased, and bilateral trade has expanded (see Table 3). Under the Gloria Arroyo

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<sup>158</sup> Cook, "Unpacking the Scarborough Shoal Dispute," 48.

<sup>159</sup> M. Taylor Fravel, "China's Strategy in the South China Sea," *Contemporary Southeast Asia* 33, no. 3 (December 2011): 300.

<sup>160</sup> Republic Act No. 9522, March 10, 2009, [http://www.lawphil.net/statutes/repacts/ra2009/ra\\_9522\\_2009.html](http://www.lawphil.net/statutes/repacts/ra2009/ra_9522_2009.html); Zheng Zemin, "An Insight into South China Sea Dispute and Beijing's Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea," *Zhongguo Pinglun*, June 1, 2012, Open Source Center (CPP20120604787013), 2.

<sup>161</sup> "Philippine Participation at the 10<sup>th</sup> China-ASEAN Expo 2013," Center for International Trade Expositions and Missions, accessed July 23, 2014, <http://202.57.32.24/caexpo2013/index.php?page=ph-cn-trade>.

presidency, from 2001 to 2010, cooperation between the governments improved, although it was sometimes attributed to Arroyo's encouraging economic growth by not taking a hard line on the disputed territories in the South China Sea.<sup>162</sup> The Declaration on Conduct in the SCS (DOC) and the attempted development of the SCS through the Joint Marine Seismic Undertaking (JMSU) were put into action during her presidency. The DOC, signed in 2002, attempted to reduce further tensions to protect both states' economic interests in the region, including trade.<sup>163</sup> The JMSU was ventured as a joint natural-resource survey of the region between China, Vietnam, and the Philippines, beginning in 2005. The project ended a few years later due to popular Philippine protests over Arroyo's failure to protect Philippine sovereignty.<sup>164</sup> Nevertheless, Arroyo yielded more cooperation in the SCS than did her predecessors or successor, despite whatever cost to Philippine sovereignty may have been involved. In 2009, relations took a step back as the Philippines passed Republic Act No. 9522, also known as the Philippine Baseline Act, which established a new maritime baseline for the Philippines, to include sovereignty over the Kalayaan group and Scarborough Shoal.<sup>165</sup> Later that year, China submitted its nine-dash line to the UN to reinforce its claims in the region, over Philippine objections.<sup>166</sup>

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<sup>162</sup> *Stirring Up the South China Sea (II)* (Brussels: International Crisis Group, 2012), 6.

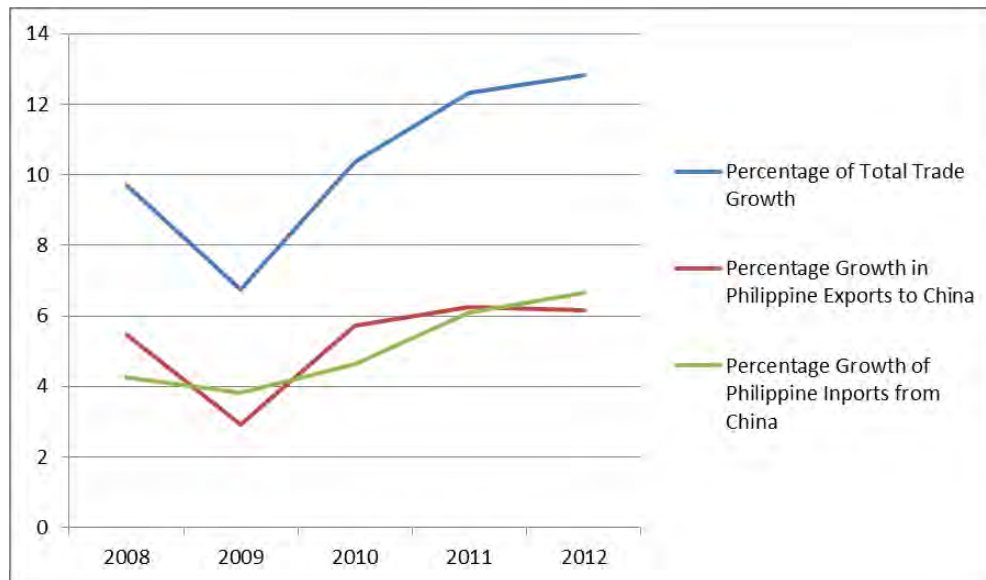
<sup>163</sup> Wu Shicun and Ren Huaifeng, "More Than a Declaration: A commentary on the Background and Significance of the Declaration on the Conduct of the Parties in the South China Sea," *Chinese Journal of International Law* 2, no. 1, (January 2003): 311–317.

<sup>164</sup> Ian Storey, "Conflict in the South China Sea: China's Relations with Vietnam and the Philippines: Part II" *China Brief* 8, no. 9 (April 28, 2008), <http://www.japanfocus.org/-ian-storey/2734>.

<sup>165</sup> Republic Act No. 9522.

<sup>166</sup> *Stirring Up the South China Sea (II)*, 7.

Table 3. Percentage Growth In Sino-Philippine Trade<sup>167</sup>



When President Aquino came to power in 2010, cooperation over the disputed islands continued to disintegrate as the two players engaged in territorial disputes over the South China Sea. China saw Aquino as a hardliner who refused to pursue cooperation, gaining domestic political support by focusing the people on an external threat.<sup>168</sup> The Reed Bank incident, in which a Philippine survey ship was confronted by two Chinese patrol boats, leading to escalating Philippine shows of force via military aircraft and coast-guard escorts, kicked off 2011 as a year of skirmishes. These were partly instigated by the Philippines’ unilateral investigation of the region for natural resources.<sup>169</sup> China viewed this action as setting a precedent for other states with which it had territorial disputes; in essence, relaxing its position in one dispute could make China vulnerable in others.<sup>170</sup> The diplomatic rift was further exacerbated by the Philippine

<sup>167</sup> “Philippine Participation at the 10<sup>th</sup> China-ASEAN Expo 2013,” Center for International Trade Expositions and Missions.

<sup>168</sup> Zemin, “An Insight into South China Sea Dispute and Beijing’s Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea,” 2.

<sup>169</sup> *Stirring Up the South China Sea (II)*, 7; Ian Storey, “China and the Philippines: Implications of the Reed Bank Incident,” *China Brief*, vol. 11, no. 8, Jamestown Foundation (2011), [http://www.jamestown.org/single/?no\\_cache=1&tx\\_ttnews%5Btt\\_news%5D=37902#.U9VzyfldVqU](http://www.jamestown.org/single/?no_cache=1&tx_ttnews%5Btt_news%5D=37902#.U9VzyfldVqU)

<sup>170</sup> Zemin, “An Insight into South China Sea Dispute and Beijing’s Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea,” 5.

government's reference to the South China Sea as the "West Philippine Sea" in October 2011.<sup>171</sup> While economic integration has continued, rows over disputed territories have damaged diplomatic relations.<sup>172</sup> The Scarborough Shoal standoff in 2012 brought tensions to a fever pitch, creating diplomatic rifts that would have to be overcome if the standoff were to end through negotiation.

## 2. Economic Relations

The increasing economic dependence of the Philippines on China set the stage for possible economic coercion by increasing the mutual reliance and vulnerability of both states. Without a high level of trade, negative economic sanctions could not coerce a state to change its behavior, particularly in areas where the trade balance is asymmetric, with one side banking trade surpluses or sector-specific advantages. China and the Philippines have enjoyed the benefits of mutual trade since 1975, with China now the third largest trading partner for the Philippines.<sup>173</sup> In the 15 years before the Scarborough Shoal standoff, bilateral trade grew from \$874 million to \$12.6 billion, a remarkable growth of over 140 percent, and averaged a growth rate of 12.28 percent over the four years preceding the standoff (see Table 3).<sup>174</sup> Chinese investments in the Philippines topped \$251 million in 2011, with the majority going toward the power, mining, and manufacturing sectors.<sup>175</sup> For the Philippines, China is an important market, not only for its fruit industry, but also for electrical products and mined resources.<sup>176</sup> Even with the increase in trade, only 0.89 percent of China's total trade involved the Philippines and 0.75 percent of Chinese imports came from the Philippines in 2011 (see Table 4).<sup>177</sup> FDI

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<sup>171</sup> Jean Magdaraog Cordero, "Manila Formalizes West Philippine Sea Name," *Asia Pacific Defense Forum*, October, 24, 2012, [http://apdforum.com/en\\_GB/article/rmiap/articles/online/features/2012/10/24/philippines-sea-name](http://apdforum.com/en_GB/article/rmiap/articles/online/features/2012/10/24/philippines-sea-name).

<sup>172</sup> *Dangerous Waters: China Japan Relations on the Rocks*, 8.

<sup>173</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 110.

<sup>174</sup> *Ibid.*, "China's Potential for Economic Coercion in the South China Sea Disputes," 110; "Philippine Participation at the 10<sup>th</sup> China-ASEAN Expo 2013," Center for International Trade Expositions and Missions.

<sup>175</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 111.

<sup>176</sup> *Ibid.*, 111.

<sup>177</sup> *Ibid.*, 115.

and import numbers were equally low as a part of China's total FDI and importation. By contrast, China made up over 11 percent of the Philippines total trade in 2011 and sent 12 percent of its exports to China (see Table 5).<sup>178</sup> In addition, 10 percent of Philippine imports came from China, China provided over 18 percent of the total FDI flowing into the Philippines in 2011.<sup>179</sup> As a result, economically speaking, the Philippines were a minor market for China and received a small portion of its investment, while China was a large market for the Philippines, on which over 10 percent of the Philippine GDP depended.<sup>180</sup> In this bilateral relationship, China held the advantage, able to lose the Philippines as a trading partner without much effect on its overall economy—while the loss of China as a major trading partner for the Philippines would threaten 10 percent of its GDP and trade. With China important to the Philippine economy and the Philippines negligible to the Chinese, clearly China could afford coercion.

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<sup>178</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 115.

<sup>179</sup> *Ibid.*, 115.

<sup>180</sup> *Ibid.*, 115.

Table 4. Percentage of Philippine Trade in the Chinese Economy<sup>181</sup>

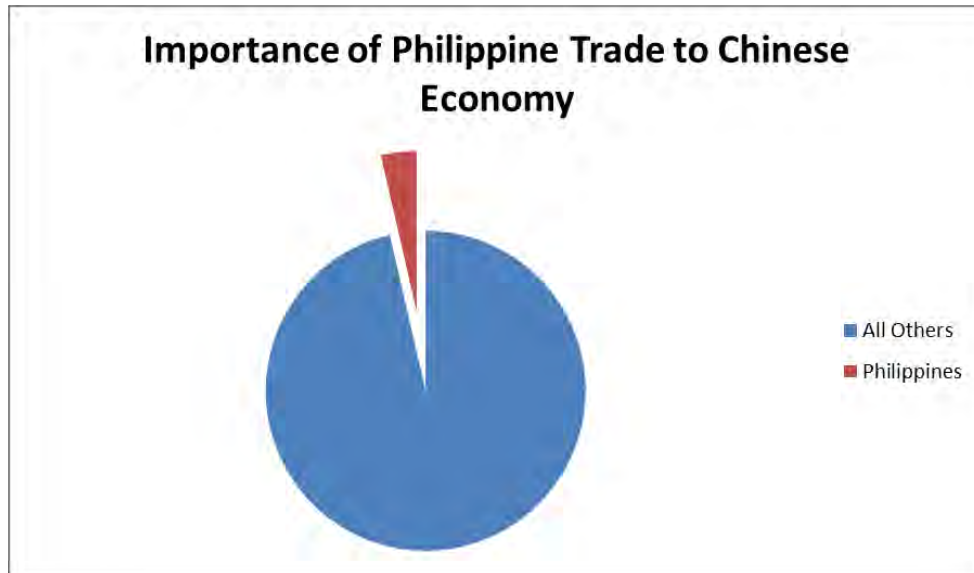
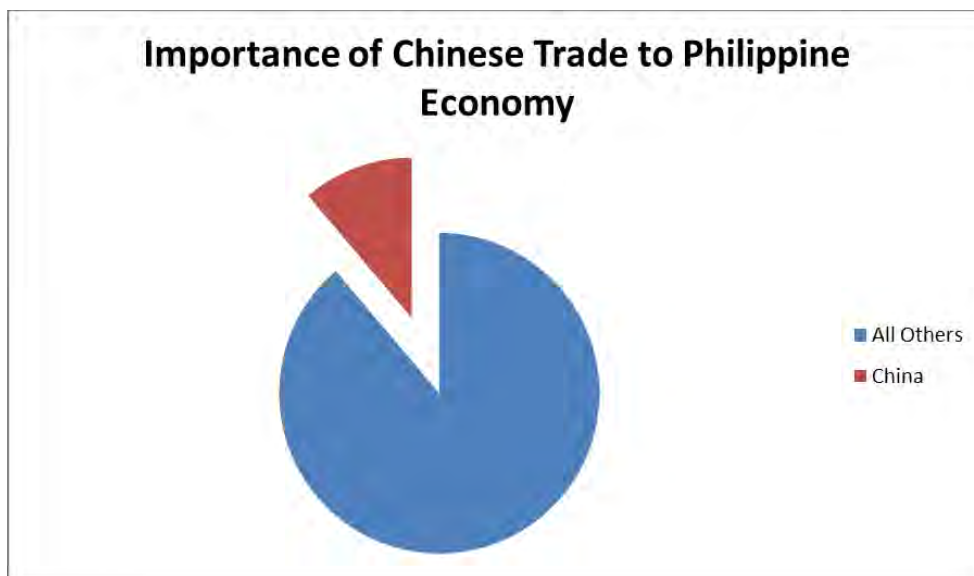


Table 5. Percentage of Chinese Trade in the Philippine Economy<sup>182</sup>



<sup>181</sup> "Top 10 Trading Partners of the Chinese Mainland," *China Daily*, February 20, 2014, <http://english.people.com.cn/business/8541023.html>.

<sup>182</sup> "Foreign Trade," Republic of the Philippines, accessed July 23, 2014, <http://www.census.gov.ph/>.

#### D. THE SCARBOROUGH SHOAL STANDOFF

On the morning of April 8, 2012 a Philippine maritime-patrol aircraft sighted eight Chinese fishing vessels in the vicinity of Scarborough Shoal and reported their position. The standoff began when the *Gregorio Del Pilar*, the Philippine navy's most advanced vessel, formerly a U.S. Coast Guard cutter, moved into the area two days later and searched a vessel, finding live sharks, giant clams, and corals, and moved to arrest the fishermen on charges of poaching. Two Chinese surveillance vessels belonging to the China Marine Surveillance Agency (CMSA) and responsible for law enforcement within Chinese waters, the *Haijian 75* and *Haijian 84*, positioned themselves to prevent the arrest and search of more fishing boats.<sup>183</sup> The CMSA merged with other agencies to produce a unified coast guard under the command of China's state oceanic administration in 2013.<sup>184</sup>

Both parties to the action immediately denounced each other for infringement on territorial waters and illegal actions.<sup>185</sup> Two days later, a third Chinese surveillance vessel arrived and a smaller Philippine coast-guard vessel arrived to relieve the *Gregorio Del Pilar*, which needed refueling and replenishment. The *Gregorio Del Pilar* sailed for port shortly thereafter.<sup>186</sup> On the April 13, China dispatched more marine-surveillance ships from the CMSA and some of the fishing boats were able to head back to China under protection of Chinese ships.<sup>187</sup> By April 15 all fishing boats had departed the area.<sup>188</sup> Early in the standoff, the number of vessels involved dwindled to as low as one per side,

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<sup>183</sup> "Philippines Says Navy Involved in a 'Standoff' with Chinese Ships," *Hong Kong AFP*, April 11, 2012, Open Source Center (SEP20120411055001); "Manila to 'Secure' Sovereignty if 'Challenged' by Beijing in Spratlys Standoff," *Makati City Inquirer*, April 11, 2012, Open Source Center (SEP20120411019003).

<sup>184</sup> Xinhua, "China to Restructure Oceanic Administration, Enhance Maritime Law Enforcement," March, 10, 2013, [http://news.xinhuanet.com/english/china/2013-03/10/c\\_132221768.htm](http://news.xinhuanet.com/english/china/2013-03/10/c_132221768.htm).

<sup>185</sup> Xinhua, "Chinese Embassy Urges Philippines to Stop Illegal Activities in China's Territory;" Tan and Legaspi, "PHL Says It Will 'Secure Sovereignty' if Challenged by China."

<sup>186</sup> "Philippines, China in Fresh Maritime Dispute," *BBC*, April 17, 2012, <http://www.bbc.com/news/world-asia-17741644>; Andreo Calozzo, "Philippine Warship Leaves Scarborough Shoal for 'Operational Reasons,'" *Quezon City GMA News*, April 12, 2012, Open Source Center (FEA20120412027614).

<sup>187</sup> Pia Lee-Brago, "Foreign Affairs Chief: Philippines, China Set Aside Protests to Ease Tensions," *Manila Philstar*, April 14, 2012, Open Source Center (SEP20120414001001).

<sup>188</sup> "Sovereignty or Vassalage?" *Manila Times*, April 15, 2012, Open Source Center (SEP20120415001006).

until China redeployed additional surveillance vessels to the shoal.<sup>189</sup> Throughout April, a series of cyber-attacks were allegedly conducted, targeting university websites on both sides and news and government websites in the Philippines.<sup>190</sup>

The situation escalated in May with China imposing additional inspections and quarantines on fruit imported from the Philippines and issuing a travel warning that resulted in the cancellation of group tours to the Philippines. The inspections and quarantines involved several types of fruit, but were aimed mainly at bananas, a large export crop particularly in the southern province of Mindanao.<sup>191</sup> The quarantine caused an estimated 1 billion PHP (approximately 23 million USD) in losses as fruit rotted on Chinese docks.<sup>192</sup> China stated that the quarantine was imposed due to a discovery of insects and bacteria on shipments of bananas.<sup>193</sup> In *Xinhua*, Aquino was reported as shifting some of the blame to Philippine exporters.<sup>194</sup>

The travel restriction caused the cancellation of 15–20 percent of all airline tickets from mainland China to the Philippines from May to September 2012, a major blow to the tourist industry.<sup>195</sup> China claimed that the travel warning was merely a precaution against the possibility of anti-Chinese demonstrations in the Philippines.<sup>196</sup> Both the

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<sup>189</sup> Andreo C. Calonzo, “DND: China’s Move Not ‘Helpful’ in Solving Panatag Shoal Tiff,” *GMA News*, April 15, 2012, <http://www.gmanetwork.com/news/story/255048/news/nation/dnd-china-s-latest-move-not-helpful-in-solving-panatag-shoal-tiff>; Amita O. Legaspi, “Palace Websites Targeted by Suspected Chinese Hackers,” *GMA News*, April 23, 2012, <http://www.gmanetwork.com/news/story/255935/scitech/technology/palace-websites-targeted-by-suspected-chinese-hackers>.

<sup>190</sup> Fleire Castro, “Pinoy Hackers Strike Back at China Websites, UP Site Restored,” *GMA News*, April 21, 2012, <http://www.gmanetwork.com/news/story/255765/scitech/technology/pinoy-hackers-strike-back-at-china-websites-up-site-restored>.

<sup>191</sup> Zhoa, “Foreign Policy Implications of Chinese Nationalism Revisited,” 549.

<sup>192</sup> Ravindran, “China’s Potential for Economic Coercion in the South China Sea Disputes,” 117.

<sup>193</sup> *Xinhua*, “China Intensifies Quarantine on Philippine Fruit Imports,” May 9, 2012, [http://news.xinhuanet.com/english/china/2012-05/09/c\\_131577736.htm](http://news.xinhuanet.com/english/china/2012-05/09/c_131577736.htm).

<sup>194</sup> *Xinhua*, “Some Exporters to Blame for Rejected Bananas in China: Philippine President,” June, 20, 2012, [http://news.xinhuanet.com/english/world/2012-06/20/c\\_131666237.htm](http://news.xinhuanet.com/english/world/2012-06/20/c_131666237.htm).

<sup>195</sup> “China’s Territorial Disputes with Japan and the Philippines See Traffic Dips,” CAPA Centre for Aviation, September 12, 2012, <http://centreforaviation.com/analysis/chinas-territorial-disputes-with-japan-and-the-philippines-see-traffic-dips-83336>.

<sup>196</sup> *Xinhua*, “China Airline Cuts Flights to Philippines,” May 15, 2012, [http://news.xinhuanet.com/english/china/2012-05/15/c\\_131588999.htm](http://news.xinhuanet.com/english/china/2012-05/15/c_131588999.htm).

banana quarantine and tourism restriction were intended to telegraph resolve concerning Scarborough Shoal.

The standoff broke on June 16 with the Philippines announcing that an agreement had been reached for both sets of ships to withdraw due to weather concerns as the typhoon season began.<sup>197</sup> The Philippine vessels left almost immediately and the Chinese vessels withdrew on June 24. Following the passing of the storm on June 26, some of the Chinese ships returned to the shoal, unchallenged. China continues to assert its sovereignty around the region with impunity, through maritime-surveillance ships that protect Chinese fishermen in the area. The conclusion of the standoff so far is that China has taken de facto control of the shoal.

#### **E. THE USE OF ECONOMIC COERCION**

China as a rising power has time on its side in all territorial disputes, but was forced to take action for two reasons. First, the PRC claimed that Philippine actions within the region were illegal and violated Chinese sovereignty.<sup>198</sup> In the eyes of the Chinese, the Philippines initiated the standoff by its aggressive actions, and China was forced to counter to maintain the status quo ante. The Philippines were in direct violation of the DOC, requiring China to send surveillance vessels.<sup>199</sup> Second, China's need to protect its fishermen and their vessels necessitated a response. Just as they reacted to the Japanese arrest of a fishing crew in 2010, the attempt to search and seize was viewed as a provocation, particularly as it was done by a naval rather than a law-enforcement vessel. The attempted arrest at Scarborough Shoal challenged Chinese interests in the region and disrupted the status quo, supporting hypothesis H2, that the PRC uses economic coercion to defend Chinese citizens, property, and the status quo. This affair was compounded, in the Chinese view, by the declining cooperation between the two governments and

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<sup>197</sup> Wu Dan, "China-ASEAN Relations, May 2012 to August 2012: Chronology of Events," *China: An International Journal* 10, no. 3 (December 2012): 150.

<sup>198</sup> *Xinhua*, "Chinese Embassy Urges Philippines to stop Illegal Activities in China's Territory."

<sup>199</sup> Zemin, "An Insight into South China Sea Dispute and Beijing's Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea," 4.

hardening of Aquino's response.<sup>200</sup> Based on its interpretation of the standoff as a violation of the status quo, the threatened arrest of Chinese citizens, and the use of a Philippine warship for a policing action, China felt compelled to signal resolve and strengthen its claim to the shoal.

As in the Senkakus case, China was faced with three options with which to assert its claim: diplomacy, military might, or economic coercion. Diplomatically, China did attempt to placate the Philippines and ease the standoff by sticking to its position and expressing both its right to the shoal and its wish for a peaceable outcome. Bilateral meetings were held to solve the crisis, but were often suspended or cancelled due to misunderstandings or vexatious moves on both sides, and concluded without resolution.<sup>201</sup> In an apparent response to a statement by Philippine foreign secretary Albert Del Rosario, China continued to urge diplomacy. A spokesman of the CFM, Hong Lei, stated, "the Chinese side demands the Philippine side seriously respect China's territorial sovereignty and stop all moves that will expand and complicate the situation."<sup>202</sup> The dispute has lasted several years, with each side attempting to resolve it through diplomatic channels. The present standoff has not encouraged success in diplomatic negotiations and the Philippines has appealed to the international community for assistance, unsuccessfully calling on ASEAN to side against China, and has investigated its options under UNCLOS.<sup>203</sup>

In the background of the negotiations between China and the Philippines was the presumed Chinese perception of U.S. support for the Philippines, which had two diplomatic effects. First, it weakened the position of China, who faced an adversary with a powerful friend. This unspoken assumption led to America's playing a role in the mediation of the dispute, despite its insistence that the U.S. took no position. The U.S.'s perceived backing raised the bargaining position of the Philippines, making it less weak

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<sup>200</sup> Zemin, "An Insight into South China Sea Dispute and Beijing's Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea," 1.

<sup>201</sup> *Stirring Up the South China Sea (II)*, 8.

<sup>202</sup> *Xinhua*, "Philippines Urged to Stop Inflaming Huangyan Tensions," May 14, 2012, [http://news.xinhuanet.com/english/china/2012-05/14/c\\_131587313.htm](http://news.xinhuanet.com/english/china/2012-05/14/c_131587313.htm).

<sup>203</sup> *Stirring Up the South China Sea (II)*, 9.

and small than it would otherwise have appeared.<sup>204</sup> How far the U.S. was willing to back the Philippines is unknown, making the possibility of its support a factor. While not outwardly stating that it feared the possibility of the U.S. taking the side of the Philippines, repeated statements were made to discourage any state to become involved in what China considered to be a bilateral dispute. A Chinese foreign ministry spokesman, although not explicitly naming the U.S., claimed “The Philippines' attempt to draw any third party for disruption of or intervention into this issue in any form will surely escalate the situation, or even change the nature of this issue.”<sup>205</sup> In the end, the U.S. did not move to protect the Philippines, although China could not assume this at the time.

Second, knowing that it could not compete with China without the backing of the U.S. led the government of the Philippines not only to seek assistance, but to delay the dispute until it officially arrived, in order to strengthen its bargaining position. That support never came. The 1951 U.S.–Philippine mutual-defense treaty was not clarified to state whether it included Scarborough Shoal or the South China Sea, and the standoff was eventually ended by a threatening storm as the two states' ships withdrew. Diplomatically, although it reached out for help from ASEAN and the backing of the U.S., the Philippines did not attempt to delegitimize or undermine CCP rule within China, thus not supporting the third hypothesis of this thesis. In addition, while a few localized protests did occur and the website hacking was no doubt inspired by nationalism, there is little evidence that those actions hardened the foreign policy of China, as predicted in the fourth hypothesis (H4). As shown in the previous chapter, cases in which threats were made to the status quo or territorial integrity elicited similar responses, regardless of the level of nationalist fervor directed toward the target state.

Militarily, despite superior might, China could not directly use the PLAN for two reasons. First, the U.S.–Philippine treaty might have been invoked, bringing China and

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<sup>204</sup> Aileen S. P. Baviera, “Domestic Interests and Foreign Policy in China and the Philippines: Implications for the South China Sea Disputes,” *Philippine Studies: Historical and Ethnographic Viewpoints* 62, no. 1 (March 2014): 134.

<sup>205</sup> *Xinhua*, “FM Press Conference on May 22 (Full Text),” May 29, 2012, [http://news.xinhuanet.com/english/bilingual/2012-05/29/c\\_131618328.htm](http://news.xinhuanet.com/english/bilingual/2012-05/29/c_131618328.htm)

the U.S. into armed conflict. While China's military is superior to its regional neighbors, it is still not ready to compete with the U.S., especially far from shore and close to an American ally from which logistical and air support could be launched. The threat of U.S. intervention was enough of a deterrent that China did not send naval vessels, even though the initiating vessel on the Philippine side was its most modern warship.

Instead, China sent what amounted to coast-guard vessels. While not PLAN ships, they were enough to seize control of the area following the standoff and protect Chinese interests. Sending in the Chinese military would surely have elicited a stronger reaction from the Philippines and increased Philippine domestic insistence that the U.S. live up to its treaty obligations. The U.S. government sent mixed signals as to whether it would include the shoal in the mutual-defense treaty. On one hand, Secretary of State Clinton stated during the standoff that the U.S. would not take a side.<sup>206</sup> By contrast, in a speech during the row, Senator John McCain declared that American support for the treaty was as strong as ever.<sup>207</sup> To exacerbate the situation, the Philippines and the U.S. continued with planned military exercises during the standoff and the Philippines announced it was receiving additional U.S. military aid.<sup>208</sup> It is unclear whether the U.S. would have gotten involved, but the possibility was certainly a looming threat in Chinese military calculations.

Second, China's bargaining power in the Scarborough Shoal and other disputes is not declining relative to the Philippines, thus incentivizing China not to engage militarily until its modernization program is complete. Under this scenario, China's position can only improve with time. In terms of relative power, China is already strong in the region and continues to grow stronger. Its economy is growing, its diplomatic clout is increasing, and its military spends more than any other Asian power as modernization

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<sup>206</sup> Joe Galvez, "Clinton: U.S. Won't Take Sides in Panatag Shoal Dispute," *GMA News*, May 1, 2012, <http://www.gmanetwork.com/news/photo/18911/clinton-us-won-t-take-sides-in-panatag-shoal-dispute>.

<sup>207</sup> "McCain: U.S. Commitment to Mutual Defense Treaty Unshakable," *GMA News*, June 14, 2012, <http://www.gmanetwork.com/news/story/261916/news/nation/mccain-us-commitment-to-mutual-defense-treaty-unshakable>.

<sup>208</sup> Zemin, "An Insight into South China Sea Dispute and Beijing's Bottom Line From the Perspective of PRC-Philippines Standoff over South China Sea," 2.

plans continue to improve its might. As a state's bargaining power increases, so also does its incentive not to engage in disputes that could lead to military conflict.<sup>209</sup> The state has more to gain by biding its time with smaller states and waiting as its relative power increases. Even in facing the U.S., China has incentive to wait. As China's power grows, one of two things will happen: either China will overtake the U.S. as its power increases and American power declines, as some models have predicted, or the relative power gap will decrease, even if the U.S. stays more powerful. China, therefore, had little incentive to engage the Philippines in a military fight that might bring in the U.S.

Unable to solve the standoff diplomatically and with little incentive to escalate militarily, China signaled resolve through a combination of maritime surveillance vessels to secure the area and economic statecraft. Although time is on the side of China due to its increasing power the perceived provocation required a response to ensure that the Philippines did not take de facto control of the shoal. With a large investment in the Philippines already, China had better incentives to use of economic coercion to signal resolve. China was already providing 13 percent of the Philippine's official development assistance and \$251 million in investment in 2011, so it figured that sticks were likely to work better than carrots,<sup>210</sup> and in the event, its fruit and travel sanctions did elicit the desired response of the Philippines's backing away.

The Philippines were susceptible for two reasons. First, as a democracy, the Philippines is vulnerable to pressure from special-interest groups, and unpopular foreign-policy decisions can threaten reelection. The banana quarantine in particular produced strong political pressure on the Aquino government. Because the majority of the crop comes from Mindanao, the fallout unequally burdened one segment of the population and threatened 200,000 jobs.<sup>211</sup> The localization of the impact leveraged the use of the governed against the government, creating pressure from both industrial leaders and local

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<sup>209</sup> M. Taylor Fravel, "Power Shifts and Escalation: Explaining China's Use of Force in Territorial Disputes," *International Security* 32, no. 2 (Winter 2007/08): 46.

<sup>210</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 111.

<sup>211</sup> *Ibid.*, 117.

political elites. Not backing down would have carried a heavy political cost for President Aquino.<sup>212</sup>

Second, Chinese had an asymmetric advantage in the fruit sector to exploit.<sup>213</sup> This trade imbalance put time on China's side with respect to sanctions, and the withdrawal of the Philippine coast-guard vessels due to weather provided an opportunity for China to further its claims by occupying the area. Denying that its imposition of inspections and quarantines was related to the standoff, China simply cited health concerns.<sup>214</sup>

The travel warning, which constituted led to an estimated one million USD in losses for the industry, worked similarly.<sup>215</sup> It also fell on one sector of the economy, the tourist industry, but the effects were not as localized. The tourist industry is mainly centered on Luzon, but other islands were impacted as well. Again, China had an advantage in the relationship by being the fourth-largest source of tourists to the Philippines; a similar warning issued by the Philippines toward China would not have had much impact on the Chinese tourist trade.<sup>216</sup> The use of negative sanctions in only two sectors only partially supports hypothesis H5, that coercion is used when China has a trade advantage over the target. China did exploit an asymmetry, as discussed; but, holding sway over 10 percent of the Philippine GDP, it could have signaled its resolve with much greater strength.

The two negative economic sanctions imposed political costs on a democratic state. The Philippine government was vulnerable to losing power following the dispute, because China enjoyed an advantageous relationship in both industries and could target them without burdening itself. China perceived that its status quo and interests were being challenged, forcing it to assert its claim through economic coercion and occupation,

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<sup>212</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 125.

<sup>213</sup> Zhao, "Foreign Policy Implications of Chinese Nationalism Revisited," 549; Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 117.

<sup>214</sup> *Xinhua*, "China Intensifies Quarantine on Philippine Fruit Imports."

<sup>215</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 118.

<sup>216</sup> *Ibid.*, 118.

thus supporting the second hypothesis (H2). As the Chinese returned to the region following the storm, the political costs associated with the furtherance of negative economic sanctions and more standoffs with Chinese vessels prevented Aquino from countering. China was prepared to carry out the quarantine and ban for quite some time, making the conflict far costlier to the Philippines than to China. Different export restrictions, such as the ones used in the Senkakus dispute a few years earlier, would have caused China to take on more of the cost than the quarantine and travel warning.

## **F. CONCLUSION**

The goal of economic coercion is to maximize the cost of negative economic sanctions for the target while minimizing the cost to the initiating state, and the banana and travel industries provided excellent asymmetrical relationships in which to work. The combination of the democratic nature of the Philippines plus the large advantage that China held in trade allowed it to shape Philippine governmental decisions through economic coercion, targeting vulnerable sectors to produce internal political pressure while minimizing economic impacts to itself. Whether the South China Sea is truly a core interest for the Chinese is a matter of debate. In any case, China's claims remain steadfast, as does its core interest of territorial integrity and sovereignty. Clearly, perceived territorial violations and deviations from the status quo challenged Chinese interests. Since diplomatic meetings had largely failed early on in the crisis and, owing to the U.S.–Philippine treaty, China was not prepared to defend its claim militarily, the only option was to pursue economic coercion to signal resolve and use maritime-surveillance ships to enforce sovereignty. While the typhoon forced the Philippine vessels to withdraw, it was actually political risk that prevented the Philippines from continuing the confrontation as China resumed its maritime patrols and cemented its claim.

In the Scarborough Shoal case, it appears that only H1, territorial integrity and sovereignty, and H2, the status quo, are fully supported. H5, asymmetric trade relationships, is partially supported, but the economic coercion was used as a condition of the first two and not as fully as it might have been. The asymmetric trade relationship operates as an underlying precursor to provide the conditions necessary for economic

coercion. H3, regime legitimacy, is not supported by this case. The dispute over Scarborough Shoal continues, with many of the diplomatic and military qualifiers unchanged, making the use of future economic coercion in the region likely—particularly in defense of China’s territorial integrity.

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## IV. THE DALAI LAMA IN EUROPE

The final full case study to be presented, the Dalai Lama case study is different from the previous two in that it is not a dispute over territory and involves states outside of China's region. China's use of economic coercion is discussed through less overt means of influencing neighboring states.

### A. INTRODUCTION

While famously urging patience in territorial integrity issues, Communist Party Leader Deng Xiaoping is also credited with observing, "no one should expect China to swallow the bitter fruit that hurts its interest."<sup>217</sup> China reiterated this phrase in response to key meetings with the Dalai Lama, particularly the 2010 President Barack Obama–Dalai Lama meeting.<sup>218</sup> If China was willing to speak so menacingly to a state whose economy is greater than its own, less powerful states may well anticipate retaliation for meeting with the Dalai Lama. Tibet continues to be a sensitive subject in Chinese foreign policy, and meetings between heads of state and the Dalai Lama will at best cause the Chinese administration to react with strongly worded statements and at worse with negative economic sanctions. In recent years, several heads of state in Europe have met with the Dalai Lama, causing China to react negatively, cancelling trade summits and high level meetings and suspending trade on certain items. Although similar to the previous case studies, the use of economic coercion in this case is more subtle. The cancellation of meetings can cause missed economic opportunities and the suspension of tourism can affect an important industry, but a specific sector, like REEs, was not targeted. The closest to that level of economic coercion was the suspension of an Airbus contract, which was resumed later. China views any meetings between the Dalai Lama and heads of state as challenges to its sovereignty in Tibet. In protection of that sovereignty and the continuation of Chinese rule, China turns to coercion to extract desired behavior from its European trading partners.

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<sup>217</sup> Zhao, "Foreign Policy Implications of Chinese Nationalism Revisited," 547.

<sup>218</sup> *Ibid.*, 547.

Based on the cases that follow, three hypotheses are supported: the use of economic statecraft in the cases of perceived territorial infringement (H1), usage when there are challenges to the status quo (H2) of Chinese rule, and, thus, regime legitimacy (H3). The last two hypotheses are not supported. Nationalism against the EU did not harden the foreign policy of China, nor did economic asymmetry play a role (H5). While there is much information available on human rights in Tibet and the means of control currently available to the Chinese government, such a discussion is outside of the scope of this research. Rather, China's claims on Tibet are presented, along with counter claims by the exiled government and the current standing of EU–Chinese diplomatic and economic relations. This data provides a background for the two cases presented: the Dalai Lama's meeting with German chancellor Angela Merkel on September 23, 2007, and with French and EU president Nicholas Sarkozy on December 6, 2008. Analysis of China's use of coercion against Germany, France, and the EU is made to evaluate the hypotheses of this research.

## **B. CLAIMS ON TIBET**

China's claims on Tibet are internationally recognized. China claims it began to administer Tibet during the Yuan dynasty in [year].<sup>219</sup> The Central Tibetan Administration claims to embrace the Dalai Lama's wish for a more meaningful autonomy in Tibet, not succession.<sup>220</sup>

### **1. China's Claims**

China's claims to Tibet go back to the Han dynasty (206 BC – 220 AD), when it claims the first bilateral relationship was established. By the Tang dynasty (618 – 907), that relationship was well established and flourishing. It was under the Yuan dynasty that dynastic rule in Tibet was finally cemented, beginning with the Mongol empire's taking control of the region, which eventually was transferred to the Yuan dynasty (1271-1368),

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<sup>219</sup> People's Republic of China, Information Office of the State Council, *Tibet: Its Ownership and Human Rights Situation*, (Beijing: Information Office of the State Council, 1992), article 1

<sup>220</sup> "Middle Way Approach," His Holiness the 14<sup>th</sup> Dalai Lama of Tibet," accessed August 9, 2014, <http://www.dalailama.com/messages/middle-way-approach>.

instituted by Kublai Khan to control all of what was considered China at the time. When the Ming dynasty came to power after the fall of the Yuan, it inherited the right to rule the region and administered Tibet from 1368–1644. Once the Qing dynasty (1644–1911) took over, it continued ruling Tibet, with the power to confirm all Buddhist reincarnations of leaders, including the Dalai Lama. In 1727, the Qing established the first high commissioner to Tibet to administer the Tibetan region, a practice that lasted until its collapse. Once the Republic of China was declared, Sun Yat-sen proclaimed in his inaugural speech that “the unification of lands inhabited by the Han, Manchu, Mongol, Hui and Tibetan people into one country means the unification of the Han, Manchu, Mongol, Hui and Tibetan races.” Tibetans were allowed to participate in statewide elections, giving them full participatory rights in the new government. Once the CCP took over in 1949, they called for the Tibetan local leadership to send representatives to Beijing, but the request was ignored and in 1950, PLA troops invaded Tibet and “liberated” the territory.<sup>221</sup> The PRC has controlled the territory since, but the common program of the Chinese People’s Political Consultative Conference (CPPCC) provided for the regional autonomy of Tibet. The CPPCC established some regional authority, but also outlawed any nationalist agendas intent on “splitting of the unity of the various nationalities.”<sup>222</sup> Regional autonomy was confirmed a few years later in 1951 with the signing of the Agreement of the Central People’s Government and the Local Government of Tibet on Measures for the Peaceful Liberation of Tibet, also referred to as the Seventeen-Point Agreement.<sup>223</sup> From 1951 until the present, the PRC successfully consolidated and retained its rule over Tibet.

## **2. Central Tibetan Administration’s Claims**

The Tibetan government in exile has a different take on Tibet’s relationship with China. Claiming that it has over 2,000 years of written history, the Central Tibetan

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<sup>221</sup> People’s Republic of China, Information Office of the State Council, *Tibet*, article 1.

<sup>222</sup> “The Common Program of the Chinese People’s Political Consultative Conference,” paper presented at the First Plenary Session of the Chinese People’s PCC, Peking, September 29, 1949.

<sup>223</sup> State Council of the People’s Republic of China, *Agreement of the Central People’s Government and the Local Government of Tibet on Measures for the Peaceful Liberation of Tibet*, accessed August 5, 2014, [http://english.gov.cn/official/2011-07/11/content\\_1904075\\_4.htm](http://english.gov.cn/official/2011-07/11/content_1904075_4.htm).

Administration (CTA) maintains that Tibet was a sovereign state before China's invasion.<sup>224</sup> Thus the leadership does not characterize China's entry as liberation. The Dalai Lama, the head of the government until his retirement in 2011, fled Tibet to Dharamsala, India, in 1959 after an alleged failed attempt to capture him.<sup>225</sup> Although no longer leading the government, he remains the spiritual leader for Tibet. The Seventeen-Point Agreement that China flourishes to legitimate its rule was claimed by the Dalai Lama in a statement after his escape to have been signed under duress.<sup>226</sup> The Dalai Lama does currently advocate independence, but only full autonomy, including the establishment of a democratic regional government. In his middle-way approach, the Dalai Lama proposed a new type of autonomy, in which Tibet still belonged to China and would not be independent, but would govern itself.<sup>227</sup> Despite these proclamations, the Dalai Lama is accused of encouraging the Tibetan independence movement. In particular, his trips abroad are seen as a way to gain international support. Europe has been a popular destination; 60 percent of the Dalai Lama's travels from 1991–2008, were to Europe.<sup>228</sup> It is his meetings with heads of state that concern China.

### **3. The Importance of Tibet to China**

After the signing of the Seventeen-Point Agreement, China has seen any meeting with the Dalai Lama or statement on Tibet as a foreign power as interfering with China's internal affairs. China relates issues on Tibet to its core interests of sovereignty and territorial integrity<sup>229</sup> and claims that despite his words to the contrary, the actions of the Dalai Lama show that he is at heart a separatist, working toward an independent state.

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<sup>224</sup> "Issues Facing Tibet Today," Central Tibetan Administration, accessed August 9, 2014, <http://tibet.net/about-tibet/issues-facing-tibet-today/#>.

<sup>225</sup> "Birth to Exile," His Holiness the 14<sup>th</sup> Dalai Lama of Tibet, accessed August 9, 2014, <http://www.dalailama.com/biography/from-birth-to-exile>

<sup>226</sup> "Birth to Exile," His Holiness the 14<sup>th</sup> Dalai Lama of Tibet.

<sup>227</sup> "Middle Way Approach," His Holiness the 14<sup>th</sup> Dalai Lama of Tibet.

<sup>228</sup> Andreas Fuchs and Nils-Hendrik Klann, "Paying a Visit: The Dalai Lama Effect on International Trade," paper presented at the 19th Workshop on Political Economy, Silvaplana, Switzerland, July 2010, 16.

<sup>229</sup> *Xinhua*, "China Hope Germany Honors Its Commitments on Taiwan, Tibet," January 22, 2008, [http://news.xinhuanet.com/english/2008-01/22/content\\_7473523.htm](http://news.xinhuanet.com/english/2008-01/22/content_7473523.htm).

China frequently refers to the exiled government and its supporters as the “Dalai Lama clique,” and claims they have founded a conspiracy for separatism.<sup>230</sup> In 2008, the Chinese foreign minister, Yang Jiechi, stated, “the Dalai Lama issue is not a religious or ethnic issue, but one concerning China’s sovereignty and territorial integrity.”<sup>231</sup> He also confirmed that “the Dalai Lama’s conspiracy to split Tibet from China and his secessionist attempt is doomed to fail.”<sup>232</sup> As a result, any interference in Tibet that could lead to a separate Tibetan state might inspire the separatists in Xinjiang and Inner Mongolia, two of China’s other autonomous regions. The Dalai Lama’s participation in an allied committee with other ethnic minorities in autonomous regions does little to assuage these fears.<sup>233</sup> Time is on the side of China; it controls the territory and all the leverage in the region and continues to increase in strength.<sup>234</sup> Interference from an outside power could change this and, as a result, China repeatedly rejects offers of mediation and third-party intervention in Tibet, including an offer from Norway.<sup>235</sup> Like most states, China is unwilling to reduce its territory based on the nationalist agenda of the population and is willing to secure that territory by force. The CCP would become the party that lost Tibet, and if the dominos fall, Xinjiang and Inner Mongolia, reducing its ability to hold onto power. This reality supports H3; meetings between heads of state and the Dalai Lama challenge the CCP’s rule in Tibet and possibly in the state as a whole.

### C. SINO–EU DIPLOMATIC AND ECONOMIC RELATIONS

Up until 2005, diplomatic relations between the EU and China were improving. In 2005, the relationship became a bit more strained with the continuation of the EU arms

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<sup>230</sup> People’s Republic of China, Information Office of the State Council, *Tibet: Its Ownership and Human Rights Situation*, article 3.

<sup>231</sup> *Xinhua*, “Dalai Lama Issue Not Religious or Ethnic: Chinese FM,” March 12, 2008, Open Source Center (CPP20080312968130).

<sup>232</sup> *Xinhua*, “Dalai Lama Issue Not Religious or Ethnic.”

<sup>233</sup> Barry Sautman, “The Tibet Issue in Post-Summit Sino-American Relations,” *Pacific Affairs* 72, no. 1 (Spring 1999): 12.

<sup>234</sup> *Ibid.*, 14.

<sup>235</sup> *Ibid.*, 18.

embargo against China that was under consideration for reversal.<sup>236</sup> Like the previous case studies, the economic relationship has continued to blossom, with trade in goods up 300 percent since 2003, despite the downturn in diplomatic relations.<sup>237</sup>

## 1. Diplomatic Relations

Diplomatic relations between the EU and China have been improving since their establishment in 1975, under a precursor to the EU known as the European Political Cooperation Agreement.<sup>238</sup> The shadow of the century of humiliation, in which many of the states in the EU carved up parts of China, loomed, but relations improved steadily. At the 2003 EU–China summit, there was some conversation about the development of a “strategic partnership,” and 2004 was a banner year for cooperation.<sup>239</sup> In 2004, there were 206 official visits from EU officials to China. However, in 2005 the relationship began to suffer when negotiations with China over ending the arms embargo failed.<sup>240</sup> The embargo, which was enacted in 1989 as a response to the crackdown on Tiananmen Square protesters, restricted the sale of military weaponry to China. The arms embargo was opposed by Angela Merkel, chancellor of Germany, reportedly because of differences in human rights. This was particularly striking to China, because her predecessor, Gerhard Schröder, supported abolishing the ban.<sup>241</sup> In addition, Chinese goods exports to the EU began to climb, causing concern over the flood of Chinese-made textiles and an increasing trade deficit with China.<sup>242</sup> Mostly, relations began to suffer over concerns about the Chinese human-rights record, the environment, and democratic

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<sup>236</sup> Kerry Brown and Stanley Crossick, “The EU and China Time for a Change?” *Asia Programme Paper* (Chatham House, London: 2003), 3.

<sup>237</sup> Directorate-General for Trade, “European Union, Trade in Goods with China,” European Commission, May 5, 2014, 10, [http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc\\_113366.pdf](http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113366.pdf).

<sup>238</sup> Jing Men, “The EU and China: Mismatched Partners?” *Journal of Contemporary China* 21, no 74 (2012): 325.

<sup>239</sup> Brown and Crossick, “The EU and China Time for a Change?” 4.

<sup>240</sup> *Ibid.*, 3.

<sup>241</sup> “Hu Meets Merkel as Germany Reaffirms EU Arms Ban,” *Deutsche Welle*, November 11, 2005, <http://www.dw.de/hu-meets-merkel-as-germany-reaffirms-eu-arms-ban/a-1773563>.

<sup>242</sup> Men, “The EU and China: Mismatched Partners?” 333.

values that the EU sees as important. The Dalai Lama is popular in Europe precisely because they see him as embodying many of these values.<sup>243</sup>

In addition to the arms-embargo rift, after the Dalai Lama's Merkel meeting but before the Sarkozy meeting, a series of protests in Paris disrupted the April 2008 Olympic-torch relay. The protesters combined a number of issues on which Europe criticizes China, but China considers them to be internal, such as human rights, democracy, Taiwan, and the ethnic minorities in Tibet and Xinjiang.<sup>244</sup> The protests embarrassed China and brought attention on the French popular stance on Tibet. In December of the same year, Sarkozy agreed to meet with the Dalai Lama. From the Chinese perspective, this looked like two attempted interferences with a domestic issue in less than a year, challenging the CCP and straining relationships.

Overall, some of the diplomatic tension that has occurred since 2005 centers on the different interpretations of sovereignty held by the EU and China. Ironically, China holds steadfastly to the original principle of sovereignty that originated out of Europe, as the right to a lack of interference in domestic matters from third parties. Europe's view of sovereignty has shifted. The EU comprises states that have agreed to surrender control over some of their state functions to a larger body.<sup>245</sup> The EU tends to focus not on economic development, as China does, but on the advancement of liberal ideals, mainly human rights. Conversely, China focuses strictly on economic development and the continuity of the Chinese state. These differing views do not provide a foundation from which to expand diplomatic relations. As Zhongpi Pan, a Chinese scholar observed, "for China, the EU is too stubborn to move beyond a human rights perspective when dealing with China: for the EU, China is too stubborn to renew its outdated notion of sovereignty."<sup>246</sup>

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<sup>243</sup> Ibid., 347.

<sup>244</sup> Katrin Bennhold and Elisabeth Rosenthal, "Olympic Torch Goes Out, Briefly, in Paris," *New York Times*, April 8, 2008, [http://www.nytimes.com/2008/04/08/world/europe/08torch.html?pagewanted=all&\\_r=0](http://www.nytimes.com/2008/04/08/world/europe/08torch.html?pagewanted=all&_r=0).

<sup>245</sup> Zhongpi Pan, "Managing the Conceptual Gap on Sovereignty in China-EU Relations," *Asia Europe Journal* 8, no. 2 (2010): 236.

<sup>246</sup> Ibid., 239.

## 2. Economic Relations

Although the EU and China place different premiums on human rights and sovereignty and despite the strained diplomatic relations in 2005, the economic relationships between China and the EU have flourished, from 2003–2013, trade in goods increased nearly 300 percent (see Table 6).<sup>247</sup> In 2003, while good diplomatic relations entered their peak, trade between the two surged \$120 billion.<sup>248</sup> China is the EU's second-largest trading partner, with investments in 24,000 firms in China up to 2006.<sup>249</sup> Also in 2006, 80 percent of the European companies in China reported growth, and the EU provided the fourth most FDI.<sup>250</sup> This trade has been beneficial for China as well, with four of the top 10 trading partners for China in the EU and China holding a large trade surplus. China claims this surplus to be \$70.1 billion, but the EU estimates it closer to \$132.2 billion.<sup>251</sup> In 2006, the EU passed the U.S. as the largest trading partner for China.<sup>252</sup> In trade in goods, trade between China and the EU accounted for around 10 percent of the EU's total trade in 2006.<sup>253</sup> By comparison, the EU held 18 percent of the total trade in goods by China in 2006.<sup>254</sup> Both states are almost equal in mutual important in terms of economic development and trade, with the EU having a slight edge in percentage of total trade. That being the case, China does hold a trade surplus with the EU, one that creates a slight asymmetrical relationship, but the instigation of a trade war would harm China more.

While consistently rising, trade relations did have a few stumbles after the downturn in diplomatic relations in 2005. First, the inflow of textiles from China to

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<sup>247</sup> Directorate-General for Trade, "European Union, Trade in Goods with China," 4.

<sup>248</sup> Men, "The EU and China: Mismatched Partners?" 334.

<sup>249</sup> Ibid., 333; Mingjiang Li, "China-EU Relations: Strategic Partnership at a Crossroads," *China: An International Journal* 7, no. 2 (September 2009): 232.

<sup>250</sup> Li, "China-EU Relations: Strategic Partnership at a Crossroads," 232-233.

<sup>251</sup> Ibid., 242.

<sup>252</sup> "EU Replaces U.S. as Biggest Trading Partner of China," Embassy of the People's Republic of China in the United States of America, last modified September 15, 2006, <http://www.china-embassy.org/eng/xw/t272113.htm>.

<sup>253</sup> Directorate-General for Trade, "European Union, Trade in Goods with China," 10

<sup>254</sup> Ibid., 9.

Europe after the ending of the World Trade Organization (WTO) quotas in 2005 caused some pushback from the EU. The WTO had from 1974–2005 allowed some protection for domestic textile manufacturers, but the end to those restrictions opened up the textile industry to the regular, less protectionist, General Agreement on Tariffs and Trade (GATT) regulations.<sup>255</sup> China responded by flooding the European market with cheaper textiles. The EU countered by imposing quotas on Chinese textiles and once those were reached, held up Chinese goods in the port of debarkation. A deal was eventually reached a few months later, in which the EU would release the products on the condition that half of them counted toward the 2006 quota.<sup>256</sup> The Chinese media applauded the deal as showing that China was willing to make sacrifices in the short run for healthy economic relationships.<sup>257</sup>

The other economic concern of the EU that came to light in 2005 with the increase in trade was the corresponding increase of the trade deficit with China. This was a result of two compounding factors. First, the *renminbi* has depreciated against the euro dollar, making the EU less competitive within Chinese markets, down 10 percent from 2005 to 2007. Second, China simply exports to the EU more than it imports from it (see Table 6), mostly due to the different levels of development of the competing economies. This caused a concern that the market in China was not as open to European trade as it could be.<sup>258</sup> Despite these issues, the amount of total trade, including imports to China from the EU, steadily increased from 2003.

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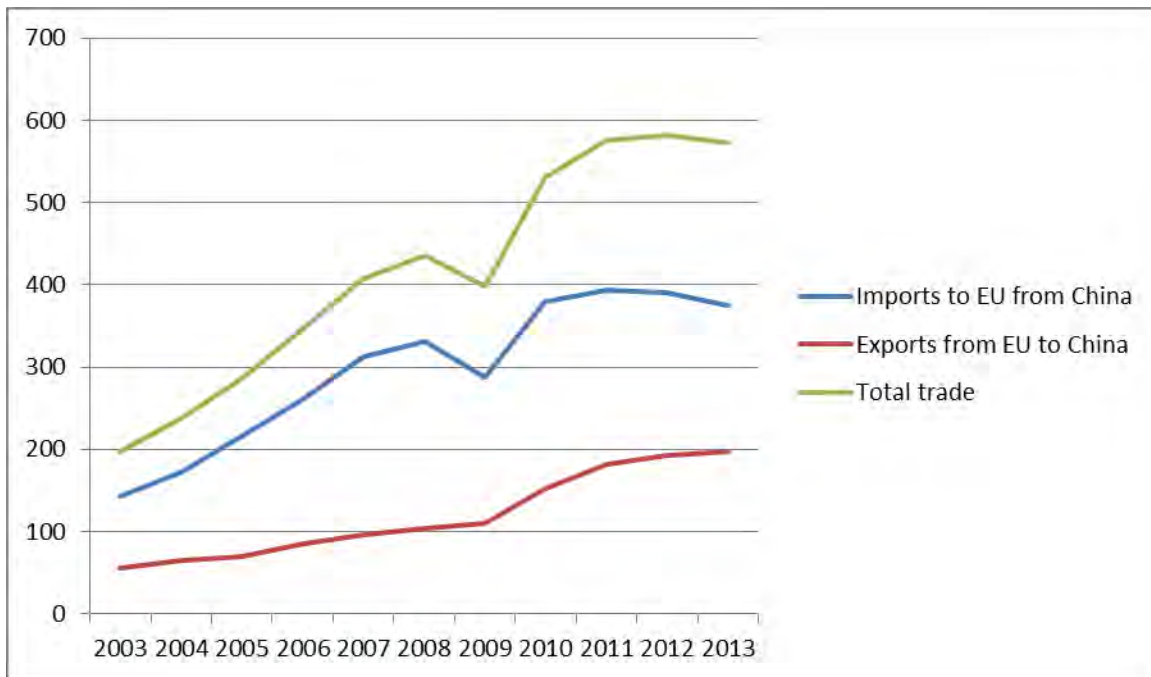
<sup>255</sup> “Understanding the WTO: The Agreements,” World Trade Organization, accessed August 9, 2014, [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/agrm5\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm5_e.htm).

<sup>256</sup> Michael White and David Gow, “EU and China in ‘Bra Wars’ Deal,” *Guardian*, September 5, 2005, <http://www.theguardian.com/business/2005/sep/06/politics.europeanunion>.

<sup>257</sup> “EU: No Trade War with China over Textiles,” *China Daily*, May 5, 2005, [http://www.chinadaily.com.cn/english/doc/2005-05/05/content\\_439661.htm](http://www.chinadaily.com.cn/english/doc/2005-05/05/content_439661.htm).

<sup>258</sup> Kong Qingjiang, “Trade Disputes Between China and the EU,” *East Asian Policy* 1, no. 2 (2009): 84-85.

Table 6. EU-China trade in goods in billions of USD<sup>259</sup>



#### D. NOTABLE EU MEETINGS WITH THE DALAI LAMA

Two meetings between the Dalai Lama and EU heads of state raised objections from China in 2007 and 2008.

##### 1. The 2007 Angela Merkel–Dalai Lama Meeting

As noted earlier, relations between the EU and China have been deteriorating since 2005, and two meetings with the Dalai Lama caused the diplomatic rift to open further. Two years after she took office as the chancellor of Germany, Angela Merkel of the Christian Democratic Union Party held a meeting with the Dalai Lama on September 23, 2007, in which they discussed human rights issues in Tibet.<sup>260</sup> Merkel, as the first German chancellor to receive the Dalai Lama, was allegedly advised against the meeting, but decided to go ahead because she felt it would support her “value-oriented foreign

<sup>259</sup>Directorate-General for Trade, “European Union, Trade in Goods with China,” 4.

<sup>260</sup>Judy Dempsey, “Despite Censure from Beijing, Merkel Meets with Dalai Lama in Berlin,” *New York Times*, September 23, 2007, [http://www.nytimes.com/2007/09/23/world/europe/23iht-berlin.4.7609899.html?\\_r=0](http://www.nytimes.com/2007/09/23/world/europe/23iht-berlin.4.7609899.html?_r=0).

policy.”<sup>261</sup> The Chinese leadership was predictably angry about the meeting and responded by cancelling several high-level meetings and withdrawing from sessions on human rights and the environment.<sup>262</sup> The cancellation of high-level meetings led to a decrease in trade cooperation over the short-term and missed trade mission opportunities. According to German media reports, the Chinese told the German diplomats in Beijing that Merkel had “crossed a red line” in meeting with the Dalai Lama.<sup>263</sup> Jiang Yu, a spokesperson for the CFM, stated shortly after the meeting that “Merkel’s meeting with Dalai Lama was not only a rude interference into China’s internal affairs and strongly hurt the feelings and emotions of the Chinese people, but also gravely harmed China-Germany relations.”<sup>264</sup>

In a press conference in November 2007, Wen Jiabao said that “We oppose European leaders meeting and receiving the Dalai Lama in their official capacity.”<sup>265</sup> It was noted that when dignitaries from other nations visited China shortly thereafter, Chinese officials openly made disparaging remarks about Germany.<sup>266</sup> As a core interest, the issue of Tibetan sovereignty is sensitive in Beijing, particularly when Merkel’s predecessor chose Chinese economic cooperation over the Tibet issue.<sup>267</sup> The Chinese ambassador to Berlin, Ma Canrong, addressed the meeting and the future of relations, stating, “relations have been seriously impaired by the reception of the Dalai Lama in the federal chancellor’s office.”<sup>268</sup> Foreign-ministry spokesman Liu Jianchao also blamed the downgraded ties on Germany and expressed a desire for Germany to make amends to

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<sup>261</sup> Stefan Kornelius and Edeltraud Rattenhuber, “Crisis Between Beijing and Berlin,” September 22, 2007, Open Source Center (EUP20070922085011).

<sup>262</sup> “Lasting Consequences,” *Der Spiegel*, October 15, 2007, Open Source Center (EUP20071014085024).

<sup>263</sup> *Ibid.*

<sup>264</sup> *Xinhua*, “China Strongly Dissatisfied with Merkel’s meeting with Dalai Lama,” September, 26, 2007, Open Source Center (CPP20070925062006).

<sup>265</sup> Sun Yu-ting and Wang Yan, “Wen Jiabao: [We] Oppose European Leaders Meeting, Receiving Dalai Lama in Official Capacity,” *Zhongguo Xinwen She*, November 28, 2007, Open Source Center (CPP20071128354005).

<sup>266</sup> Brown and Crossick, “The EU and China Time for a Change?” 4.

<sup>267</sup> Li, “China-EU Relations: Strategic Partnership at a Crossroads,” 236.

<sup>268</sup> ARH, “China’s Ambassador: Relations with Germany ‘Seriously Impaired,’” *Der Deutscher Depeschendienst*, November 23, 2007, Open Source Center (EUP2007112308500).

restore the relationship.<sup>269</sup> Merkel defended meeting with the Dalai Lama, stating that as a world leader, she alone decides whom she can meet with and that “a conversation with the Dalai Lama in the chancellor’s office must be possible, and it calls into question neither Germany’s “One China policy” nor China’s importance as an emerging economic power.”<sup>270</sup>

A few months after the incident, China seemed ready to move on, with CFM spokesperson Liu Jianchao stating that the Chinese “hope China–Germany relations could move forward on a sound and smooth track as soon as possible which is in the interest of both countries,” although he also characterized the Merkel–Dalai Lama meeting as “erroneous.”<sup>271</sup> In January 2008, tensions had abated, with Merkel repeatedly confirming China’s sovereignty over Tibet and arranging a meeting between the Chinese foreign minister, Yang Jiechi and his German counterpart.<sup>272</sup> Media coverage in China, which had previously been critical of Germany, also turned more positive, signaling that relations were bettering between the two states.<sup>273</sup> However, the EU would continue to create diplomatic issues over Tibet with protests during the 2008 Olympic torch relay and another Dalai Lama meeting.

## **2. The 2008 Nicolas Sarkozy–Dalai Lama Meeting**

A year later, on December 6, 2008, French and EU president Nicolas Sarkozy met with the Dalai Lama in Gdansk, Poland for 30 minutes. Both were in town for a 25th anniversary celebration of the Nobel Prize awarded to Lech Walesa. Sarkozy was the first head of state to meet with the Dalai Lama while simultaneously serving as EU

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<sup>269</sup> *Xinhua*, “China Urges Germany to Mend Bilateral Ties as Soon as Possible,” 20 November 2007.

<sup>270</sup> Kai Diekmann and Nikolaus Blome, “We Must Not Gamble Away What We Have Achieved,” *Bild*, November 21, 2007, Open Source Center (EUP20071121085009).

<sup>271</sup> *Xinhua*, “China Hopes Ties with Germany Could Move Forward Smoothly,” November, 6, 2007, Open Source Center (CPP20071106968137).

<sup>272</sup> “Germany’s Merkel Stresses Unchanged ‘One-China’ Policy, Important Relations,” *DDP*, January 22, 2008, Open Source Center (EUP20080122072005).

<sup>273</sup> “Restoring Relations With China: Disgruntlement Between Berlin, Beijing To End,” *Frankfurter Allgemeine*, January 20, 2008, Open Source Center (EUP20080121036002).

president.<sup>274</sup> Before the incident, China had warned that a meeting would bring about “serious consequences” for Sino-French relations, according to Chinese Deputy Foreign Minister He Yafei.<sup>275</sup> Sarkozy elected to go ahead with the meeting anyway, a decision which threatened the relationship between France and China. An article in China claimed that “to most Chinese, Mr. Sarkozy is a slimy politician wanting to take advantage of China,” and called the Chinese reaction a “gentle snub.”<sup>276</sup> Foreign-ministry spokesman Liu Jianchao stated, “by meeting with the Dalai Lama, Sarkozy has interfered with China’s internal affairs and infringed upon China’s core interests.”<sup>277</sup> China demanded that France make amends for the infraction and cancelled a Chinese–EU summit that was to be held shortly thereafter.<sup>278</sup> The loss of the summit put in jeopardy \$30 billion in trade deals that Sarkozy had secured the year before.<sup>279</sup> In addition, the billion-dollar Airbus deal between China and the EU was suspended.<sup>280</sup> While the rift was ongoing, two trade delegations travelled to Europe and signed \$15 billion in trade deals with other states.<sup>281</sup> There was also a domestic call by an anonymous Internet user for the Chinese to boycott Carrefour, a French supermarket.<sup>282</sup> With the exception of the Airbus contract suspension, the economic coercion used here, like in the Merkel case, was more of missed opportunities. China was expanding economic cooperation throughout Europe at the time and skipping over France, thus imposing an economic cost. Diplomatically, Premier Wen Jiabao’s trip to Europe included visits with several neighboring states, but he did not stop in France, and as in the Senkaku Islands and Scarborough Shoal incidents,

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<sup>274</sup> “France’s Sarkozy meets Dalai Lama as China Fumes,” *AFP*, December 6, 2008, Open Source Center (EUP20081206102007).

<sup>275</sup> Wu Zhong, “China Plays Tibet Card to the Full,” *Asia Times*, December 9, 2008, Open Source Center (CPP20081210715003).

<sup>276</sup> Nai-Keung, “Proof That China Will No Longer be Bullied.” *South China Morning Post Online*, December 21, 2008, Open Source Center (CPP20081231968066).

<sup>277</sup> Xing Zhigang and Li Xiaokun, “Envoy Brief on Meeting Dismissed,” *China Daily*, December 12, 2008, Open Source Center (CPP20081212968024).

<sup>278</sup> Li, “China-EU Relations: Strategic Partnership at a Crossroads,” 237.

<sup>279</sup> Brown and Crossick, “The EU and China Time for a Change?” 5.

<sup>280</sup> Nai-Keung, “Proof That China Will No Longer be Bullied.”

<sup>281</sup> Fuchs and Klann, “Paying a Visit,” 6.

<sup>282</sup> Li Xiaokun and Qin Jize, “Fresh Call for Boycott of French Products,” *China Daily*, December 5, 2008, Open Source Center (CPP20081205968015).

Chinese tourists were discouraged from visiting Paris.<sup>283</sup> In addition, a French governmental website was attacked by Chinese hackers in December.<sup>284</sup>

In March 2009, French foreign-ministry spokesman Eric Chevallier declared, “we are not in favor of independence for Tibet. Our position is entirely unchanged and is one of support for the territorial integrity of China and a rejection of secessionist prospects or support for the independence of Tibet.”<sup>285</sup> This appeared to lessen tensions in the spring, but the hopes for reconciliation disappeared following the awarding of an honorary citizenship to the Dalai Lama by the city of Paris.<sup>286</sup> While probably due to a combination of the events leading up to and including the Sarkozy-Dalai Lama meeting, a survey of Chinese internet users, “netizens,” found that 92 percent thought a high-level meeting with the Dalai Lama in the EU would impact their opinion of the EU, and 96 percent supported the Chinese-EU summit cancellation.<sup>287</sup> In November 2009, relations warmed, with a trade summit between the two states scheduled.<sup>288</sup> The same day, a *China Daily* article stated the “France goes back on China’s shopping list.”<sup>289</sup>

Sarkozy defended his meeting with the Dalai Lama and stated in a presidential address that “I say also in the most tranquil and calm way possible that it is the duty of a French president to meet all of the Nobel Peace Prize winners who wish to meet him, whatever their origin, whatever their beliefs, whatever the cause they defend.”<sup>290</sup> The French secretary of state for human rights, Rama Yade, supported the president and urged

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<sup>283</sup> Li, “China-EU Relations: Strategic Partnership at a Crossroads,” 237; Brown and Crossick, “The EU and China Time for a Change?” 5.

<sup>284</sup> “French Embassy in Beijing Targeted by Cyberattacks,” *LeFigaro*, December 10, 2008, Open Source Center (EUP20081210029006).

<sup>285</sup> “France Reassures China It is Still Opposed to Independence for Tibet,” *AFP*, March 13, 2009, Open Source Center (EUP20090313950050).

<sup>286</sup> “Dalai Lama’s Paris Citizenship Not Part of French Foreign Policy - City Mayor,” *AFP*, June 8, 2009, Open Source Center (EUP20090608950052).

<sup>287</sup> Men, “The EU and China: Mismatched Partners?” 346.

<sup>288</sup> Fuchs and Klann, “Paying a Visit,” 13.

<sup>289</sup> Ding Qingfen, “France Goes Back on China’s Shopping List,” *China Daily*, October 29, 2009, Open Source Center (CPP20091029968033).

<sup>290</sup> “Refusal to Meet Dalai Lama would be a Betrayal of French History,” *AFP*, December 8, 2008, Open Source Center (EUP20081208950033).

Sino-French collaboration by describing the 2008 financial downturn as “a period of financial crisis we’re going through and we need to cooperate together, calmly.”<sup>291</sup> The French economic minister did not believe that there would be much reaction to what he assumed China would consider a “minor incident” in a statement given the day after the meeting.<sup>292</sup> It appears that France did not expect the negative economic sanctions imposed. JeanLuc Domenach, a French academic on China, saw the coming Chinese reaction and forecast that “we are likely to suffer somewhat, economically,” but downplayed the impact by stating the “Chinese authorities’s rhetoric with regard to France is less robust than it was in the spring.”<sup>293</sup> In addition, he added that the Chinese “are mainly punishing the numerous turnabouts in our policy.”<sup>294</sup> In statements by the French government and academics, France urged that bilateral relations remain intact, for the progress noted earlier to continue. However, the Chinese cancellation of high-level meetings and the suspension of the Airbus contract showed that the Chinese government was ignoring the plea.

Europe is not the only region to suffer an injury to relations by meeting with the Dalai Lama; recent U.S. meetings have led to strong diplomatic responses from the regime. In 2006, the Dalai Lama was awarded the Congressional Gold Medal and the action “severely hurt the feelings of the Chinese people.”<sup>295</sup> Once President Obama met with the Dalai Lama in 2010, Chinese officials immediately stated that the meeting could undermine the Sino-U.S. relationship, insinuating that the loss of that relationship could hurt economic recovery in the U.S.<sup>296</sup> While the level of meeting cancellation and economic coercion seen in Europe was not applied to the U.S. after these meetings, it shows that China feels the need to respond to states whose officials decide to meet with the religious leader.

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<sup>291</sup> Rama Yade, *LCI Television*, December 7, 2008, Open Source Center (EUP20081207950029).

<sup>292</sup> “France urges Business as Usual with China,” *AFP*, December 7, 2008, Open Source Center (EUP20081207102001).

<sup>293</sup> JeanLuc Domenach, interview by Antione Malo, “Chinese Punish Turnabouts in Our Policy,” *Le Journal du Dimanche*, December 7, 2008, Open Source Center (EUP20081208029013).

<sup>294</sup> *Ibid.*

<sup>295</sup> Fuchs and Klann, “Paying a Visit,” 9.

<sup>296</sup> *Ibid.*, 9.

## **E. THE USE OF ECONOMIC COERCION**

Since the downturn of relations in 2005 between the EU and China over the textiles quotas and arms embargo, diplomatic relations have remained amicable. The meetings between the German and French heads of state and the Dalai Lama were an affront to Chinese interests in Tibet and strained these relations, but not relations with the EU as a whole. In both cases, economic progress continued, but there was a diplomatic freeze. Diplomacy eventually ended both of the incidents, but only after China signaled its resolve with economic coercion. In the Merkel case, there was a meeting of foreign ministers to restore relations, but in that case, as well as the Sarkozy case, relations only improved after both European leaders recognized China's sovereignty over Tibet.

China could not signal its resentment with the meetings in Europe militarily, and unlike the island disputes, the use of law enforcement would not been effective. China already maintains a military and law-enforcement presence in Tibet, and there was little incentive to move in more troops, because the European nations would not be directly impacted. Nor do China's forces have the kind of power projection that could reach Europe to signal their resolve.

Economically, the damage done was not irreversible, but mostly to signal China's displeasure. In an empirical study, Fuchs and Klann showed the existence of the "Dalai Lama effect."<sup>297</sup> Meetings of high-ranking state officials with the Dalai Lama will have an impact on the economic cooperation between China and that state in the short term. They found that the higher the official, the more severe the punishment.<sup>298</sup> In both two cases discussed here, the officials were heads of state and the reaction from China lasted about six months. China is able to impose these costs because it has a better hold over its economy than do more liberal regimes, and because the decrease of imports from the targeted state could decline as much as 16.9 percent in the two years following the meeting.<sup>299</sup> In addition, while the cancellation of summits seems as though it may have little effect, these meetings can increase bilateral trade by 8–10 percent, thus making

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<sup>297</sup> Fuchs and Klann, "Paying a Visit," 1.

<sup>298</sup> *Ibid.*, 1.

<sup>299</sup> *Ibid.*, 3-4.

cancellation a form of economic sanction.<sup>300</sup> The suspension of the Airbus contract was a more outright expression of displeasure. Fuchs and Klann found that China was more willing to bear the economic and political costs to ensure that China remained whole, thus supporting regime survival (H3).<sup>301</sup> Merkel and Sarkozy, on the other hand, operate in democracies in which economic coercion can have more effect than in China, as pointed out by Ravindran's study.<sup>302</sup> The cancellation of meetings, suspension of the Airbus contract, and the snubbing of both governments during European visits support the first hypothesis (H1), that China will use economic coercion to signal its resolve when it perceives that a state is challenging its territorial integrity.

## **F. CONCLUSION**

The meetings between the Dalai Lama and world leaders caused China to use economic coercion, whether outright, as in the Airbus contract suspension, or implied, as in the cancellation of high-level summits. The EU emphasis on human rights and democracy versus China's emphasis on economic growth and sovereignty are clear philosophical differences separating the parties. This separation led to a downturn in diplomatic relations in 2005, with the continuation of the arms embargo to China and the Olympic protests in 2008. Economically, however, the relationship continued to improve despite the textile dispute in 2005 and controversy over the increasing trade deficit with China. Trade between the two states has improved since 2003, and China has become the second-most-important trading partner for the EU, and the EU the first for China.

The use of economic coercion through the Dalai Lama effect, and suspension of the Airbus contract, supports the following hypotheses: H1, territorial integrity and sovereignty; H2, the status quo; and if extrapolated, H3, regime legitimacy. Engagement of the "Dalai Lama clique" by heads of state have been found to incite economic coercion from China, mostly to signal resolve through the Dalai Lama effect, which can reduce a

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<sup>300</sup> Fuchs and Klann, "Paying a Visit," 6.

<sup>301</sup> *Ibid.*, 7.

<sup>302</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 120.

state's exports to China as much as 16.9 percent over the two years after the meeting.<sup>303</sup> H5, economic asymmetry, and H4, nationalism, are not supported. As pointed out earlier, China holds 10 percent of the goods trade done by the EU, while the EU holds 18 percent of China's goods trade.<sup>304</sup> Despite the trade deficit, the discontinuation of trade could adversely impact the Chinese economy as much, if not more, than the EU, thus making economic asymmetry (H5) not a likely condition of the use of economic coercion. In addition, while there was one cyber-attack on a French website, nationalist sentiment in China did not appear to have much impact on policy makers, showing little support for H4. There were no protests and only a short-lived boycott of a French supermarket. China clearly sees meetings between the Dalai Lama and foreign heads of state as a challenge to its interests and uses economic coercion in an attempt to shape the behavior of another international player.<sup>305</sup>

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<sup>303</sup> Fuchs and Klann, "Paying a Visit," 3-4.

<sup>304</sup> Directorate-General for Trade, "European Union, Trade in Goods with China," 9-10

<sup>305</sup> Baldwin, *Economic Statecraft*, 38.

## V. ANALYSIS OF HYPOTHESES AND MINI-CASES

The final chapter and conclusion, Chapter V is intended to compare the case studies in the hopes of identifying one or several triggers which make the use of Chinese economic coercion more likely. The selected hypotheses are then tested against mini-case studies and the implications of the study results are discussed.

### A. INTRODUCTION

David Baldwin states that the purpose of economic coercion is to constrain the actions of an opposing international actor through negative economic sanctions.<sup>306</sup> In the cases reviewed in this thesis, China engaged in economic coercion to shape Japanese and the Philippine behavior in territorial disputes and to prevent heads of state from meeting with the Dalai Lama. In the territorial dispute cases, the use of economic coercion was more outright than in the Dalai Lama case study. Each case, however, included the use of economic coercion to signal China's displeasure with the opposing state's actions, during the current conflict and to shape future action.

These selected studies highlight the circumstances under which China will use economic coercion and other steps to secure its interests. In the Senkakus and Scarborough case studies, China employed similar economic tactics, such as cancelling high-level meetings, restricting tourism, and targeting a sector in which it had an asymmetric advantage for sanctions or inspections. The cancellation of high-level meetings had to dual impact of punishing the targeted state through lost trade and signaling displeasure through political channels. To back its signal of resolve with economic coercion, in both cases China increased patrols of law-enforcement vessels to physically protect Chinese fishermen and property, and to increase China's control over the disputed territories. In the Dalai Lama cases, increasing the presence of law enforcement in Tibet was not required, since there was no disputed territory and China controlled it outright, but the type of economic coercion was similar. China cancelled meetings, decreased tourism, increased rhetoric, and, for the Sarkozy meeting, suspended

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<sup>306</sup> Baldwin, *Economic Statecraft*, 38.

a \$30 billion Airbus contract. The case studies show that China will use economic coercion when it perceives that its territorial integrity and sovereignty or the status quo of territories are being challenged. Economic asymmetry is a necessary condition for the targeting of a specific sector, but not a trigger of coercion. The hypotheses presented in this research and the evidence contained in all three case studies are reviewed below and the conclusion as to the validity of the hypothesis is applied to recent examples to discover whether the findings of the research have any explanatory power. Finally, implications for U.S. policy and the U.S. Navy will be discussed before finalization of the argument.

## **B. PRESENTATION OF HYPOTHESES**

In this research, two hypotheses were supported across all three cases for the use of economic coercion by China: H1, when a challenge to territorial integrity and sovereignty is perceived, and H2, challenges to the status quo are perceived. Challenges to CCP legitimacy (H3) and presence of economic asymmetry (H5) are only partially supported by the cases and nationalism as a driver of economic coercion (H4) is not supported.

### **1. H1: Territorial Integrity and Sovereignty**

As shown in the case studies, China does use economic coercion in territorial disputes with other states. Both the Senkaku Island and Scarborough Shoal case studies indicate that a way for China to signal its resolve in these disputes without using military force is economic coercion. In the Senkakus case, China cancelled bilateral meetings, suspended talks on joint energy exploration, and decreased tourism to Japan. China also leveraged REE at a time when it provided 80–90 percent of Japan’s REE imports<sup>307</sup> and sent law-enforcement vessels to protect its interests.

With Japanese dependence on China for the much-needed raw material, it left Japan vulnerable to China manipulating the supply. In the two months following the

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<sup>307</sup> Pui-Kwan, “China’s Rare-earth Industry,” 2; Tabuchi, “The Hunt for Rare Earths.”

arrest of the captain and crew of the *Minjinyu 5179*, exports of REE fell drastically, signaling Chinese displeasure with the infringement of Chinese territory.

China also used economic coercion in the Scarborough Shoal dispute, again cancelling meetings, reducing tourism, and manipulating an economic sector, in this case, the fruit trade.<sup>308</sup> China restricted banana imports from the Philippines with the explanation that it was being done so to prevent the inflow of foreign organisms. This economic coercion was able to target the banana industry on Mindanao and bring domestic pressure on President Aquino to back down. As a storm passed a few months into the standoff, the Philippines and China withdrew their coast guards, with only China returning a few days later to claim de facto control over the shoal. In both cases of territorial dispute, China used a combination of economic coercion and law enforcement vessels solidify its interests.

The third case study examines China's response to Dalai Lama visits with heads of state in Europe. While Tibet is not a disputed territory between two recognized states, it is the subject of an internal conflict between the PRC and a people whom they believe are separatists. As the Dalai Lama calls for a more meaningful autonomy, China believes his real agenda is to push for an independent Tibetan state. Therefore, reception of the Dalai Lama by other heads of state is perceived as supporting the exiled government. China responded to a perceived challenge to its territorial sovereignty and integrity with the "Dalai Lama effect," in which it is shown that trade between China and a targeted state decreases by as much as 16.9 percent over the two years following a meeting.<sup>309</sup> China also cancelled high-level meetings, withdraw from conversations on the environment, and, in France, boycotted a summit, targeted tourism, and suspended a \$30 billion Airbus deal. Diplomatically, both these cases subsided following repeated statements by the German and French governments recognizing China's sovereignty over Tibet. China's heavy-handed snubbing and outright suspension of lucrative contracts effectively indicated China's displeasure with the offending heads of state and warned others not to interfere in like manner.

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<sup>308</sup> Ravindran, "China's Potential for Economic Coercion in the South China Sea Disputes," 115.

<sup>309</sup> Fuchs and Klann, "Paying a Visit," 3-4.

## 2. H2: The Status Quo

The status quo defended by China is made up of bilateral agreements and alleged formal and informal deals with other states. The case studies support an assertion that changes to the status quo will cause China to use economic coercion. China's policy on territorial disputes is, as Deng Xiaoping stated, to "set aside dispute and pursue joint development."<sup>310</sup> China is not ignoring issues of sovereignty under this policy, just delaying disputation until a later time. With this in mind, the actions of a foreign power attempting to change current conditions is perceived in China as an affront to its interests. In the Senkakus dispute, although the islands are administered by Japan, the arrest and charging of Zhan Qixiong violated the 1997 China–Japan Fisheries Agreement and a supposed secret deal between China and the LDP. Unfortunately, the DPJ officials in power did not know about this arrangement. Previously, any vessel and crew that was detained was released in short order, and any charges were filed by the state under which the vessels were flagged. The arrest and charging of Zhan violated this arrangement. As a result, China responded with law enforcement vessels and economic coercion, most notably the suspension of REE shipments. During the Scarborough Shoal incident, Chinese interests were offended due to an attempted search and seizure by a Philippine warship. This appeared to be an escalation from the DOC terms and therefore elicited a PRC response of economic and law-enforcement coercion to protect Chinese interests in the region—which it now controls.

Tibet lends a different perspective on the importance of the status quo in disputed territories. China legitimates its hegemony according to the Seventeen-Point Agreement, which made Tibet an autonomous region of China. Since then, China has administered the Tibetan region and views reception of the Dalai Lama by foreign heads of state as hostile to its interests. International support for the Dalai Lama as the leader of an independent Tibet would change the status quo significantly and possibly trigger the loss of the Xinjiang region and Inner Mongolia. China sees meetings with the Dalai Lama as a challenge to a settled right to rule Tibet, and responds with sticks.

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<sup>310</sup> "Set Aside Dispute and Pursue Joint Development," Ministry of Foreign Affairs of the People's Republic of China.

### **3. H3: Regime Legitimacy**

The legitimacy of the CCP was not questioned in the maritime disputes of the Senkaku Islands and Scarborough Shoal. While Japan and the Philippines did challenge China's interests, they did not attack the CCP's right to rule China. In Tibet, however, the loss of Tibet could set off a chain reaction in which China might lose a large part of its territory to separatists. This blow would challenge the legitimacy of the CCP, which would descend from being the party of economic prosperity to the party that allowed foreigners to carve up China again. That said, the prospect of the CCP's toppling is more than a few steps removed from receiving the Dalai Lama as a respected international figure, and many more events would have to occur before China lost Tibet, let alone Xinjiang and Inner Mongolia. This being so, it is likely that since the Dalai Lama case is the only instance where a challenge to the CCP's legitimacy could be involved, H3 is not supported by the evidence and another hypothesis is more likely.

### **4. H4: Chinese Nationalism**

In each of the case studies, Chinese citizens protested, boycotted, or wrote editorials to denounce foreign actions, but the nationalist outbursts were more prevalent in the Senkaku Island case study than the others. Although nationalist outcries were seen, the evidence does not support the hypothesis that these protests influenced Chinese decision making. The Senkaku Island dispute aroused the most public reaction; in the Scarborough Shoal case, there were small protests and a few cyber-attacks; but in both cases, the steps China took to signal resolve were very similar. China responded as if operating out of a playbook: applying economic coercion by targeting a resource on which it had an asymmetrical advantage, suspending travel, and canceling meetings. The difference was a matter of detail: the suspension of an export versus increased inspections on an import. Nationalism in the Senkakus case may have played a role in China's decision to ban REE over a longer period of time, past when they achieve a better law enforcement presence around the Senkaku Islands and the release of Zhan.

In the Dalai Lama case, hypothesis H4 also remains unsupported. Nationalistic fervor mostly consisted of a call to boycott a French supermarket chain and one cyber-

attack. There was little pressure from the general population to strike at Germany or France, although the EU's favorable reputation did decrease. Comparing the Senkakus and Scarborough case studies and factoring in the lack of outcry over the Dalai Lama meetings, the case studies do not support nationalism as a restrictor in Chinese foreign policy.

## **5. H5: Asymmetric Trade Advantage**

While China's economic coercion depends on an asymmetric relationship with the target, that relationship is not a trigger per se. In the Senkakus and Scarborough cases, China targeted sectors in which it could impose costs without absorbing many costs itself. With respect to Senkakus, China had a near monopoly on the REE sector and could manipulate the supply as it pleased. In the Scarborough case, China chose an industry in which it is a major importer, and thus important to the target state, but—owing to asymmetry—of negligible importance to the Chinese. In both cases, the suspension of trade could be sustained by the instigator. China uses economic coercion in retaliation; asymmetry in economic trade is an important part of that, but not sufficient to trigger coercive action. As shown in the discussion of the Dalai Lama, China is willing to use sticks even when approximately matched in economic strength. An asymmetrical relationship does have an important part in the explanatory power of results. China's near monopoly or overwhelming share of trade in a sector increases an opposing state's vulnerability to coercion.

## **C. APPLICATION OF HYPOTHESES IN RECENT DISPUTES**

The explanatory power of the findings centers on under what conditions it can be predicted that China will be more likely to use economic coercion. The confirmed hypotheses should predict which sectors are vulnerable to economic coercion and what will trigger an action. In cases where the targeted state is dependent on China, more stringent actions might be taken to signal resolve. To expand on the major studies in this research, three recent examples are presented below to help ascertain whether the findings hold true and Chinese actions are in line with predictive models.

## 1. The 2012 Senkakus Dispute

On September 10, 2012, Japan announced that it would purchase the Senkaku Islands from their private owner.<sup>311</sup> The announcement renewed the territorial dispute, which had lain dormant two years, since the arrest of Zhan Qixiong. Prime Minister Yoshihikoda Noda stated that the purchase was intended to reduce tensions in the maritime dispute, not to incite China.<sup>312</sup> In response, the CFM issued a statement that characterized the move as a “severe infringement of Chinese territorial sovereignty, which gravely hurts the feelings of the 1.3 billion Chinese people.”<sup>313</sup> In a later statement, vice foreign minister Zhang Zhijun stated that “Japan has no right to buy or sell Chinese territory in any way and no transaction is allowed over even one inch of the Diaoyu [Senkaku] Islands.”<sup>314</sup> Zhang also linked the sale directly to an infringement on China’s territorial sovereignty.<sup>315</sup> Domestically, the Chinese population responded with mass protests. On September 15<sup>th</sup>, Japanese businesses and property were damaged. On September 18<sup>th</sup>, the anniversary of the Japanese invasion of Manchuria, the protests spread, causing more damage to Japanese interests.<sup>316</sup> From the Chinese perspective, the selling of the islands, regardless of the intention of the Japanese state, challenged their claim and thus China’s territorial integrity.

From the previous row over the Senkaku Islands, it might be expected that China would counter this affront by economic coercion and increased maritime patrols. The previous case would predict that China would find an asymmetrical relationship with Japan and reduce imports or exports accordingly. As noted, Japan’s reliance on China for REE decreased after the 2010 territorial dispute, leaving China with fewer options for

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<sup>311</sup> “Timeline: The Diaoyu-Senkaku Islands Dispute,” *South China Morning Post*, last updated September 18, 2012, <http://www.scmp.com/news/china/article/1039204/timeline-diaoyu-senkaku-islands-dispute>.

<sup>312</sup> “Central Government Plans to Buy Senkaku Islands,” *Asahi Shimbun*, July 7, 2012, [http://ajw.asahi.com/article/behind\\_news/politics/AJ201207070062](http://ajw.asahi.com/article/behind_news/politics/AJ201207070062).

<sup>313</sup> *Xinhua*, “Statement of the Ministry of Foreign Affairs of the People's Republic of China,” September 10, 2012, [http://news.xinhuanet.com/english/china/2012-09/10/c\\_123697340.htm](http://news.xinhuanet.com/english/china/2012-09/10/c_123697340.htm).

<sup>314</sup> *Xinhua*, “Japan has No Right to Buy or Sell Chinese Territory: Official,” October 27, 2012, [http://news.xinhuanet.com/english/china/2012-10/27/c\\_123877013.htm](http://news.xinhuanet.com/english/china/2012-10/27/c_123877013.htm).

<sup>315</sup> *Ibid.*

<sup>316</sup> “Timeline: The Diaoyu-Senkaku Islands Dispute,” *South China Morning Post*.

negative economic statecraft. No embargo was put into effect, but Japan did notice a dip in car sales in China, as documented by Dong Yang of the China Association of Automobile Manufacturers and Toshiyuki Shiga of Nissan.<sup>317</sup> While this did not imply a state response to the challenge, it did show that Chinese consumers are responsive to Japanese actions. Consumer boycotts were common in the cases studied, but they were of minimal importance next to state actions. In this instance, it appears that the state did not resort to economic coercion, but the population may have. In addition, China increased its law-enforcement patrols in the area.

## 2. Second Thomas Shoal

In the Spratly Islands, 105 nautical miles west of the Philippines, an old rusted WWII-era landing transport ship, BRP *Sierra Madre*, has been grounded with a rotating crew from the Philippine military since 1999. China recently established a presence around the vessel and is attempting to block the Philippines from resupplying the marines or swapping the crew. Liu Zhemin states that “China has sovereignty over the Nansha [Spratly] Islands and adjacent waters, nor will it shake the Chinese government's will and resolution to safeguard territorial sovereignty, maritime rights, and interests.”<sup>318</sup> Chinese air force major-general Zhang Zhaozhong advocated that China take on a “cabbage strategy,” in which the PLAN would surround the area further out and Chinese coast-guard vessels would patrol closer in.<sup>319</sup> China has characterized the presence of the vessel and its crew as contrary to the DOC and maintains that it has sovereignty over the shoal.<sup>320</sup> Also asserting ownership of the shoal, the Philippines recently updated a claim sent to the UN Arbitral Tribunal under the UN Convention on the Law of the Sea to

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<sup>317</sup> Kiyoshi Takenaka and Sui-Lee Wee, “Japan Infuriates China by Agreeing to Buy Disputed Islands,” Reuters, September 10, 2012, <http://www.reuters.com/article/2012/09/10/us-china-japan-idUSBRE8890AU20120910>.

<sup>318</sup> *Xinhua*, “China Lodges Solemn Representation to Philippines over South China Sea Dispute,” March 31, 2014, [http://news.xinhuanet.com/english/china/2014-03/31/c\\_133228099.htm](http://news.xinhuanet.com/english/china/2014-03/31/c_133228099.htm).

<sup>319</sup> Bonnie S. Glaser and Alison Szalwinski, “Second Thomas Shoal Likely the Next Flashpoint in the South China Sea,” *Jamestown Foundation*, June 21, 2013, [http://www.jamestown.org/single/?tx\\_ttnews%5Btt\\_news%5D=41054&no\\_cache=1#.U\\_F4JvldVqU](http://www.jamestown.org/single/?tx_ttnews%5Btt_news%5D=41054&no_cache=1#.U_F4JvldVqU).

<sup>320</sup> *Ibid.*

include it, further straining relations between the two states.<sup>321</sup> Wu Schicun, president of the National Institute for South China Sea Studies, called the filing of the complaint “an abuse of law procedures.”<sup>322</sup>

Based on the case studies and hypotheses above, China would be expected to respond to the Philippine claim submission and presence on the shoal. However, the initial provocation—the grounding of the ship—occurred in 1999, when China lacked the maritime capability it wields now. The status quo for the past 15 years has been occupation of the ship by the marines; the Philippines have not built additional structures on the shoal. For economic coercion to be effective, action should have been taken in 1999 to prevent the Philippines from establishing a presence. This research found no evidence that sticks were used at the time. However, China was not the economic juggernaut it is today and held less weight in the Philippine economy. In 2002, three years after the grounding, China was merely the ninth-largest trading partner with the Philippines<sup>323</sup> and may not have had enough economic advantage to attempt coercion. China was also nearing the finalization of 15 years of negotiation to join the World Trade Organization, which may have limited its desire to use economic coercion. Instead, China used the second tactic found in the case studies, the deployment of law-enforcement vessels. China maintains a constant presence by the shoal and attempts to interdict the resupplying of the marines to starve them off.<sup>324</sup> China responds with the use of law enforcement vessels to protect its interests, which was seen in both the territorial dispute case studies. The building of additional structures on the shoal, would be a further provocation and may elicit economic coercion from China. With economic coercion not expected due to the upholding of the status quo in this dispute, the findings did rightly predict that China would attempt to enforce its claim through coast-guard ships.

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<sup>321</sup> Carl Thayer, “South China Sea: Regional States Push Back Against China,” *The Diplomat*, April 7, 2014, <http://thediplomat.com/2014/04/south-china-sea-regional-states-push-back-against-china/>.

<sup>322</sup> *Xinhua*, “The Philippines’ Violation of International Laws to End in Vain,” April 3, 2014, [http://news.xinhuanet.com/english/indepth/2014-04/03/c\\_133235657.htm](http://news.xinhuanet.com/english/indepth/2014-04/03/c_133235657.htm).

<sup>323</sup> “Trade Relations,” Philippine Consulate General Shanghai, accessed August 15, 2014, <http://www.philcongshanghai.org/pages.asp?ids=519>.

<sup>324</sup> Carl Thayer, “South China Sea: Regional States Push Back Against China,” *The Diplomat*, April 7, 2014, <http://thediplomat.com/2014/04/south-china-sea-regional-states-push-back-against-china/>.

### 3. The President Obama and Prime Minister Cameron Meeting with the Dalai Lama

President Barack Obama had his third meeting with the 14th Dalai Lama on February 21, 2014. Like his first two meetings, it was protested by the PRC, with the usual denunciations of U.S. interference in Chinese domestic matters.<sup>325</sup> China emphasized cooperation with the U.S., but noted that meeting with the Dalai Lama could undermine the relationship. Deng Yushan, a *Xinhua* staff writer, stated that “it is common sense that slamming on the brakes of a fast-moving car might result in unpredictable consequences” and urged the U.S. to respect its relationship with China.<sup>326</sup> CFM spokesperson Qin Gang touted Chinese economic progress, including a higher standard of living and the abolition of serfdom, as “facts that won’t be denied by anyone without political bias,” drawing attention to the positive aspects of Chinese rule without broaching Western concerns over human rights. Obama, meanwhile, endorsed the Dalai Lama’s middle-way approach, stating that he is not challenging China’s territorial integrity.<sup>327</sup> While Obama endorsed the middle way, China denounced it, stating that it ran counter to “history and reality.”<sup>328</sup> Despite Chinese rhetoric, Obama proceeded with the meeting, disregarding the threatened potential economic impacts, which did not occur.

Prime Minister David Cameron met with the Dalai Lama on May 14, 2012, in the face of Chinese protests. A British spokesman held that “it is for the prime minister and deputy prime minister to choose who they see. The Dalai Lama is an important religious figure and advocate for peace and the prime minister regularly meets with such

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<sup>325</sup> *Xinhua*, “China Expresses ‘Strong Indignation, Firm Opposition’ Against Obama-Dalai Lama Meeting,” February 21, 2014, [http://news.xinhuanet.com/english/china/2014-02/22/c\\_133134386.htm](http://news.xinhuanet.com/english/china/2014-02/22/c_133134386.htm).

<sup>326</sup> Deng Yushan, “Commentary: White House Should Not Become Bully Pulpit for Tibetan Secessionists,” *Xinhua*, February 21, 2012, [http://news.xinhuanet.com/english/indepth/2014-02/21/c\\_133133119.htm](http://news.xinhuanet.com/english/indepth/2014-02/21/c_133133119.htm).

<sup>327</sup> “Reiterating Support for Middle Way Approach, President Obama Says Results in China and Tibetans’ Interest,” Central Tibetan Administration, last updated February 21, 2014, <http://tibet.net/2014/02/21/reiterating-support-for-middle-way-approach-president-obama-says-results-in-china-and-tibetans-interest/>.

<sup>328</sup> *Xinhua*, “China Focus: What is the ‘Middle Way’ the Dalai Lama Preaches?” February 22, 2014, [http://news.xinhuanet.com/english/indepth/2014-02/22/c\\_133135524\\_2.htm](http://news.xinhuanet.com/english/indepth/2014-02/22/c_133135524_2.htm).

figures.”<sup>329</sup> China, on the other hand, stated that the meeting interfered with its domestic affairs and affronted the Chinese people.<sup>330</sup> CFM spokesman Hong Lei stated that the British “grossly interfered in China's internal affairs, hurt the feelings of Chinese people.”<sup>331</sup> Notably, Cameron’s meeting with the Dalai Lama did not provoke as much Chinese media attention as Obama’s. Nevertheless, the meeting was seen as a challenge to Chinese interests by its implied support for Tibetan separatism.

The previous case studies encourage the assumption that China would cancel high-level meetings, suspend contracts, and possibly issue travel warnings in the wake of the Dalai Lama visits. Despite the uproar, however, there appears to be little movement toward economic targeting of the U.S. This hesitation could be due to America’s standing as the number-one trading partner of China or and attempts to realize a new great power relationship. In England, high-level meetings were cancelled, including a visit while on European tour by Wu Bangguo, chairman of the standing committee of the National People’s Congress.<sup>332</sup> At the same time, British officials in Beijing discovered that their meetings were cancelled or reduced to lower levels.<sup>333</sup> Despite these shows of disrespect, China did not suspend travel or economic trade with England.

#### **D. FUTURE LIKELIHOOD OF CHINESE ECONOMIC COERCION**

China’s rise in relative economic and military power in the international system will set the conditions necessary for an increase in the use of economic coercion, but it may also limit its usage as well. Economically, as China continues to progress and take a larger share of international trade, more states will become dependent on China for their economic survival. This dependency translates to more sectors vulnerable to economic

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<sup>329</sup> “China Protests Dalai Lama Meeting,” *Radio Free Asia*, May 15, 2012, <http://www.rfa.org/english/news/tibet/meeting-05152012153045.html/>.

<sup>330</sup> *Xinhua*, “China Lodges Representation over David Cameron-Dalai Meeting,” May 15, 2012, [http://news.xinhuanet.com/english/china/2012-05/15/c\\_131589679.htm](http://news.xinhuanet.com/english/china/2012-05/15/c_131589679.htm).

<sup>331</sup> *Ibid.*

<sup>332</sup> “Top Chinese Official Cancels UK Visit over Dalai Lama Meeting,” *BBC*, May 25, 2012, <http://www.bbc.com/news/uk-politics-18208252>.

<sup>333</sup> “China Halts UK Ministerial Meetings over Dalai Lama Row,” *BBC*, June 14, 2012, <http://www.bbc.com/news/world-asia-china-18440767>.

coercion, and thus, more options for China to signal its resolve and desires through. China's ability to influence the internal decision-making processes of other states will increase. While a greater ability to use economic coercion could lead to an increase in cases, it could also decrease its use for two reasons. First, states with large trade dependency on China may begin to make decisions with China's interests in mind, thus imposing a type of self-imposed behavior modification which would benefit China. This would lead to the number of challenges in which China would feel the need to respond with economic coercion decreasing. Second, as China's economic sway over states increases, its ability to shape state behavior without the actual use of economic coercion, just the threat of it may influence a state. Although China's economic ability to use coercion may increase, its willingness and necessity to do so may not.

Similarly, China's rise in military power may reduce its use of economic statecraft. The military modernization program improves China's might and improves its standing as a regional power. As a result, states within the region and under threat of China's military will be less likely to challenge Chinese interests. Fear of Chinese military retribution will increase and shape the behavior of states before incidents occur. The military also adds an additional tool for China to use to signal its resolve in disputes, thus lowering the likelihood of economic coercion. On the other hand, as China's military remains a regional and not global power, states outside of the region may continue to face economic coercion. For states within Asia, as China's military might grows will reduce the likelihood of economic coercion, while more far-flung states may still see it as a tactic until military modernization makes projection of power more likely.

The increasing number of democracies makes the use of economic coercion more likely globally, not only from China. Democracies are more vulnerable to economic coercion from its ability to increase domestic pressure on regimes through the imposition of costs on the population. Democracies will continue to be a likely target of economic coercion because of this susceptibility. States such as Vietnam remain insulated to economic coercion, while Japan and the Philippines are not, based solely on regime type. This translates to China's use of economic coercion more likely to be utilized against democracies due to its ability to pressure regimes from within.

China's rise may increase its ability to use economic coercion, the combination of an additional tool, the military, and the a reduction in the need for it may cause a drop in the likelihood of Chinese economic coercion. When used, China is likely to target democracies outside of the reach of China's military to shape state behavior through the use of economic coercion.

#### **E. IMPLICATIONS FOR THE U.S. AND U.S. NAVY**

The case studies selected have economic and security implications for the U.S. and its interests in the Asian–Pacific region. First, China not only uses economic coercion to defend its territory and the status quo, but may also resort to law enforcement to improve its position. The vulnerability of U.S. economic sectors to Chinese coercion is troublesome. The targeting of specific sectors was carried out where China held an advantage. Where China's advantage was less pronounced, it engaged in economic coercion, but did not target a sector. The Obama administration has had three meetings with the Dalai Lama and has thus far avoided the measures that were used against France and Germany. As China becomes more powerful economically, it may exploit the vulnerability of U.S. industrial sectors when it perceives challenges. To avoid being targeted, all sectors should diversify as to suppliers and markets. If China makes up only a small portion of a larger marketplace, it will have difficulty retaliating through the sector involved; on the other hand, if China is relied upon for the preponderance of a raw material or necessary good, the state is vulnerable to economic coercion. Economic diversity is the first step towards limiting PRC control over American markets and resources.

From a security perspective, it is significant to note that the U.S. has treaty obligations with the targeted states studied. One of the PRC's responses to maritime challenges is to increase law-enforcement patrols in disputed areas. This presence protects Chinese interests, but also increases tensions and the risk of an aggravating incident that will precipitate U.S. involvement based on treaty obligations. In Japan, the 1951 San Francisco Treaty and the 1972 Agreement between Japan and the United States of America Concerning the Ryukyu Islands and the Daito Islands delineate that the U.S.

is obligated to aid Japan in the event of attack, and this obligation covers the Senkaku Islands. The current administration has affirmed its commitment to the treaty, with President Obama in 2014 and Secretary of State Clinton in 2010 making reference to the islands as included in the agreement.<sup>334</sup> In the Philippines, the U.S. relationship is governed by the mutual-defense treaty between the Republic of the Philippines and the United States of America. The U.S. has not clarified whether it considers Scarborough Shoal to be covered and it is unclear whether the U.S. would aid the Philippines if it were defending its rights there. Secretary Clinton stated that the U.S. would remain neutral in the dispute between China and the Philippines, but hoped it can be resolved peacefully.<sup>335</sup> Treaty commitments could expose the U.S. to large conflicts over the rights to eight small islands or five rocks. The U.S. should use caution to avoid a conflict where it has little at stake.

To mitigate the security risk the territory disputes pose, the U.S. has three policy options: abandon allies, stay neutral, or stand with allies, but only the latter are feasible. The abandonment of treaty allies would send a signal throughout Asia that the U.S. cannot be trusted and would push many states toward alliance with China. This would be inimical to U.S. interests in balancing other states against China, and thus it would be off the table. The U.S. currently maintains indifference in the ultimate resolution of sovereignty in the territorial disputes. A neutral stance toward disputants is likely the only policy that will incur neither China's wrath nor an ally's disapproval. In the cases researched, to back up treaty allies more definitively and formally to side with Japan or the Philippines would likely be seen as a violation of the status quo and thus encourage China to increase patrols and target the U.S. It is preferable that the U.S. encourage third-party mediation of territorial disputes and continue to attract regional allies to balance China's growth. A formal crisis-resolution framework should be worked out to mitigate

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<sup>334</sup> "Obama Says U.S. Will Defend Japan in Island Dispute with China," *The Guardian*, April 24, 2014, <http://www.theguardian.com/world/2014/apr/24/obama-in-japan-backs-status-quo-in-island-dispute-with-china>; "Clinton: Senkakus Subject to Security Pact," *Japan Times*, September 10, 2010, <http://www.japantimes.co.jp/news/2010/09/25/national/clinton-senkakus-subject-to-security-pact/>.

<sup>335</sup> Joe Galvez, "Clinton: U.S. Won't Take Sides in Panatag Shoal Dispute," *GMA News*, May 1, 2012, <http://www.gmanetwork.com/news/photo/18911/clinton-us-won-t-take-sides-in-panatag-shoal-dispute>.

the risk of incidents that provoke military action on either side. The U.S. Navy should continue its forward presence in Asia to retain the confidence of treaty allies and deter Chinese escalations.

#### **F. SUMMARY AND OPPORTUNITIES FOR FURTHER RESEARCH**

While the cases presented are not inclusive of the few alleged incidents of economic coercion, the results suggest that China uses economic coercion to defend its territorial interests while also pursuing its stated foreign policy of putting disputes aside to focus on cooperation and economic growth. Further research into the topic could yield a more exhaustive list of alleged instances of coercion to test the hypotheses affirmed. Since one of the drivers of coercion is also a core Chinese interest—that is, territorial integrity and sovereignty—additional research might look at other core interests to see if they have likewise been defended through economic coercion.

The researcher's hypotheses were further tested in four comparatively minor examples of territorial challenges or violations of the status quo, and were confirmed consistent with China's historical response to violations—cancellations, travel warnings, rhetoric, and, if advantageous, sanctions. The U.S., thus far has not been a target of economic coercion due to meetings with the Dalai Lama, but as China's economic strength rises, U.S. economic sectors could become more vulnerable. In addition, as a supplementary response China uses law enforcement vessels to physically defend its territorial interests. From a security perspective, increased patrols in disputed waters increases the likelihood of a maritime incident happening between states, possibly with states that are treaty allies with the U.S. In the future, with China's responses being seemingly standardized, it is reasonable to expect that further challenges or escalations would elicit similar responses. Depending on the state's dependencies, economic coercion could threaten a sizable portion of a target's GDP and possibly destabilize the Asian–Pacific region.

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