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Abstract

This article lays out the overarching context of economic cooperation in Asia and discusses the two big questions: the strategic consequences of economic integration in Asia and the economic consequences of the lack of a security consensus in Asia. The rise of China is central to both. China's economic rise has led to the rapid growth of Asian economic integration as well as given rise to security rivalries, both land and maritime, all around its borders. The article examines whether economic integration will mitigate security rivalries or whether the absence of a regional security arrangement instead of the hub-and-spokes US-centred security system in the Asia-Pacific will impede the growth of economic and political cooperation. Much depends on the unpredictable and evolving interaction of Chinese behaviour and the US and Asian responses to it.

Keywords

Economic integration, security consensus, FTAs, FDI, plurilateral

Introduction

This article takes a broad overview of the political and security context of the growing economic integration of Asia, which for the purposes of this article we define as East, Southeast and South Asia, poses two big questions below and attempts some tentative answers in the light of international relations theory.

Two big questions: What are the strategic consequences of economic integration for Asia and economic consequences of the absence of a security consensus for Asia?

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If one looks at the big picture over the post-Cold War period in Asia, there are two overarching trends.

First, the growing economic integration of the Asia-Pacific region through trade and investment, and to a lesser extent through movement of people, all helped by multilateral and regional liberalization of trade within Asia, which for our purposes I define as East, Southeast and South Asia. This has led to the growing intermeshing of economies of the larger Asian region and even more so in East Asia (China, Japan, South Korea, Taiwan, Hong Kong) and in the Association of South-East Asian Nations (ASEAN). The rise of China to the position of the world's second-largest economy and trading nation, and the growing importance of China in the trade profiles of all Asian countries have made Asia's trade increasingly China oriented over the past decade. Some of the major features as of 2012, the latest year available for comprehensive trade figures, are as follows.¹ In 2012, each of the major trading countries/groups in Asia 'traded more with other major Asian countries/groups than with the USA and the EU combined'. Thus, of China's \$3.867 trillion trade, \$1047 billion (28 per cent) was with its major Asian partners compared to 26 per cent with the USA–EU bloc. Of Japan's \$1.47 trillion trade, 39 per cent was with its major Asian partners, 21 per cent with USA–EU. Of the ASEAN's \$2.475 trillion trade, 56 per cent was with its Asian partners including ASEAN countries disaggregated, and 18 per cent with USA–EU. Of India's \$791 billion trade, 25 per cent was with major Asian partners and 21 per cent with USA–EU. These figures actually underestimate intra-Asian trade as they consider only major Asian trading partners, China, Japan, Korea and ASEAN and not many smaller countries. These figures also hold true for exports alone, the driver of much of Asian growth, particularly China's, except for China, which still exports more to the USA–EU than to Asia, the others exporting more to Asia.

This Asian trade integration was driven by both multilateral trade liberalization under the rules of the General Agreement on Tariffs and Trade (GATT), later World Trade Organization (WTO) since 1996, and by bilateral and plurilateral (multi-country, which can be both regional as well as cross-regional) free trade agreements in the Asian region. To give an indication of the growth in the number of such bilateral agreements between 2000 and 2013, the number of WTO-notified bilateral agreements within Asian sub-regions (for example, within East Asia, within South Asia) grew from 1 to 8, and the number of bilateral agreements across sub-regions (for example, between an East Asian and a South Asian country) grew from zero to 17. If one takes both WTO-notified bilateral free trade agreements (FTAs) and those not yet notified (including those under negotiation) between 2000 and 2013, the number of FTAs within Asia grew from 1 to 43!² If we look at Asian plurilateral FTAs between 2000 and 2013, the number of such WTO-notified FTAs grew from 4 to 7, and number of FTAs between an Asian plurilateral organization (for example, ASEAN) and individual Asian countries grew from zero to 5. If we look at all Asian plurilateral FTAs, both WTO-notified and those not yet notified (including those under negotiation) from 2000 to 2013, then the number of Asian plurilateral FTAs grew from 4 to 12, and the number of

FTAs between an Asian plurilateral grouping (for example, ASEAN) and individual Asian countries grew from zero to 8. These figures are indicators of the rapid proliferation of Asian FTAs, both bilateral and plurilateral since 2000, which have been the drivers of trade integration within the region. Such trade integration also was a driver of, and conversely was also driven by, foreign direct investment (FDI) flows, although the latter will be more politically influenced than trade alone. FDI data from the United Nations Conference on Trade and Development (UNCTAD) database indicate a massive increase in outward FDI from five major Asian countries/blocs (Japan, China, Korea, ASEAN and India) between 2000 and 2012, a leap from \$46 billion to \$309 billion, of which non-Japan FDI outflows skyrocketed from \$15 billion to \$187 billion, led by a Chinese jump from \$1 billion to \$84 billion. This compares with a slippage of combined US+EU FDI outflows for the same years from \$952 billion to \$652 billion.³ A very large part of Asian outward FDI flows would have been to Western countries but it can safely be assumed that an increasing part of it would have been intra-regional and closely correlated with growing intra-Asian trade integration and also driving the latter by the internationalization of production chains.

Second, the striking fact about the security/strategic situation in Asia is the absence of a security consensus and an overall security treaty or regional cooperation treaty analogous to the North Atlantic Treaty Organization (NATO) in the North Atlantic and the European Union (EU) on the European continent. In the post-1945 Asia-Pacific region, the strategic alignments have been of a hub-and-spokes type. The USA as the security provider for non-communist Asia has been the hub. It has had spokes-like individual security guarantee treaties with Japan, South Korea and Australia and less formalized arrangements with other states/entities from Taiwan to Indonesia. Over the past decade, the rise of China—touted as the peaceful rise until recent assertive actions in all directions since 2011—has led to the aggravation of existing and new territorial and maritime boundary disputes and strategic, particularly naval, rivalries all around China from the East China Sea to through the South China Sea to the Sino-Indian Line of Actual Control (LAC). Apart from the tension over Taiwan, China has now asserted itself aero-navally in the East China Sea over the Diaoyu/Senkaku islands and has made sweeping maritime territorial claims in the South China Sea over the Paracel and Spratly islands, and has asserted that its vital national interests extend to the second Pacific island chain, bringing it into conflict with Vietnam, Philippines, Malaysia, Indonesia and Brunei. Economic growth has had strategic consequences. China's economic growth is redefining its core interests, most recently expanding to the second Pacific island chain and the Indian Ocean, much further afield, linked to protection of energy and raw material supplies. China now has military supply and port construction relationships, plus substantial trade and aid, with Pakistan, Sri Lanka, Bangladesh and Myanmar in the Indian Ocean.

The big question in the political economy of Asia is how these two contradictory tendencies will play out over the coming years? Will growing economic interdependencies provide the ballast for building political and security

cooperation resulting in regional or pan-Asian security consensus embodied in a treaty or treaties? Or will the absence of a security consensus and growing strategic rivalries and distrust prevent the political integration that usually follows growing economic integration?

Can Asia-wide political/security cooperation be built as a consequence of economic integration?

At the regional, all-Asian level, or even at the East Asian or Southeast Asian level, despite the existence of the US–Japan and US–South Korea security treaties, the existence of ASEAN as a political grouping—although not a situation of political integration unlike the EU—since 1968, and that of SAARC since 1985, there has been no institutionalization of security relations, even after the Cold War. Indeed, the rise of China and its assertiveness since 2011 has led the US to announce a planned ‘rebalance’ or ‘pivot’ of its aero-naval forces from the Atlantic in the ratio of 60–40 favouring the Pacific, a clear indication of intent to balance the rise of China.

This is partly the legacy of the history of the Cold War in Asia, and partly a question of fundamental differences in regime types between a democratic/democratizing Asia and an authoritarian communist party-led China. However, it is also a consequence of unresolved territorial, including maritime, disputes. Recently, the democratic peace theory, widely popular in the West, has itself been questioned, with Gibler (2007) making the argument that democracy and peace are symptoms not causes of the removal of territorial issues between neighbours.

The first thing that China—and India—need to diligently pursue, is to settle or freeze/shelve outstanding border issues, including maritime border issues, with smaller neighbours. As Gibler (1996) shows, territorial settlement treaties are more likely than anything else to end the incidence of war. The next most important thing is to promote economic cooperation in a way that creates ‘incentives without the fear of being dominated’, losing one’s autonomy, etc., for the smaller states.

The literature indicates that the largest state typically has to be prepared to bear a disproportionately large share of the costs of regional cooperation-building and maintenance and obtain only a disproportionately small share of the benefits, at least in the short run, for example, by non-reciprocal economic openness, in order to be able to make the usually necessary side payments to smaller partner countries. This insight is derived from coalition theory as applied to states in an anarchic world system, which shows that it is in the interest of smaller partners to coalesce with a larger partner both in a legislative setting and in international politics mainly when the larger partner is willing and able to make side payments that make the sharing of the payoff disproportional. As Bruce Bueno de Mesquita puts it:

If the benefits derived from a winning coalition are distributed so as to preserve the initial relative distribution of resources among the winners, then the largest member

of the coalition must get the largest share of the benefits. Of course, the ratio of this actor's size to that of each of its partners remains constant. . . , but its absolute size moves closer to the system's definition of the size required to win. (Bueno de Mesquita 1975, pp. 9–10)

The argument essentially is that the largest partner, even when bearing and taking only a proportionate share of the costs and benefits respectively, is making a disproportionate quantum gain by its 'being enabled to cross an international size/power/status threshold that makes it a qualitatively more important international player'. That is, an effective Asian regional security organization would need to compensate the smaller and less secure countries more than proportionately in cost and benefit sharing for it to be in their interest to be in such a regional coalition, and for the same reason, it would be in the interest of the big country/countries in such a coalition to so compensate them. What needs to be analyzed are the kinds of cross-issue linkages and trade-offs, such as between economic and security issues, and foreign policy and domestic policy changes affecting international relations, that are involved in the role played by the largest states and the transactions between it and smaller states.

The incentives for regional economic cooperation—building for leading regional states could be analogous to that for global hegemony, from the perspective of hegemonic stability theory, for building global economic cooperation regimes, as neoliberal institutionalists, Robert Keohane and Joseph Nye, argue:

...stable economic regimes require leaderships—that is, willingness to forego short-term gains in bargaining in order to preserve the regime—and that an actor is most likely to provide such leadership when it sees itself as a major consumer of the long-term benefits produced by the regime. (Keohane and Nye 1977, p. 44)⁴

And further, 'When the hegemonial power does not seek to conquer other states, but merely to protect its favoured position, other states may benefit as well (Keohane and Nye 1977, pp. 44–45). This argument can be modified to apply to regional economic cooperation regimes in which there is a clear regional economic power whose relative global or extra-regional status would be boosted by leading a regional group and hence would have incentives to be 'generous' to smaller states as argued by Bueno de Mesquita.⁵

Scholars looking at successful cases of regional economic integration would argue that there are political prerequisites for successful economic integration leading to political integration. The most successful case is the European Union. The process of European integration began with the Schuman Plan (for the European Coal and Steel Community) presented in May 1950, the European Coal and Steel Community Treaty in 1951, ratified to bring it into effect in 1952. Helen Milner argues that,

The Schuman Plan called for countries and their firms to relinquish control of two vital economic sectors, coal and steel, to a supranational 'High Authority' (HA). Since

these sectors undergirded the rest of the economy and provided the means to make war, control over them was not just an economic issue... Once these sectors were integrated internationally, it was felt, war between these countries would never again be possible. (Milner 1997, p. 180)

The Treaty thus neutralized the Saar, Rhine and Ruhr border areas between France and Germany that produce coal and steel. Thus, the Treaty would constrain Germany. It should be noted, moreover, that this Treaty was preceded by the formation of NATO as a security umbrella under US leadership, the Warsaw Pact as a common threat and the Korean War as an ongoing regional hot war in the Cold War confrontation, in addition to which there was US pressure on both France and Germany to ratify the Treaty. Thus, the process of economic integration was built on political preconditions from its very inception rather than being an economic process bringing about security and political integration.

However, the opposite view that trade cooperation does not need prior political amity, merely a truce-like deterrent capacity, also has empirical substance. The 'cold politics but hot economics' scenario of East Asia since the 1980s, with trade booming between China, Taiwan, South Korea and Japan, and now Vietnam and the rest of ASEAN without any security pact and in fact with territorial and maritime disputes and competitive arming, indicates that an effective and well-understood deterrent capacity including guarantees by an outside power like the US, can be a substitute for a formal political or security agreement and that trade can flourish under such circumstances leading, perhaps, in the long term to reduced political differences and mutual stakes in each others' economies.

In the context of Asia, there is no clearly hegemonial power analogous to the United States in the North Atlantic or the Americas, that can play the role of a benevolent hegemon or nucleus of an Asian regionalism. Nor is there a common threat analogous to the perceived Soviet threat to the post-war West, nor a common political or economic ideology, or even a common cultural identity other than being non-Western, still less a common racial, ethnic or religious identity. Hence, these preconditions for regional political or security integration, quite apart from disputed borders and territories, do not exist, unlike in the case of post-war European integration or the formation of the Western alliance.

However, as the literature on the trade-security relationship shows, trade and security are closely inter-linked, and FTAs are used as an instrument to bolster diplomatic and security ties, or to embed security ties, in addition to being for trade promotion alone, particularly cross-regional FTAs or plurilateral FTAs involving significant powers. This is particularly so since the decade of the 1990s, due to what Aggarwal and Koo (2008) have called the triple shocks of the end of the Cold War, the Asian financial crisis of 1997, and the 9/11 shock to global security (Aggarwal and Koo 2008, p. 2). This has led to a search for regional, and sub-regional and cross-regional institution building in the form of both FTAs for trade integration and economic expansion but also politico-diplomatic and security institutionalization. This is a search for regional institutions that go

beyond the loosely structured US-centred hub-and-spokes system in place since the Cold War and are intended to mutually bolster both security cooperation and economic integration. As of 2014, this is a still nascent and evolving architecture, which is in a state of flux due to the rise and newly-assertive behaviour of China. The future depends on the interaction between Chinese behaviour and the US and Asian responses to it, both of which are unpredictable and evolving.

To sum up, Asian economic integration and the rise of China are both inter-related, and pose both opportunities and challenges for political and security integration. This is bound to be a long-term process but is vulnerable to being derailed by short-term opportunistic behaviour on the part of both major and minor actors.

Acknowledgements

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Notes

1. All figures from standard sources such as the IMF *Direction of Trade Statistics* and from individual country data, and www.asean.org statistics.
2. See Asian Development Bank's Asia Regional Integration Center database (www.aric.adb.org/fta) for these and other figures on bilateral and plurilateral FTAs in Asia.
3. See UNCTAD database on FDI (www.unctad.org/fdistatistics).
4. For hegemonic stability theory, see Krasner (1976). For a critical survey of hegemonic stability theories, disaggregating its strands, see Lake (1993).
5. Bueno de Mesquita (1975), Chapter 1, for a survey of power maximization theories of coalition politics which shows that it is in the interest of smaller partners to coalesce with a larger partner both in a legislative setting mainly when the larger partner is willing and able to make side payments that make the sharing of the payoff disproportional. The argument is essentially that the largest partner is only compensating for the disproportionate quantum gain that it is enabled to make either by enabling government formation or by enabling crossing of a political threshold that makes it a qualitatively more important player in the system.

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