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China's Economic Diplomacy in the 21st Century

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Abstract. The author takes on China's economic diplomacy, a key area of that country's foreign policy in the 21st century that includes economic rewards and coercion. She addresses, in particular, the measures Beijing is taking to make other countries heavily dependent on China. The author also discusses the significance of aid China offers in an effort to advance its foreign policy goals.

Keywords: *China, economic diplomacy, foreign aid, economic dependence, economic sanctions, China's foreign policy, "core interests."*

Economic diplomacy, a term generally understood as the use of a country's economic instruments and economic opportunities to promote its national interests and achieve its foreign policy objectives, has been playing a growing part in China's activities around the world since the onset of the 21st century. Used widely in Beijing's foreign policy behavior since Mao Zedong and Deng Xiaoping, economic diplomacy has acquired a new dimension since early in this century. The staggering financial and economic power China had built up at the turn of the 20th and 21st centuries has given its economic diplomacy a greater leverage on a much broader scale than ever before.

China's economic power is enormous in both hard figures and in comparison to the world's all other economies, and so is its involvement in international economic exchanges. China has the largest gold reserves put at \$3.8 trillion in 2013 and has been a solid second in overall GDP in the world since 2010. In the estimates of various experts, China has every chance of pulling ahead of the U.S. over the next ten to fifteen years, to become the world's biggest economy.

China placed ahead of the U.S. in total foreign trade three years ago, in 2012, when it registered \$3.87 trillion in foreign trade, billions of U.S. dollars more than America's \$3.82 trillion.¹ China now is a leading trading partner for over a hundred countries, some of which, like Russia, Brazil, Australia, India, and

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Kazakhstan, are big economies themselves. In 2013, China was the biggest trading partner for Japan, South Korea, Vietnam, Malaysia, Indonesia, Myanmar (Burma), Singapore, Thailand, and Mongolia in East Asia, the fastest-growing region of the world.²

Even though China's foreign trade is booming, its performance in the investment business is far less spectacular – it only ranks 15th in the world for total accrued foreign direct investments.³ Here too, though, a steady trend for fast growth in China's investments in the rest of the world has emerged. The buildup of Beijing's investments across the world has intensified significantly since sometime in 2004 and 2005 when it launched a government-sponsored "going out" strategy.⁴ The aid China is giving to developing countries has been growing fast, pushing it up, in some estimates, to sixth place in the rankings of the world's biggest aid donors in 2013.

These examples are all evidence of China's immense economic potential that keeps climbing up continuously and is used by its leaders more frequently to promote the country's national interests. In this way, economic diplomacy, in no way different from public diplomacy, is turning into an instrument of choice for Beijing to achieve its foreign policy goals.

Rewards for Other Countries and Their Growing Dependence on China

It has long been a custom to look at economic diplomacy from two different angles of the way in which economic power is used – economic reward (or carrot) and coercion or punishment (stick), most frequently meted out through economic sanctions. Its economic power as a way to project its influence across the world, Beijing prefers encouragement as a priority, rather than punishment. Encouragement can take a great variety of forms to invigorate trade with other countries (for example, by giving special first-priority treatment to its partner countries and placing large procurement orders with foreign suppliers for China's government needs), by making more investments in foreign projects, and increasing aid to other countries, including assistance to foreign countries launching major infrastructure projects. These and similar other measures contribute to stronger commercial and economic links and political relations with beneficiary countries and to China's more favorable international image. Economic sanctions are applied in response to a target country's intransigence and are sporadic and, as a rule, temporary (remaining in force until the desired effect on the target country has been achieved or until their rationale of the sanctions has been exhausted), while rewards are used consistently over a long timespan. Economic rewards are ultimately intended to make countries dependent increasingly more heavily on China, reinforce China's political influence on aid recipients, and eventually facilitate Beijing's efforts to pursue its national interests.

China's government gives a special role to free trade agreements with foreign countries as a factor stimulating trade with them, to the establishment of subregional and regional free trade areas, and to the initiation of programs on special trading preferential treatment. Beginning in 2003, when China first used preferential treatment agreements as an instrument of its trade policy, it has entered into bilateral preferential treatment agreements with eleven countries and territories – Hong Kong, Macau, Chile, Pakistan, New Zealand, Singapore, Peru, Costa Rica, Taiwan, Switzerland, and Iceland. Talks are now in progress on free trade agreements with South Korea, Australia, Norway, and Sri Lanka, and on multilateral agreements with Japan and South Korea and the Gulf Cooperation Council countries.

Free trade agreements on liberalization of trading terms promote trade and economic relations between China and its counterpart (or counterparts) and their greater reliance on one another. Where a country entering into a free trade agreement with Beijing runs a small-scale economy and conducts a significant part of its trade with China, it eventually falls into heavy economic dependence on China, rather than is its equal, and gives leverage to China to potentially influence its government decision-making.

Beijing enters into preferential treatment agreements on trade guided, above all, by its long-term strategic political interests, rather than by immediate economic gains. As a rule, China makes greater concessions in trade liberalization in free trade agreements than its counterparts.

A good example of how Beijing uses preferential treatment trade agreements to achieve its key political objectives is provided in the framework agreement on economic cooperation signed by China and Taiwan in June 2010 and put into effect in September of that same year. Under the agreement, a three-year Early Harvest program that went into effect on January 1, 2011, China undertook to lower its customs duties on 539 items of Taiwanese goods and services, eventually lifting them altogether, and Taipei reciprocated in kind on 268 items of Chinese goods. This latest agreement was a sequel to measures Beijing had been taking since 2008 to expand and diversify its commercial and economic relations with Taiwan and intensify the dependence, heavy as it already is, of the Taiwanese economy on China. Taiwan's biggest trading partner since 2003, China keeps on building up its trade with the island – Chinese statistics put the growth in trade between both shores of the Taiwan Strait within the range of \$145 billion in 2010 and \$197 billion in 2013.⁵ Chinese investments in Taiwan have been increasing as well.

The economic convergence between China and Taiwan that started off in 2008 has brought sizeable political gains to Beijing – there has been a visible change in Taipei's behavior over issues touching upon China's "core interests." In September 2009, for example, Taipei bowing to Chinese authorities' sensibilities refused to issue an entry visa to Rabia Kadir, an Uyгур human rights activist, pronouncing her to be a *persona non grata*. That same year, Taiwan's

President Ma Ying-jeou declined to meet the Dalai Lama *tête-à-tête* when Tibet's spiritual leader came on a visit to the island. In 2011, Zhonghua Telecom, Taiwan's leading telecommunications company, made public its hesitations over a contract with the New Tang Dynasty Asia Pacific channel beaming its programs to Continental China and the island that was controlled by the Falun Gong sect banned in China.⁶

Even though these elegant bows Taipei made to China struck a positive cord with the government in Beijing, China's economic pat on Taiwan's back hides a far more significant objective – reunification of both shores of the Taiwan Strait, a challenge four generations of Chinese leaders have labored to meet, with nothing yet to show for it. Given China's significant economic enlargement, tethering Taiwan's economy to that of China and developing the island's absolute and all-pervasive dependence on the mainland has turned into an obsessive idea of China's strategy of charming the island back into its embrace. The current Chinese leaders are staking on economic leverage, rather than coercion by force, in resolving their Taiwan problem.

While China has chosen entering into free trade agreements to be the best way to lure developed and moderately advanced developing countries into closer relationships, Beijing offers preferential treatment in trade with the least developed countries unilaterally to encourage their exports to flow to China.

In 2005, Beijing set out with lifting all duties from 190 categories of goods China imported from 25 least developed African countries to stimulate African exports. By July 2010, zero customs duties had been applied to over 4,700 items of African goods. Between 2005 and July 2010, \$1.32 billion in duty-free African goods had entered China.⁷ The Chinese authorities committed themselves to gradually raising the share of duty-free African goods to 95%.⁸

Speaking at the G20 summit in November 2011, China's President Hu Jintao announced plans to lift customs duties from 97% of the goods facing duties on entry into China's customs territory from the least developed countries having official diplomatic relations with China.⁹

In late November 2014, Beijing announced its intention to remove all customs duties from 97% of the duty-carrying goods imported to China from the least developed Pacific states as a way to intensify bilateral contacts and establish closer economic relations with those insular countries.¹⁰

It is mostly because of its preferential trade treatment that China has been consistently, since 2008, the biggest export market for the world's least developed countries that take 23% of all their exports to China.¹¹ Growing exports to China contributes to something of a boom in the economies of the least developed countries that put a high prize on Beijing's export promotional measures and China's image gets a brighter luster for them. On its part, Beijing does not suffer economic losses to speak of by giving preferential treatment to them in trade – Chinese goods do not suffer much competition from goods China imports from the least developed countries because of their small quantities as compared

to China's total foreign trade. In fact, at a small cost in efforts, China receives expanding international support among the least developed countries.

In the context of expanding trade and economic ties, and also its growing regional influence, Beijing attaches much significance to the establishment of subregional and regional free trade areas. On its first attempt, China joined the ASEAN free trade area (KAFTA) that eventually involved 11 countries with a population of almost 1.9 billion people. In November 2002, China and the Association of Southeast Asian Nations (ASEAN) entered into a framework agreement on comprehensive economic cooperation in a free trade area to be set up for ten years. The 2002 FTA agreement was followed by an agreement on trade in goods in 2004 and on trade in services in 2007. The KAFTA free trade area agreement that went into force on January 1, 2010 stimulated stronger commercial and economic relations between China and ASEAN countries and greater interdependence between them. The Chinese government's focused policy led to a significant growth in trade between China and ASEAN nations in gross figures and in China's share of ASEAN's foreign trade in general. Between 2003 and 2013, trade between China and ASEAN rose sixfold, from \$59.6 billion to \$350.5 billion, and China's share of the Association's trade with the rest of the world almost doubled, from 7.2% to 14%.¹² China has been invariably ASEAN's biggest trading partner since 2009 on the year by year count. Besides, China is the biggest market for ASEAN exports and just as important a source of imports. In geopolitical terms, the CAFTA free trade area has boosted China's weight in the Southeast Asia (SEA) and all Asia in general.¹³

Its CAFTA experience and its goal of having a Sinocentric economic integration model in East Asia (or the Asia-Pacific Region, in a broader sense) have given China an incentive to intensify efforts to set up a vast regional free trade area. The idea of getting together an Asian replica of the EU or NAFTA (North American Free Trade Area) was conceived in Beijing as two alternatives – a Regional Comprehensive Economic Partnership (RCEP) (ASEAN+6 format) or an APR free trade area. If put into practice, the idea would tag China as the “architect” of new institutions and a regional system of rules in trade and investment as a groundwork for a future regional economic system to be built on.

Lastly, modern China's economic diplomacy has a global dimension as well. In the backwash of the world financial and economic crisis in 2008 and 2009, the realignment of forces in the global economic system that pushed China up to a top player berth, Beijing has firmed up its international standing by playing a bigger role in the international financial system. China has joined hands with the leading BRICS (Brazil, Russia, India, China, and South Africa) developing countries in efforts to gain bigger quotas and voting weight in international financial institutions (the International Monetary Fund and World Bank) and institute new financial mechanisms (the currency reserve pool and a BRICS Development Bank) that give China a free hand in seeing about its own interests.¹⁴

Aid as Economic Carrot

Giving aid to countries in any part of the world is a powerful instrument of a donor country's foreign policy as a way to build up its political and economic leverage in beneficiary countries and regions across the globe. Aid helps fortify economic and political relations between donor and beneficiary, foster contacts between their ruling elites, impress the donor country's favorable image on the public mindsets in the aid recipient's society, and give a boost to the donor country's prestige in the international community.

Favorable conditions emerged for Beijing to begin giving aid to other countries to promote its foreign policy objectives in the late 1990s when China started registering impressive economic growth rates that yielded revenue surpluses its government could use to expand the scale of its aid and increase the number of its beneficiaries. Aid climbed up steeply since 2004 when China had amassed considerable financial resources it could afford to spend on aid to other countries. Between 2004 and 2009, aid was growing at an average rate of up to 29.4% a year.¹⁵ From that time on, China had joined the ranks of the world's most generous donors, and stayed on there since. In the estimates of the Japan International Cooperation Agency's Research Institute (JICA Research Institute), China rose from 16th to 6th position in the rankings of the world's biggest aid donors between 2001 and 2013, only behind the U.S., the United Kingdom, Germany, Japan, and France.¹⁶ Beijing gave around \$7.1 billion in aid in 2013 alone.¹⁷

By 2010, Beijing had reassessed the role of aid and rated it definitely as a major instrument of economic diplomacy and a priority in foreign policy. Evidence of this about-face was provided at the first-ever national conference convened by China's Government in August 2010 to discuss aid donation, assess China's experience in aid delivery, and lay down ways of improving aid efficiency. In 2011, the first specialized White Paper in China's history to be published on foreign aid retraced the history of aid provided by China since 1949 and gave details of aid provided in 2004 to 2009. Three years later, in 2014, a second White Paper came out with a summary of China's projects to provide aid to other countries around the world in the years 2010 to 2012.

Publication of details of the China's aid to foreign countries, previously a closed book to outsiders and a source of rumors among experts and in the media of Western countries, was demonstration of the Chinese Government's intent to seek international legitimization and institutionalization of Beijing's aid and China's closer integration into today's international system. China now portrayed its aid to other countries as its responsibility of a great power ready to give a helping hand to developing and least developed countries. With the spotlights of criticism turned on it by Western countries over the last decade for its alleged "irresponsible" behavior on the world scene matching up uncomfortably to its great power status, the White Papers were an occasion for China to show its rising international responsibility. It scaled up assistance to developing countries

along the South-South axis of cooperation. Over three years, 2010 to 2012, Beijing gave \$14.41 billion in aid to 121 countries – 51 in Africa, 30 in Asia, 19 in Latin America, 12 in Europe, and nine in Oceania.¹⁸ Its biggest beneficiaries, Africa and Asia, received 51.8% and 30.5% of the total, respectively. By providing aid to Africa and Asia, Beijing uses this opportunity to spread its influence and promote its national interests in these regions.

For the most part, China offers its aid under bilateral agreements in three preferred forms: grants and interest-free and cut-rate loans (soft loans). At 55.7% of total aid in 2010 to 2012, soft loans appear to be given preference over the other forms of aid and are issued by China's Export-Import Bank (Eximbank) to borrowers on the best possible terms, at 2% to 3% per annum for a period of 15 to 20 years. Typically, soft loans are given for financing large and medium-sized industrial and infrastructure projects and purchasing machinery and electronic equipment and materials, such as, for example, development of transportation infrastructure (railroads, highways, seaports, underground railroads, airports, canals, and bridges, among others), telecommunications systems, improvements in electric power supplies (construction of hydroelectric and thermoelectric power plants), construction of oil refineries, laying of oil pipelines, and the like. Not infrequently, soft loans go to countries that cannot, or just do not want to, turn to the World Bank or the IMF because of their uneasy relationships with the West.

Grants that claimed 36.2% of all aid provided by China in the years 2010 to 2012 are given to be invested into small and medium-scale social services projects, finance cooperation projects to develop human resources, technological cooperation, and financial and humanitarian assistance. Grants can take the form of debt write-offs as well.

Interest-free loans account for the smallest share (8.1% only in 2010 to 2012) of China's aid and are given primarily to developing countries moderately well off in economic terms for the construction of social services institutions and projects designed to improve the quality of life. Loans in this category are issued for a 20-year period and drawn down over the first five years; the next five years are considered a repayment holiday, and the loan is repaid in the remaining ten years.

Completion of infrastructure projects takes central place in China's approach to aid it gives to other countries. In 2010 to 2012, 44.8% of China's aid went to contribute to the development of economic infrastructure, 27.6% to social and general-purpose infrastructure, 15% given in goods and materials, 5.8% to cooperation in the development of human resources, 3.6% and 2% to assistance in promotion of manufacturing and farming, respectively, and 0.4% to humanitarian aid.¹⁹

China's preoccupation with infrastructure projects is explained by several circumstances.

- First, developed infrastructure already in place, a situation atypical of the majority of developing countries, facilitates China's economic penetra-

tion into target regions. Construction of transportation logistics contributes, among other purposes, to the expansion of trade between China and its partner countries, while improvements in the mining infrastructure facilitates development of natural resources that are eventually exported to China.

- Second, completion of infrastructure projects helps China to project a favorable image of itself in the minds of the population of target countries and regions. In fact, China completes projects having a vital part in improving the local population's living conditions, such as water supplies, electric power, inexpensive housing, and better healthcare, education, and leisure opportunities. Nor can locals remain cool to major cultural and sports facilities going up with China's direct and most significant involvement.
- Third, infrastructure projects are favored by local elites who tend to prefer Beijing over other bidders, for example, in developing and mining natural resources. Construction of government office buildings (residences of top executives, ministerial offices, national parliaments or congresses, and so on) is an equally important factor for contacts to be maintained with local political elites.
- Fourth, infrastructure projects China undertakes abroad help it address vital socioeconomic problems at home as well. China only gives soft loans to other countries' borrowers on three conditions of no minor importance – the China-subsidized projects must be contracted to a Chinese company only, a majority of workmen have to come from China, and at least a half of materials and equipment must be purchased from China. Insistence on all these three conditions being met helps China give jobs to members of its own population, enable its indigenous companies to gain practical experience in building large-scale infrastructure projects abroad, clear the way for its manufacturers to enter international markets, and stimulates the flow of Chinese exports to the loan beneficiaries.

No political conditions set for aid beneficiaries, noninterference in their internal affairs, and respect for their free choice of development models and options are the basic principles on which China gives aid to other countries.²⁰ Even though China draws a dividing line between itself and Western countries and does not expect the beneficiary countries to conduct democratic reforms and build a decent government system, which are the staple demands made by Western countries on their aid beneficiaries, Beijing makes its aid contingent on another kind of political conditions. China gives or refuses to provide aid to aid applicants depending on the recipients' policies and attitudes toward China's "painful" problems – Taiwan, Tibet, and the Uyghurs. When, for example, Vietnam ignored China's request for Taiwan to be struck from the list of APEC summit participants in Hanoi in 2006, the Chinese authorities suspended aid to Viet-

nam, even if temporarily.²¹ And the other way around, after the Cambodian authorities deported, in December 2009, twenty Uyghurs who had found refuge in Cambodia on fleeing the Xinjiang Uyghur Autonomous Region in the wake of ethnic clashes in the region earlier in July of the same year, Beijing announced its intention to invest \$1.2 billion in Cambodia's infrastructure.²² By early 2012, Beijing raised its commitments to provide aid to Cambodia to \$2.7 billion in grants and soft loans, as probably a reward to Phnom Penh, the ASEAN chairman at the time, for its decision at the ASEAN summit in July 2012 to block passage of a joint statement censuring China for its behavior in the territorial disputes involving it in the South China Sea.²³

Aid and parading of the economic bonanza due for befriending China have proved to be an effective way for Beijing to cut down on international recognition of Taiwan. China considers its province, one among many. Between the late 1990s and 2008, China's "dollar diplomacy" coaxed many countries' diplomatic recognition away from Taiwan to the People's Republic,²⁴ starting with the Bahamas in 1997, followed by Nauru in 2002, Liberia in 2003, Dominica in 2004, Vanuatu in 2004, Grenada in 2005, Senegal in 2005, Chad in 2006, Costa Rica in 2007, and Malawi in 2008. The break in diplomatic relations with Taiwan carried a price China paid in considerable aid, and some of the turncoats were rewarded with special "prizes" – gyms or stadiums China built for them. Not so the deserters from China's cause, like Kiribati that switched its diplomatic allegiance from China to Taiwan in 2003 and had the flow of Chinese aid cut off, the China-built satellite tracking station dismantled, and construction of a stadium discontinued.

Aid has been China's major foreign policy tool kit since the early 21st century. By analogy with leading Western countries, it has used it frequently to promote its national interests and exercise its influence on the beneficiary countries on issues vital to Beijing. There is an unmistakable feedback between aid delivery by Beijing and the aid beneficiaries' delivery on a set of unwritten, and unspoken, rules – aid is a reward and no aid, punishment.

Economic Punishment and Coercion

While encouragement is the principal tool of modern China's economic diplomacy, various forms of punishment and coercion are used in a variety of ways where a pat on the back does not work, primarily where harm is caused to China's "core interests" – state sovereignty, national security, territorial integrity, the country's unity, the political system anchored in China's Constitution, social stability, and sustainable socioeconomic development, we are to gather.²⁵ This group of interests can, with dead certainty, also include the Taiwan, Uyghur, and Tibet problems, and the whole lot of territorial disputes China has yet to settle with its neighbors (particularly with Japan in the East China Sea and several

Southeast Asian countries in the South China Sea, and with India as well). Other countries showing no respect for China's interests are viewed as a direct threat to it and provoke a response by every kind of deterrence and pressure applied against them. After Xi Jinping entered the top government office, the term "red line" has become firmly embedded in the Chinese officialese in the sense that China will not stand encroachments upon its "core interests." Anything that China regards as challenge to its "core interests" can trigger imposition of economic sanctions against the abuser.

China applies sanctions unilaterally, without calling upon any other members of the world community to intercede, by doing what its top-ranking government officials tell it must do. As an example, when Nur Bekri, chairman of the People's Government in the Xinjiang Uygur Autonomous Region, went on record telling about close contacts between the Uygur terrorists and Pakistan, China withdrew its offer to finance construction of a gas pipeline between Iran and Pakistan.²⁶

Any criticisms made in the Chinese top-ranking officials' statements can sound as an indirect warning, even if its message is read distinctly between the lines, of the possibility of China invoking "punitive" measures. Beijing is not prone to publicize its intention to impose sanctions. A direct threat of the possibility of punitive measures being taken is an exception rather than the rule in official statements. This practice gives greater flexibility to the Chinese government in having its will in economic coercion and a possibility of lifting the sanctions already in force without loss of face even where coercion loses its bite. Like it did in an episode played out in early 2010. As its response to Washington's plans to sell a large quantity of weapons to Taiwan, Beijing threatened to take an unprecedented step of slapping sanctions on American companies having a hand in arms deliveries to Taiwan. Even though the U.S. shrugged off Beijing's threat, China backed off from imposing sanctions on the American military-industrial complex, much to the Chinese government leaders' discomfiture.

Beijing's recourse to economic coercion is motivated by several circumstances.

- First comes its desire to signal its displeasure with a foreign government's stand on an issue of much concern to China, to induce it to change its stand or to give assurances of minding its steps in the future.
- Second, coercion is an instructive lesson to other countries and demonstration of the potential negative consequences of anything they do harming China's "core interests."
- And third, coercion carries a domestic political subtext as the Chinese government's resolve to act decisively to uphold China's national interests against nationalism rearing its head in China today.²⁷

Chinese sanctions can take the form of a freeze of large-scale projects scheduled or already in development by Chinese companies in uncooperative coun-

tries, temporary suspension of the aid flow, cutback on investment, restriction of imports of handpicked goods to, or their exports from, China, suspension of trade talks and exchanges of trade delegations, and suspension or abandonment of government procurement orders placed in uncooperative countries, the list of sanctions could go on and on.

Experts frequently refer to the inefficiency of sanctions as a way to put pressure on other countries' governments to force them into compliance. They are not right on every point, though. Indeed, where sanctions are limited in scale, moderate in time and coverage, and do not lead to antagonisms arising between the countries in conflict, sanctions can prove to be effective enough. Besides, they are an illustration of the unfavorable effect of what other countries do or fail to do. As a lesson to learn, there is no denying the efficiency of sanctions, even if they are not intended to kill.

Beijing's sanctions proved to be effective when they were imposed on Norway that fell into disfavor with Beijing in 2010 following the award of the Nobel Peace Prize to Liu Xiaobo, a Chinese human rights activist who had been sentenced to a prison term by Chinese courts a year earlier for his calls for the overthrow of China's government. Beijing suspended its attendance of the ongoing talks on the establishment of a free trade area that Oslo wanted to be completed successfully. On the pretext of toughening its veterinary inspection rules, Beijing put restrictions on the import of Norwegian salmon at a cost of tangible losses to Norwegian exporters who had looked forward to an expansion of their presence on the fast-growing salmon market in China. Norwegian salmon imports plunged 60% in 2011, and two years hence, in 2013, Norway lost its 92% monopoly on China's salmon imports, to share the salmon market in China with the United Kingdom and the Faroe Islands, Denmark, in an approximately equal measure.

By 2013, the downturn in Norway's relations with China had, for the most part, been reversed through Norway's efforts. As a goodwill gesture, Norway supported China's nomination for an observer status on the Arctic Council. Mindful of the lesson it had been given over the Nobel Prize, Norway's government, anticipating Beijing's likely reaction, declined the Dalai Lama's request for a private meeting with the Norwegian prime minister in spring 2014. It also got its lights from a precedent – back in 2008, French President Nicolas Sarkozy's (2007-2012) intention to meet the Dalai Lama prompted China into walking out of the talks over the purchase of 150 airliners from the Airbus concern. In a lash-out at the United Kingdom, Beijing put political contacts with that country in a deep freeze for 14 months after its Prime Minister David Cameron met the Tibetan spiritual leader in May 2012.

Over the last five years, China has used economic coercion consistently against countries having serious territorial differences with it. In 2009, it attempted to block a loan the Asian Bank wanted to give to India. China claimed that some of the loan funds (\$60 million out of \$2.9 billion) were intended for the

realization of irrigation projects in the Indian state of Arunachal Pradesh in which some areas are claimed by Beijing. The best bargain China could get, though, was postponement of loan disbursement, rather than refusal, because India's loan application was voted for by the U.S., Japan, and South Korea.

The weight of Beijing's economic pressure fell in full measure on Japan, after the two countries' territorial disputes in the East China Sea flared up with renewed force in 2010. Following the collision of a Japanese and a Chinese vessels off the disputed Diaoyudao (Senkaku) Islands on September 7, 2010, Beijing cut off its export of rare earth elements to Japan. A month later, restrictions were introduced on the export of these elements to Japan's close partners – the U.S. and Europe. Home of up to 36% of the world resources of rare earth elements and exporter of 97% of their world total,²⁸ China was certain it could use its monopoly on rare earth exports as effective leverage.

A new round of sanctions against Japan began in September 2012, when Tokyo announced its decision to buy three out of the five Senkaku Islands from their Japanese private owners, triggering a protracted major crisis in relations between China and Japan. Within days of the onset of the crisis, the Chinese public took on a leading role in forcing the government's hand in applying economic pressure on Japan by committing acts of violence against Japanese companies' offices and restaurants in China and boycotting Japanese goods. Public violence cut down the sales of Japanese cars (by between 35% and 63%), car components and spares, and electronic goods, among the Japanese goods affected most.²⁹ Several Japanese enterprises, for example Toyota, Sony, Canon, and Panasonic, had to suspend their operations in China, if only for a short period. Japanese airlines and the Japanese travel industry were suffering tremendous losses because the influx of Chinese tourists thinned out dramatically, down from around 20% of the total number of foreign tourists in Japan in the years before the latest crisis. Chinese travel companies got a hint to cancel all tours to Japan between October 1 and 7, the peak of the Chinese foreign travel period. Customs toughened, with the government's authorization, their clearance inspections of goods imported from Japan, and delays were regular occurrences in working visa confirmations for Japanese nationals everywhere. The Japanese economy suffered a significant cumulative effect of Chinese sanctions, even though the restrictive measures remained in force for only a limited period of time.

To summarize, the effect of Beijing's economic sanctions is definitely contingent upon the size of the subject country's economy and the measure of its dependence on China. Countries whose economic potential is significantly inferior to China's and whose dependence on China's aid, investments, and trade with China are great will be more vulnerable than otherwise to Beijing's economic pressure and political influence. Beijing is, therefore, exerting itself all out to expand its economic presence in countries and regions around the world and make them still more dependent economically on China.

China's Economic Diplomacy in the Context of Territorial Disputes in the South China Sea

Economic diplomacy is given a high priority in Beijing's plans to press its territorial claims in the South China Sea where China is in dispute over the sovereignty to Spratly Islands (Chinese name is Nansha) and the Paracel Islands (Chinese name Xisha), and almost 80% of the sea surface area. Vietnam and Taiwan, too, have been embroiled in the dispute over the Paracel Islands for several decades already, and the Spratly Islands, too, have several other claimants – Vietnam, Taiwan, the Philippines, Malaysia, and Brunei Darussalam.³⁰

Major changes started happening in Beijing's behavior in the territorial disputes in the South China Sea in 2007 and 2008, when its awareness of its strong muscle to project its power and influence made its more assertive. The policy of good-neighborliness, reliance on "soft" tactics used to build up China's policy in Southeast Asia, and restraints in asserting its claims to disputed territories Beijing used in the preceding decade of 1997 to 2007 gave way to a go-getting foreign policy of more insistent efforts to enforce its territorial claims in the South China Sea. What is more, Beijing's steps were not limited to demonstrations and administrative measures, like publication of plans to develop recreation travel to the disputed Paracel Islands or institution of a new administrative unit, a county center of Sansha exercising jurisdiction over three groups of islands (the Paracel and Spratly, and the Macclesfield Shoal), or the issue of new Chinese passports with a map showing the disputed islands as Chinese territory. This time, it went on beyond demonstrations and publications to expand its military presence in the South China Sea.

To put pressure on countries questioning Beijing's claims to the disputed islands, China used its enormous economic presence in Southeast Asia to resort to economic coercion or punishment. This statement is illustrated most dramatically by the episode that cropped up in spring 2012 when Philippine warships interfering with Chinese fishing boats going about their trade off the Huanyan Island led to a month-long standoff between Chinese and Philippine naval vessels in the area. To back up its demand for withdrawal of the Philippine warships from the disputed area, China stepped up its pressure on Manila by toughening customs controls over fruit imports from the Philippines and called on its nationals to refrain from traveling to the Philippines.³¹ A large share of its revenue coming from fruit trade and the travel industry, both looking to China as their biggest customer, China's restrictions could leave a deep dint in the Philippine economy.

The Philippine pattern was replicated in summer 2014 when, after a stand-off lasting from May to mid-July over the siting of a Chinese oil rig in the disputed areas of the South China Sea, Beijing imposed restrictions of the import of several fruit species (in particular, bananas and pitahaya) from Vietnam, causing significant losses to Vietnamese farmers who sent around 35% of their exports of

fruits and vegetables to China. In the estimates of Vietnam Center for Economic and Policy Research, curtailment of trade between Vietnam and China because of the territorial differences between them coming to a head could reduce Vietnam's annual economic growth rates to between 4.15% and 4.88% in 2014, from 5.42% in 2013.³²

Beijing continues to use economic coercion on a limited scale. Today, though, it gives a high priority to making Southeast Asian countries heavily dependent on China in economic terms and on its economic rewards to reinforce its arguments in territorial disputes.

Against the background of growing differences in territorial disputes, the new crop of Chinese leaders under Xi Jinping initiated a series of measures in 2013 to refresh good relations with its neighbors, spread its influence, and refurbish its image in Southeast Asia. Guided by its desire to harmonize its relations with its neighbors, Beijing intensified its diplomatic efforts in 2013, gave more muscle to its economic diplomacy, and put many profitable projects on the table for the region's countries to study.

In October 2013, the Chinese delegation met with APEC leaders and attended the East Asia Summit to advance several initiatives in trade and infrastructure development in the region. Xi Jinping called for establishment of an Asian Infrastructure Investment Bank and announced the Chinese authorities' plans to boost China's trade with ASEAN to \$1 trillion by 2020 from \$400 billion in 2013.³³ In his unprecedented addresses to the parliaments in Thailand and Indonesia, Xi Jinping unveiled Beijing's strategic concept for a China-ASEAN community of common destiny and a project for a Maritime Silk Road for the 21st Century, including construction of seaports and development of sea traffic between China and countries in Southeast Asia and the Indian Ocean. In May 2014, Beijing put forward an idea of opening an economic corridor from Bangladesh to China, India, and Myanmar (Burma) by building transportation infrastructure projects, stepping up investment, and expanding trade and humanitarian cooperation.

Beginning in 2013, Beijing has been directing concerted efforts into expanding its diplomatic and economic presence in Southeast Asia – its high-ranking envoys have been traveling to the region's countries to convey Beijing's promises to increase the scale of trade and investments and offers of entering into more contacts and helping them to complete large-scale projects, for the most part, with China's funding. Plans are drawn up and polished up before they go out to fortify links between China and ASEAN and increase the Southeast Asian countries' dependence on China.

An important point to make here is that China does not relax its ambitious policy in pressing its territorial claims in the South China Sea. Unlike it used to be, China's foreign policy today combines two approaches to its relations with neighboring countries – luring them into large-scale economic cooperation and, at the same time, turning its screws tighter in territorial disputes with them. This double-track approach is aimed at making Southeast Asian countries dependent –

heavily, consistently, and thoroughly – on China and forcing them to think twice before they set on course for confrontation in territorial disputes with Beijing.

* * *

To end on this note, China has been using economic diplomacy in its foreign policy in an increasingly larger number of situations since the start of the 21st century. More preferable than the use of military force, it helps China to look after its national interests in a relatively calm way, avoiding provoking confrontation and, particularly important, getting the “Chinese threat” humbug off many people’s minds around the world. This reason is also a fitting explanation why China’s economic diplomacy is mostly about encouragement or reward. It uses economic coercion but relatively rarely for fear that this way of having its will might frequently spatter its international image and get the defiant countries to thinking about ways to reduce their economic or any other dependence on China. It might be assumed then that until China has built up its overall national power much superior to the world’s other countries and rallied a group of nations under its banner as its allies, rain or shine, it will not practice economic coercion on a wide scale. It will continue to be used some more time, and only where harm is done to China’s “core interests.” Meanwhile, China will be putting on financial and economic muscle, expanding its economic presence in many countries and regions of the world, adding weight to its role in the international financial and economic system, and spinning a web of economic dependence with lavish aid, investments, construction of major infrastructure projects, and other forms of temptation for countries anywhere in the world to drop into.

NOTES:

1. China Statistical Yearbook 2013. URL: <http://www.stats.gov.cn/tjsj/ndsj/2013/indexeh.htm>; TradeStats Express. URL: <http://tse.export.gov/TSE/ChartDisplay.aspx>
2. European Commission Trade. URL: <http://ec.europa.eu/trade/>
3. CIA World Factbook. URL: <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2199rank.html>
4. The “going out” (*zou chuqu*) strategy was framed in the latter half of the 1990s and was embedded officially in the 10th five-year plan in 2001. It comprises a series of measures to be taken to encourage China’s involvement in international economic cooperation. For example, these measures included government support for Chinese companies that wanted to make investments in other countries, incentives for investments in industries of top priority to Beijing, and enactment of laws to match. For several years immediately following the adoption of this strategy, however, no significant increase in Chinese investments in other countries was registered. Following this lackluster start, the “going out” strategy first showed efficiency in the years 2004 and 2005 after the People’s Bank of China had accumulated significant reserves and Chinese state-controlled corporations were given an opportunity to carry out major investment projects abroad.

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12. ASEAN trade by selected partner country/region, 2013. URL: http://www.asean.org/images/resources/Statistics/2014/ExternalTradeStatistics/Aug/table19_asof24Jul14.pdf; ASEAN Stats. URL: <http://aseanstats.asean.org/>
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14. Ya.V. Leksyutina, "Kitai v BRIKS: motivatsiya uchastiya [China in BRICS: Motivation for Joining]," *Mezhdunarodniye otnosheniya*, # 4, 2014, pp. 83-86.
15. *White Paper "China's Foreign Aid*," April 2011. URL: <http://www.scio.gov.cn/zxbd/wz/201104/t896900.htm>
16. Naohiro Kitano, Yukinori Harada, "Estimating China's Foreign Aid 2001-2013," Japan, 2014, p. 17.
17. *Ibid.*, p. 16.
18. *White Paper "China's Foreign Aid (2014)." Op. cit.*
19. *Ibid.*
20. *Ibid.*
21. Lum Th., "Comparing Global Influence: China's and U.S. Diplomacy, Foreign Aid, Trade, and Investment in the Developing World," August 15, 2008, p. 86. URL: www.fas.org/sgp/crs/row/RL34620.pdf
22. "Beijing's Moneyed Advance on Southeast Asia," CBCNews, March 8, 2010. URL: <http://www.cbc.ca/news/world/story/2010/03/05/f-china-economic-muscle.html>
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24. Significantly, from the time Beijing started repairing fences with Taipei and entered into an implicit agreement with it in 2008 on "a diplomatic lull," implying abandonment of the "dollar diplomacy" and rivalry for recognition, China has scaled down its efforts to win over new diplomatic partners. Rumor had it that China went as far as declining baits for establishment of official relations initiated in 2008 by Panama, Paraguay, and Guatemala (Wang T.Y., Lee Wei-Chin, Yu Ching-Hsin, "Taiwan's Expansion of International Space: Opportunities and Chal-

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