

REGIONAL COOPERATION IN EAST ASIA:  
ITS NEEDS AND CHALLENGES

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## **Abstract**

This paper analyzes the ongoing development of regionalism in greater East Asian region. Since the late 1990s, there has been much progress on forming an East Asian Community. The author argues that the 1997 East Asian Financial Crisis was a crucial point in this process, providing a strong sense of “We-ness” in East Asia. Many Asian nations felt abandoned by the U.S. at that time, and they decided to come together to hedge against further financial security risks. The economic and political rationale behind creating this regional community is clear. The concept of East Asian Community can both stimulate economic prosperity and maintain peace in East Asia especially as the People’s Republic of China becomes a regional hegemony.

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### *Caveat*

East Asia's particular geographical composition has been highly contested. No single map of East Asia is inherently self-evident as to preclude other equally plausible options. The term is highly fluid and it is subject to redefinition and reconfiguration. Different geographical groupings are used to advance or hinder specific political goals. *In this paper, I employ the term "East Asia" to be composed of the nation-states of Northeast and Southeast Asia – China, Japan, North and South Korea, Taiwan, and the ten ASEAN member states (Myanmar, Vietnam, Cambodia, Laos, Brunei, Malaysia, Thailand, the Philippines, Indonesia, and Singapore).* This configuration of the region illuminates certain amount of ongoing economic cooperation as the technology, capital-rich Northeast Asia cooperates with labor-rich and capital-poor Southeast Asia. Such a definition of the region also finds an institutional form under the ASEAN+3 formulation.

### *List of Acronyms*

ACU	Asian Currency Unit
AIIB	Asian Infrastructure Investment Bank
APEC	Asia-Pacific Economic Cooperation (APEC)
APT	ASEAN plus three (ten ASEAN members plus China, Japan, and South Korea), also identified as “ASEAN+3”
ASEAN	Association of South East Asian Nations (Indonesia, Malaysia, the Philippines, Singapore, Thailand, Brunei, Burma (Myanmar), Cambodia, Laos, and Vietnam)
BSA	Bilateral Swap Agreements
CMI	Chiang Mai Initiative
DPJ	Democratic Party of Japan
DPRK	Democratic People’s Republic of Korea (North Korea)
EAC	East Asian Community
EAS	East Asian Summit
EAEC	East Asian Economic Caucus
EAEG	East Asian Economic Grouping
EAFTA	East Asian Free Trade Agreement
EASG	East Asia Study Group
EAVG	East Asia Vision Group
EMEAP	Executives’ Meeting of East Asia Pacific Central Banks
ERPD	Economic Review and Policy Dialogue of ASEAN plus Three
EU	European Union
FTA	Free Trade Agreement

G-7	Group of seven industrialized nations (Canada, France, Germany, Italy, the U.S., Japan, United Kingdom)
GATT	General Agreement on Tariffs and Trade
GNP	Gross National Product
IMF	International Monetary Fund
NAFTA	North American Free Trade Agreement
NEAT	Network of East Asian Think Tanks
UN	United Nations
WTO	World Trade Organization

## 1. Introduction

### 1.1. East Asian Regionalism under the framework of ASEAN+3

*“We recognize the bright prospects for enhanced interaction and closer linkages in East Asia and the fact that this growing interaction has helped increase opportunities for cooperation and collaboration with each other.”*

Joint statement by the leaders of South East Asian countries, China, Japan and South Korea,  
Nov. 28, 1999 - Manila, Philippines.

A Korean scholar, An Jung-geun, already envisioned the concept of an East Asian Community actively pursued by the ASEAN+3 forum exactly 100 years ago from 2010. In 1910, An was executed by the Japanese colonial authority for the crime of assassinating the first Prime Minister of Japan, Ito Hirobumi. As a Korean independence activist, he decided to kill the main political figure behind forcing Korea's submission as a protectorate of Imperial Japan via the Eulsa Treaty. Above all things, An was also a pan-Asianist who envisioned the collaboration among China, Korea, and Japan to repel the European colonialism rampant in Asia at that time. Until his death in March 26, 1910, An worked hard on theorizing a model for Pan-Asianism in his essay, “On Peace in East Asia.” In recent years, there have been multiple events both in Korea and Japan in anticipation of the upcoming centenary of his martyrdom. Kim young-ho, the director of the International East Asian Community Scholarly Association, spoke about An to five hundred Japanese influential figures gathered at the Asahi Shimbun's conference hall in Tokyo:

“I want to introduce An Jung-geun not as a hero of the Korean independence movement but as a East Asian pacifist, or rather, the ‘Jean Monet,’ the father of European integration, of the construction of an East Asian community.”<sup>1</sup>

According to Kim, An Jung-geun’s proposal for East Asian peaceful cooperation was groundbreaking, as it possessed a comprehensive model for peaceful regional cooperation some 70 years before the creation of the European Communities. Some of his ideas were so revolutionary to the extent that they still have currency in contemporary East Asia. His ideas were: making Ryojun neutral, as it was internationally disputed territory; establishing Asian Peace Conference’s headquarters in that disputed territory of Ryojun; building a joint security regime operated by a joint peace force after disbanding the national armies; cooperating with each other towards common industrial development; issuing a common currency through a regional development bank. The latter two ideas ultimately became an early form of the initiatives currently under discussion today, including an Asian Monetary Fund and an Asian Currency Unit.<sup>2</sup> An’s vision of the Asian Peace Conference is especially interesting. He proposed the conference to be organized and led by regular citizens, not government representatives, of Korea, China, Japan, and the nations of Southeast Asia. He emphasized that citizen participation in the movement towards regionalism can help distinguish between states and their peoples, which can eventually benefit everyone in the region not just the political figureheads.

The international balance of economic power is increasingly shifting towards Asia, the home of one-third of the world’s population and one-fifth of its gross domestic product (GDP).

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<sup>1</sup> The Hankyoreh Newspaper, “East Asian Community and An Jung-geun,” editorial, March 25, 2008, translated from Korean. <<http://hanireporter.co.kr/arti/opinion/column/277994.html>>

<sup>2</sup> Ibid.

Impressive growth rates registered by China, India, and South East Asian countries along with rapidly increasing intra-regional trade and foreign direct investment (FDI) show that a historic transfer of power is taking place.

According to a 2008 IMF report, intra-regional trade within emerging Asia increased by 8½ times between 1990 and 2006 while trade volume in the rest of the world roughly tripled.<sup>3</sup> As a result, trade between the economies in emerging Asia has risen steadily from about 30 percent of total exports by the region in 1990 to more than 40 percent in 2006. It was the Plaza Accord of 1985 that stimulated a strong wave of intra-regional investment and trade in East Asia.<sup>4</sup> Facing huge appreciation of yen, Japanese firms led the way to set up extensive and sophisticated production facilities in Southeast Asia (later in newly industrialized economies such as South Korea and Taiwan) to reduce input costs and remain competitive in the market. Multinational corporations based on other countries also started to break their processing facilities into different parts of Asia according to available national factor proportions and technological capabilities.<sup>5</sup> This business scheme generated a dense web of intraregional trade networks in manufacturing and banking sectors across East Asia, enhancing the bottom-up connectedness among the regional economies.

Since late 1990s, there has been a surge of governmental force to further this de facto economic integration induced by “markets..., private trade and investment flows, and the policies and decision of companies.”<sup>6</sup> Why in that period? I argue that shared concern among East Asian states reached a new level in the aftermath of the 1997 Asian Financial Crisis. The

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<sup>3</sup> Gruenwald, Paul and Hori, Masahiro, “Intra-regional Trade Key to Asia's Export Boom,” *IMF Survey Magazine*, IMF Asia-Pacific Department, February 6, 2008, accessed via <http://imf.org/external/pubs/ft/survey/so/2008/CAR02608A.htm>.

<sup>4</sup> East Asia refers to Northeast Asia and Southeast Asia.

<sup>5</sup> Gill, Indermit Singh, and Huang, Yukon. And Kharas, Homi J., and Qun Bandhmuniratn. And World Bank and Institute of Policy Studies (Singapore) *East Asian visions: perspectives on economic development*, 2007, p. 32

<sup>6</sup> T.J. Pempel, Editor, *Remapping of East Asia: The construction of a region*, Cornell University Press, Ithaca, NY (2005), pp. 19.

financial crisis constituted a “turning point” in elevating East Asian regionalism to a new level as countries realized the need for regional economic collaboration to provide financial security for crisis prevention, management, and recovery. The 1997 crisis was the perfect apparatus in taking a big step towards institutionalizing the dream of “East Asian community.” In November 1999, the ASEAN +3 (China, Japan, and Korea) Summit released the Joint Statement on East Asian Cooperation that outlined a wide range of possible areas for regional cooperation.

The abovementioned 1999 joint declaration by thirteen Asian leaders was a groundbreaking agreement to accelerate the development of an organization promoting political, economic and cultural cooperation in East Asia under the framework of the ASEAN +3 (APT) – composed of ten member states of Association of South East Asian Nations plus China, Japan, and South Korea. Unlike the existing de facto international arrangements for integration such as the Asia-Pacific Economic Cooperation (APEC), APT is special for its concentration in East Asian affair functioning outside the umbrella of the U.S. military power and political leadership. It is also the most ambitious and comprehensive of the governmental efforts to establish an institutional framework that could help further the on-the-ground economic network in the region and cope with future crisis similar to the 1997 Asian Financial crisis. The negotiation of financial and trade policies is currently on the regional agenda. As of now, the ASEAN+3 is seen as “the most active regional grouping outside Europe, boasting an institutional structure increasingly akin to G7 and already more sophisticated than NAFTA.”<sup>7</sup> High-level political support shown by various summits along with step-by-step procedure with far-reaching ambitions, make the initiative to have “the potential to become the dominant regional institution in East Asia”<sup>8</sup> APT functions as a series of meetings at three levels: the first involving the heads of government; the

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<sup>7</sup> Zhang, Yumei, *Pacific Asia: the politics of development*, Routledge, New York: 2002, pp. 142.

<sup>8</sup> “Between Regionalism and Regionalization,” in *Remapping of East Asia: The construction of a region*, 2005, pp. 201

second involving ministerial-level meetings of economic and finance ministers; the third involves senior officials from ministries and agencies, including science and technology groups. At its embryonic stage, APT is promoting the pragmatic, economic interest-based cooperation, namely the East Asian Free Trade Agreement (EAFTA) that would encompass one third of the world's population. In the future, it will attempt to be the vehicle for deeper integration structured on some kind of "community" basis, cooperating on areas such as environmental protection, human security, cultural and personal exchanges, energy conservation, education and research, etc.

My thesis analyzes the ongoing development of regional integration in greater East Asian region. I pay special attention to the state-led efforts pushing forward for an "East Asian Community (EAC)" under the framework of ASEAN+3. My thesis attempts to address the following questions, and hope to illuminate the interplay of national and regional forces in East Asia that currently experience a historical moment:

1. What forces motivated the growing economic integration in East Asia before the 1997 financial crisis?
2. What role did 1997 Asian financial crisis have in instigating political will among East Asian states to promote the vision of an EAC? What are the possible economic benefits of forming an EAC?
3. How did political reality before the 1997 obstruct building of an EAC, and how did forces of regional integration gradually overcome those political barriers?
4. What is the role of the United States in East Asian regionalism?
5. How did the EAC framework develop recently? What are some recommendations to further the ongoing process of East Asian integration?

## 1.2. Regionalism

### a. Definition and Explanation of Different Levels/Forms of Regionalism

Regionalism is a term used in international affairs and the commercial system. In its broad sense, regionalism refers to *an expression of common sense of identity or purpose through a conscious policy of states or nongovernmental actions to coordinate activities and arrangements in a greater region.*<sup>9</sup> In its specific use in international economics, regionalism can also refer to the “creation of intergovernmental institutions designed to promote economic integration by liberalizing or facilitating trade or other forms of cross-border economic activities within a region.”<sup>10</sup> Various forms of regionalism require different levels of commitment. An FTA between two countries in the same region is considered a ‘solid regionalism’ with binding rule of law. On the other hand, consultative bodies are not legally binding in nature, and are considered a looser form of regionalism. Among the forms of legally enforced regionalism, there are five stages of regional economic integration ranging from shallow to deep level: preferential trade agreements, free-trade area, custom union, common market, and economic union.<sup>11</sup> The first three stages are considered “shallow integration” stages as they attempt to establish low level of trade barriers among member countries via policies like providing preference to trading partners, eliminating tariffs and quantitative restriction. Examples include ASEAN FTA and North American Free Trade Area. The last two stages are characterized as “deep integration.” Each stage respectively represents promoting free movements of factors of production and integrating national economic policies and a common currency. Most notable example includes the European Union.

Regional integration in the global economy has been on the rise from the 1990s onwards. Countries began to realize that building cooperative regional and multilateral institutions is an

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<sup>9</sup> “Regionalism and world economic order,” in *Regionalism in World Politics*, edited by Louis Fawcett and Andrew Hurrell (Oxford University Press, 1995), pp. 77-80.

<sup>10</sup> Munakata, Naoko. *Transforming East Asia: The Evolution of Regional Economic Integration*. Washington D.C.: Brookings Institution Press, 2006, pp. 189

<sup>11</sup> Das, Kilip K., *Regionalism in Global Trade*. Cheltenham: Edward Elgar, 2004, pp. 15

effective way to overcome complex global economic and trade realities. The regionalization of world trade operating simultaneously with advancing global integration, particularly trade in goods and services, has attracted much scholarly attention. Many theories were born out to measure the progress of regional integration and the proliferation of Regional Integration Agreements (RIA) in the background of globalization. Neo-liberalism argues that increasing interdependence creates demand for more integration. Integration efforts primarily come from state elites in a 'top-down' manner. Cooperation occurs to the extent that it can solve problems arising from interdependence and/or produce direct economic or other benefits from it.<sup>12</sup> Neo-functionalism envisions regional integration to be a 'bottom-up' process involving mostly technical experts and business groups cooperating in relatively non-controversial areas. Cooperation proceeds in an incremental fashion, eventually moving beyond the private technical areas to high politics governed by interest groups and political parties. Finally, inter-governmentalism argues that integration is the result of a process of bargaining between state leaders. Thus depending on the bargaining preferences, integration is more likely to proceed in sudden vigorous manner than the smooth incremental fashion envisioned by neo-functionalism.<sup>13</sup>

In addition to the conditions described by major theoretical approaches, several other conditions are important for regional integration. One is geographic compactness. States that are close together are more likely to share common interests and take advantage of trading and other collaborative opportunities. Another condition for successful integration efforts is relative symmetry in capabilities (military, political, and economic) among prospective members. The logic is that states with approximately equal power will be better able to form greater cooperative arrangements. Other analysts indicate that *projected* stability in the distribution of those

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<sup>12</sup> Lee, Pho Ping, Tham, Siew Yean & Yu, George T. (eds.) *The Emerging East Asian Community: Security & Economic Issues*. Penerbit UKM: Bangi, 2006, pp. 41

<sup>13</sup> Ibid. pp. 42

capabilities *over time* is more relevant than simple comparison of relative capabilities among prospective members.<sup>14</sup> All these conditions have contributed to the proliferation of regional institutions on the ground or in study. Such institutions include European Union, Free Trade Area of the Americas (FTAA), NAFTA (North American Free Trade Agreement), the Gulf Cooperation Council (GCC), the Central American Common Market (CACM), the Caribbean Community (CARICOM), and the Southern Common Market (Mercosur), etc.<sup>15</sup>

#### b. Development of Regionalism in the East Asian Context

Generally, East Asian regionalism has been following the trajectory envisioned by neo-functionalism as the region became economically integrated through a ‘bottom-up’ process involving proliferating number of non-governmental, mostly business, cooperation in the region. Despite being one of the three ‘mega-regions’ (Europe, North America, and East Asia), in which most of the world’s production, trade and investment is concentrated, ‘top-bottom’ process of regionalism involving government initiatives only started in the late 1990s after the 1997 financial crisis. Relative to other regions, East Asian governments were slow and late in adopting the concept and phenomenon of regionalism while enterprises were quick to arrange a series of activities that enhanced regional economic integration. There is one exception in this paradigm: Japan-led Greater East Asia Co-Prosperity Sphere during the 1930s and 40s. Japanese imperial state during the World War II was much devoted to establishing an exploitative trade networks linking Japan and other Asian economies in order to acquire natural resources for the war efforts. As the self-designated leader of the Greater East Asia Co-Prosperity Sphere, Japan promised economic development and industrialization to other East Asian countries to face the Western colonial powers. However, the Japanese scheme of Pan-Asian unity was soon debunked as a

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<sup>14</sup> Ibid. pp. 43

<sup>15</sup> FAOSTAT (Food and Agriculture Organization of the United Nations), Concepts & Definitions, <http://faostat.fao.org/site/374/default.aspx>

myth. Instead of providing assistance and pursuing mutual development, Japan took over other Asian local economies, extracted local natural resources, and exploited native labor resulting in death toll of millions of Asian civilians due to fighting, atrocities, disastrous labor and economic policies, and the starvation and disease that followed.<sup>16</sup>

After the Second World War, however, Japan achieved remarkable economic growth from the 1950s to the 1980s thanks to the export-driven development strategy. Japan first began by exporting labor-intensive products like textiles. Gradually, the composition of exports changed through technological progression, including heavy industrial goods, complex machinery and equipment, and consumer durables that require large capital and advanced technology. Japanese government policies played a large role in encouraging the export of higher value goods, providing positive feedback effect of greater industrialization. Some of those policies were:

1. Compulsory saving deductions – it curtailed consumption and yielded high rates of saving.
2. Investment in strategic industries – substantial amounts of saving were channeled into industries such as iron and steel, autos, shipbuilding and semiconductors that have large technological spillover effects.
3. Export and import growth – the growth in exports generated revenue in foreign currency, which allowed Japan to import capital goods and technology from abroad.
4. Public and private capital – allocation of capital was primarily through the banking system with government guarantees of high debt levels in major industries.
5. Cozy insider relations between business and government – the government set up export processing zones, raised capital by attracting foreign investment, and provided subsidies to key industries.<sup>17</sup>

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<sup>16</sup> Dower, John W. *War Without Mercy: Race and Power In the Pacific War*. 7<sup>th</sup> printing, corr. by the author, New York: Pantheon Books, 1993, c.1986, pp. 7.

<sup>17</sup> Prestowitz, Clyde, “What happened to the Japanese Economic Model?” *Washington Post*, December 14, 1997. <[www.washingtonpost.com/wp-srv/business/longterm/asiaecon/stories/japecon121497.htm](http://www.washingtonpost.com/wp-srv/business/longterm/asiaecon/stories/japecon121497.htm)>

Japan's export-oriented growth model had substantial impact on structural transformation of the newly industrialized Asian economies (NIAEs),<sup>18</sup> four members in the Association of Southeast Asian Nations (ASEAN-4),<sup>19</sup> and the People's Republic of China (hereafter China). These countries had learned much from Japan's economic miracle and adopted similar yet localized version of Japanese economic policies in their homelands. However, the real beginning of regional economic integration occurred *after* the Plaza Accord<sup>20</sup> in September 1985. A new division of labor among East Asian countries arose when the yen appreciated sharply against dollar by 40 percent between 1985 and 1987 due to the Plaza communiqué. The yen's dramatic rise in short period of time compelled many Japanese companies to move their factories offshore so that they could cut production costs by taking advantage of cheap labor and remain competitive in the U.S. market. Japanese companies set up production networks first in NIAEs, then in ASEAN-4 countries and China, leading to brisk expansion of intra-regional trade and investment. According to Dilip K. Das (2004), this phenomenon is explained by the "*flying geese hypothesis*." He describes:

It implies a more developed economy aiding and stimulating economic growth in the less developed ones, which in turn aids and stimulates growth in the even less developed economies, in the process making a functional chain of leader-follower economies. Generally there will be one leader economy and several follower ones at various strata of economic development, providing an imagery of flying geese. Asian economic development followed

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<sup>18</sup> Hong Kong SAR, South Korea, Singapore and Taiwan.

<sup>19</sup> Indonesia, Malaysia, the Philippines, and Thailand.

<sup>20</sup> On 22 September 1985, the Group of Five (G-5, United States, Germany, Japan, France, and the United Kingdom) finance ministers and central bankers met at the Plaza Hotel in New York and called for the appreciation of the yen and the deutsche mark, instead of the depreciation of the dollar. The Plaza communiqué had a substantial short-term impact over the foreign exchange markets and the dollar went into a steep decline, while the yen and deutsche mark began to appreciate, the former sharply (Das, 2004, Regionalism in global trade, p. 168)

this paradigm, where the Japanese economy was the lead economy, followed by the NIAEs as the second tier economies, and further down the line came the ASEAN-4 and China.<sup>21</sup>

The so-called “flying geese” paradigm remained a major boost for pan-Asian economic growth for decades. Economic linkages and interdependence in the region have grown considerably since the mid-1980s. The 2001 value of intra-regional trade in East Asia was \$722 billion, or 48.2 percent of total Asian trade.<sup>22</sup> Changes in currency value configuration in 1985 led to building of extensive intra-regional production/investment network, and ultimately to the bottom-up market-driven economic regionalism in East Asia. However, despite of the large-scale on-the-ground economic networks, East Asian governmental efforts towards regional economic integration did not arise until the aftermath of 1997 financial crisis. What prompted the sudden surge of political will towards East Asian institutional arrangement after that particular incident? In the following chapter, in regards to the 1997-98 Asian Financial Crisis, I will address this question with detailed explanations.

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<sup>21</sup> Das, p. 168

<sup>22</sup> Das, Dilip K. (2005) “Market-Driven Regionalization in Asia,” *Global Economy Journal*: Vol. 5: Iss. 3, Article 2.

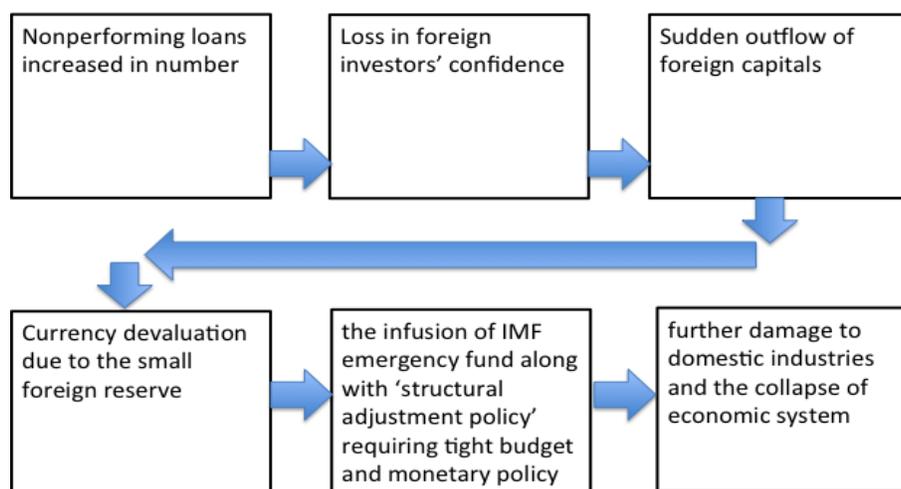
## **2. Economic Needs Realized in the *post-crisis East Asia***

The Asian Financial Crisis and the Global Financial Crisis played an important role in promoting regionalism. In this chapter, I will answer the question: “What has been the effect of the financial crisis on East Asia regionalism?” The 1997-98 Asian Financial Crisis is the turning point for East Asian countries to look at formation of the East Asian Community, which replication the European Union and the European Economic Area. This chapter begins with a general overview of the causes and extent of the crisis in different East Asian economies, then the discussion about the disastrous social, economic impacts of the Asian crisis follows. I extensively analyze some key factors of the Asian crisis such as rapid financial liberalization headed by the U.S. during 1990s, Washington Consensus, and sudden in/out-flows of foreign capital, all leading to huge loss of confidence among international investors in the region. Then, I discuss the role of the Global Financial Crisis and economic relationship of China to East Asian countries, including the establishment of the Asian Infrastructure Investment Bank (AIIB). Though the U.S. finds the establishment of the AIIB as China’s political agenda, the bank further strengthens the economic relationship of China to the East Asian countries and to the world.

### 2.1. 1997-98 Asian Financial Crisis

It was the 1997-98 Asian Financial Crisis that provided a prime catalyst for the growth of governmental initiatives aiming to further East Asian regional economic cooperation. It was the third international financial crisis after two crises affecting Latin America in 1982 and Mexico in 1994. The Asian crisis spread from Thailand to Indonesia, the Philippines, Malaysia and South

Korea, with devastating socio economic consequences at each destination. The sequences of the crisis were unfolded in this manner<sup>23</sup>:



Despite of its terrible economic blow, the Asian financial crisis also illuminated economic interconnectedness among ASEAN+3 countries, contributing to the heightened East Asian consciousness. The crisis also demonstrated the increasing need for regional approach to financial stability since both national and global solution (i.e. the solution by the International Monetary Fund) had shortcomings. Individual countries could not mobilize enough resources to ward off currency pressure. On the other hand, the IMF took very little account of national variations; it simply prescribed one economic recovery model for almost all the affected countries (except Malaysia), and it also exacted too high political/social/economic costs for giving out its emergency loans. Through combination of these reasons, a *strong political will* towards East Asian regionalism finally arose. The ASEAN+3 grouping became the main instrument through which the East Asian consciousness was expressed to help alleviate the crisis and to prevent future crisis.

#### a. Background

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<sup>23</sup> Gregory W. Noble and John Ravenhill, "Cause and Consequences of the Asian Financial Crisis," in Gregory W. Noble and John Ravenhill, eds., The Asian Financial Crisis and the Architecture of Global Finance, ed., Cambridge, 2000, pp. 1-35.

A number of complex factors appear to have contributed to the Asian financial crisis. Most diagnoses center on a combination of factors, including overreliance on short-term foreign capital, excessive investment in real estate, inadequate financial supervision, and politically motivated credit allocations that resulted in a massive non-performing loan problem.<sup>24</sup> Many economists, particularly from the World Bank and the IMF, have pointed out “crony capitalism” as the root cause of the Asian crisis. They argue that Asian governments were responsible for misguided economic policies such as mismanaging the inflows of capitals, banks rife with favoritism and incompetence, lax accounting procedures, allowing massive bad loans to large corporations, and a lack of transparency on the parts of banks, corporations, and governments.<sup>25</sup> Economists suggest that further liberalization of their financial system is necessary to mend the governmental deficiency. However, I argue that the root cause of the crisis was rather hasty liberalization of the Asian financial system (particularly in regards to short-term capital inflows) that is courted and actively sponsored by the United States, the IMF, and the World Bank with their collective commitment to the “Washington Consensus.” The reduction of government-imposed restrictions on the capital inflow and outflow has put many countries financially vulnerable to foreign investment. Liberalization of capital controls lifted limits on foreign investment in a country’s financial markets, on direct investment by foreigners in businesses or property, and on domestic residents’ investments abroad. Joseph Stiglitz, former Chief Economist from the World Bank, concurs with this view regarding the cause of the 1997 crisis as he once commented; “the single most important factor leading to the Asian crisis is ‘capital

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<sup>24</sup> Richard P. Cronin, "Asian Financial Crisis: An Analysis of U.S. Foreign Policy Interests and Options," Congressional Research Service *Report for Congress*, April 23, 1998, at [http://www.stimson.org/southeastasia/pdf/98-74f\\_1998Apr23.pdf](http://www.stimson.org/southeastasia/pdf/98-74f_1998Apr23.pdf) (July 12, 2007).

<sup>25</sup> Goldstein, Morris, and Institute for International Economics (U.S.) *The Asian financial crisis: causes, cures, and systemic implications/ Morris Goldstein* Institute for International Economics, Washington, DC: 1998

account liberalization.”<sup>26</sup> Financial liberalization indeed has had many adverse consequences for developing countries in Asia by undermining their financial arrangements, institutions, and regulation systems.

The U.S. gradually pushed for opening up foreign countries’ financial market via what is called “Washington Consensus,” involving a set of policies aimed at liberalizing international financial order. U.S. based finance firms also supported the policies as they expected that profits were correlated with higher capital mobility in the world. In addition, both the U.S. Treasury Department and the International Monetary Fund (IMF) pushed foreign countries to remove their restrictions on international borrowing and investing in the rhetoric of trade liberalization and government deregulation. They have made claims that financial liberalization would assure high economic growth with massive capital inflows into developing countries.<sup>27</sup> However, this type of short-term inflows rarely contribute to real capital formation and, thus, to economic growth. Rather, they contribute to creation of asset market bubbles, mostly in the stock and real property markets. Short-term inflows also bring in strong foreign financial interests in the borrowing economies, making them susceptible to herd behavior by foreign investors. A significant upsurge of foreign assets in regional markets, thus, increases the chances of contagion from abroad.<sup>28</sup>

Whether the five most affected Asian countries (Malaysia, Philippines, Indonesia, Thailand, and South Korea) have room for political maneuver to avoid the influence of the Washington Consensus, it is still debatable. Yet, there is still no doubt that the U.S. at the time has enormous power and influence over economic policy of the listed Asian countries through the IMF. Quite often the IMF stood as a vanguard of the U.S. interest; the US Treasury

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<sup>26</sup> Beeson, Mark. *Regionalism & Globalization in East Asia: Politics, Security & Economic Development*. New York: Palgrave Macmillan, 2007, pp. 210

<sup>27</sup> Gill, Huang, and Kharas, editors, 2007, pp. 114.

<sup>28</sup> Ibid.

Department held (and continues to hold) not only a veto but also an overwhelming dominance within the organization – theoretically, Europe and Japan together could outvote the U.S. but they have not chosen to do so since its inception in 1944 for fear that any challenge to Washington’s dominance in the institution (and the World Bank) might help developing countries gaining a voice.<sup>29</sup> The IMF also exerts its real power through its position as “gatekeeper” for official credit, having lots of sway over the international circle of creditors. A borrowing country that does not meet IMF conditions will often face hard time borrowing loans from the much larger scale, such as the World Bank, regional banks (i.e. Inter-American Development Bank), high-income country governments including those belonging to the Paris Club, and sometimes even the private sector.<sup>30</sup> Thus, the Asian countries experienced tremendous political pressure to adhere to the “suggestions” given by the IMF before the crisis.

The decision to liberalize financial sectors throughout 1990s turned out to be a reckless one as proven by statistics such as ratio of foreign liabilities to foreign assets, non-performing loans, and contribution of inward foreign direct investment to current account financing. All of the indicators pointed towards the rise in *purely speculative capital* in the Asian countries; such capital termed as “*hot money*” – extremely volatile short-term capital that moved on a short notice to any country providing better returns – tended to enter the country in massive quantity when economies were growing thereby contributing to economic bubble and artificial aura of success, and tended to exit very quickly on a mere suspicion of a downturn or other negative factor, causing a near collapse of the country’s financial structure.<sup>31</sup> In the pre-crisis period, high GDP growth in many Asian countries was the result of both increase in exports and large inflow

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<sup>29</sup> Weisbrot, Mark. “Ten Years After: The Lasting Impact of the Asian Financial Crisis.” Center for Economic and Policy Research (CEPR), August 2007.

<http://www.cepr.net/index.php/publications/reports/ten-years-after-the-lasting-impact-of-the-asian-financial-crisis/>

<sup>30</sup> Ibid.

<sup>31</sup> BusinessDictionary.com, definition of ‘hot money.’ <[www.businessdictionary.com/definition/hot-money.html](http://www.businessdictionary.com/definition/hot-money.html)>

of those speculative foreign capitals due to lax regulation of the financial market. Then the bubble burst, where all the capital flew out of the Asian countries as fast as it once flowed in. The trigger for the massive capital flight was rooted upon heavy short-term international borrowing of the five Asian countries. South Korea's government, for example, removed a number of restrictions on foreign ownership of domestic stocks and bonds, residents' ownership of foreign assets, and overseas borrowing by domestic financial and non-financial institutions as part of financial liberalization.<sup>32</sup> Korea's foreign debt nearly tripled from \$44 billion in 1993 to \$120 billion in September 1997. The short-term percentage of the loan reached the country's record high at 67.9 percent by mid-1997.<sup>33</sup> For comparison, the average ratio of short-term to total debt for non-OPEC less developed countries at the time of the 1980s debt crisis (1980-82) was twenty percent.<sup>34</sup> Other countries faced similar vulnerabilities. Indonesia piled up \$39.7 billion of debt by mid 1997, 87 percent of which was short-term.<sup>35</sup> As the crisis loomed over, the five countries had a combined debt to foreign banks of \$274 billion, with about sixty-four percent in short-term obligations.<sup>36</sup>

The high percentage of short-term debt relative to reserves invited much panic among investors when the Asian countries' economic growth slowed down. In order to serve the debts, people sold their domestic currency to get dollar or other "hard" currencies; a resulting depreciation of the domestic currency led to even higher costs of debt service. This situation especially became dangerous when there was a "rush" for the capital exits as more and more investors converted the domestic currency and asset into dollars. The reserve shrank further in

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<sup>32</sup> Chang, Ha-Joon, Hong-Jae Park, Chul Gyue Yoo. 1998. "Interpreting the Korean Crisis - financial liberalisation, industrial policy, and corporate governance." *Cambridge Journal of Economics*, vol. 22, no. 6.

<sup>33</sup> Radelet, Steven and Jeffrey Sachs. 1998b. "The East Asian Financial Crisis: Diagnosis, Remedies, Prospects." Harvard Institute for International Development, April 20, 1998.

<sup>34</sup> Chang et al, 1998.

<sup>35</sup> Bank for International Settlements data cited in Radelet and Sachs 1998b.

<sup>36</sup> Ibid.

order to meet the rising demand, which then sent signals to currency speculators about the expected fall in the currency value. Thus, the downward spiral continued as the domestic currency value against dollar plummeted and foreign lenders refused to renew the short-term loans. Capital flight intensified as more and more investors lose confidence in the country, leading to currency and stock market crash.

#### b. Impact

The Asian financial crisis was unfolded in the sequences mentioned above, first starting in Thailand. In the beginning of 1997, a large number of Thai financial institutions failed to pay some of their short-term borrowings invested in development projects for various attraction sites and real estate markets, where government bailouts were expected.<sup>37</sup> Thai government relied on its reserves to take up some of these loans, leading many currency speculators to bet against the Thai baht; they knew that Thai government would eventually have to devalue Baht as the efforts to maintain the currency peg to dollar would surely result in reserve draining. By June of that year, that speculation came into reality. The Bank of Thailand used approximately \$28 billion out of its \$30 billion international reserves to defend the value of the baht in the course of forward market interventions.<sup>38</sup> On 02 July, Baht was 18 percent devalued in one day, causing investors to lose confidence in Thailand's economy. Investors suddenly lowered their valuation of all the assets of Thailand, leading to an even sharper fall in the Thai exchange rate. The baht reached the bottom at 48.80 baht per dollar in December of the same year, the highest rate (lowest value of the Thai baht) ever since Thailand started keeping record in 1969.<sup>39</sup> Thailand's cratered economy quickly spread financial instability and political turmoil from Indonesia to

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<sup>37</sup> Laplamwanit, Narisa. "A Good Look at the Thai Financial Crisis in 1997-98." Columbia University, Fall, 1999. <[http://www.columbia.edu/cu/thai/html/financial97\\_98.html](http://www.columbia.edu/cu/thai/html/financial97_98.html)>, accessed on December 14, 2012.

<sup>38</sup> Laplamwanit, Narisa.

<sup>39</sup> Gargan, Edward A. "As Currency Crisis Roils Asia, Thais Ask for IMF's Help." *New York Times*, July 29, 1997, <http://www.nytimes.com/1997/07/29/business/as-currency-crisis-roils-asia-thais-ask-imf-s-help.html?pagewanted=2>

South Korea. Many currency speculators bet heavily against many Asian currencies with exchange rates linked to the U.S. dollar, and as a result they indirectly triggered herd-like behavior of foreign investors; massive capital flights from the Philippines, Malaysia, Indonesia, and South Korea followed.

On 11 July 1997, nine days after the Thai baht collapsed, Manila gave in. The Philippine peso was devalued by 4 percent; increasing import prices and much fall in domestic demand. Eventually the stock market went down 22 percent.<sup>40</sup>

Malaysian economy followed the suit. It surrendered on 14 July as the ringgit plunged to a 33-month low, even after the central bank tried its best to safeguard the currency by jacking up interest rates to 50 percent and spending almost \$1 billion from its foreign reserves. Lamented Malaysian Finance Minister Anwar Ibrahim stated, "there's a limit to what we can do."<sup>41</sup> Indonesia's rupiah also fell to a record low of 2,471 to the U.S. dollar.<sup>42</sup>

The crisis then spread to a Northeast Asian country of South Korea. The South Korean won depreciated by 68.25 percent in 1997 against the U.S. dollar. Korea's stock market also suffered severely during the Asian financial crisis, falling by 7 percent in November 8, 1997, the biggest one-day drop ever recorded there to date; by the end of 1997, it fell to low 42.62 percent from the height of 1996 data.<sup>43</sup>

Relatively a minor currency crisis in Thailand had wide-range spillover effects across East Asia via contagion effects; the herd-like behavior beset by the period of financial turmoil in foreign exchange markets led many foreign investors to panic and set the capital flight in motion

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<sup>40</sup> "The Currency Crisis Sweeping Southeast Asia." Finance: Foreign Exchange. BusinessWeek, July 28, 1997. <http://www.businessweek.com/archives/1997/b3537090.arc.htm>

<sup>41</sup> Ibid.

<sup>42</sup> Ibid.

<sup>43</sup> "Timeline: Asia's Financial Crisis 1997-1999," *Washington Post*, <http://www.washingtonpost.com/wp-srv/business/longterm/asiaecon/timeline.htm>

out of Asia. In Thailand, Malaysia, Indonesia, the Philippines and Korea, a *positive net inflow* of over US\$92.8 billion in 1996 quickly turned into a *negative net outflow* of over \$12.1 billion in 1997. This \$105 billion turnout in less than a year represented about 11 percent of the total GDP of the five countries.<sup>44</sup> Rapid capital outflows resulted in further currency devaluations and stock market crashes. Economic instability led to negative GDP and wage growth along with soaring inflation and unemployment, and eventually a severe economic recession. For example, in a matter of months, the number of unemployed workers increased by over 800,000 in Indonesia, 1.5 million in Thailand, and about 1.35 million in South Korea. As currency values plummeted, people's effective wages also dropped. By the end of 1998, real wages had dropped by 12.5 percent in South Korea and by 6 percent in Thailand.<sup>45</sup>

### c. Post-Crisis Recovery Efforts

Negative views about the merits of IMF crisis-management policies dominated much of East Asian sphere in the aftermath of the crisis. The IMF emphasized the internal factors as the main cause of the crisis, criticizing the ‘crony capitalism’ and ‘corruption’ of the affected countries. In this line of thinking, the IMF and the Treasury Department overlooked the actual cause of the crisis, which was the *liquidity problem*; the IMF could have restored confidence among foreign investors and stabilized the currency market in the crisis-hit countries if it provided enough currency reserves to the affected economies.<sup>46</sup> In September 1997, when it was still early enough to avoid much of upcoming financial disaster, Japan proposed the creation of an “Asian Monetary Fund” to provide much needed emergency liquidity to faltering East Asian

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<sup>44</sup> Weisbrot, Mark (2007).

<sup>45</sup> World Bank, *East Asia & Pacific Update: 10 Years After the Financial Crisis*, April 5, 2007, at <http://www.worldbank.org/eapupdate> (July 12, 2007).

<sup>46</sup> Masahiro Kawai. (1998) The East Asian currency crisis: Causes and lessons. *Contemporary Economic Policy*. 16 no. 2 (April 1): 157-172, accessed December 16, 2012.

economies. Other Asian countries endorsed the proposal and total combined endowment up to \$100 billion was supported by Japan, China, Taiwan, Hong Kong, and Singapore. However, after staunch opposition from the U.S. Treasury Department and the IMF, the proposal was dropped by November.<sup>47</sup> To many Asian leaders, the U.S. antagonism to the creation of a pan-Asian stabilization fund seemed as though Washington's top priority was maintaining its financial dominance in the region by only supporting the IMF in which the U.S. had much influence.

After regaining control over the post-crisis international settlement, the IMF then set out the details of "structural adjustment policy" in return for financial bailouts. The policy contained a far-reaching reform packages: "high interest rates and a tightening of domestic credit to slow economic growth; fiscal tightening, including cuts in food and energy subsidies; and further liberalization of international capital flows including those relating to the domestic financial service market and foreign exchange controls."<sup>48</sup> The policy based on misdiagnosis of the problem unmistakably exacerbated the situation. South Korea was required to rescind virtually every remaining restriction on capital flows, making itself more vulnerable to the international speculation. South Korean currency (the won) had depreciated by 80 percent soon after it signed a deal with the IMF. In the first few months of the intervention, the IMF also failed to organize a rollover of the short-term debt owed by Indonesian firms. Thus, Indonesian currency and economy suffered, as the firms could not even acquire enough credits for essential imports and exports. As a result, the Indonesian Rupiah took its worst plunge just days after the signing of the second IMF agreement in January 1998. The IMF made a further mistake of disbursing the funds too little and too late to alleviate the damage. Only \$3 billion had been provided by March 1998,

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<sup>47</sup> Weisbrot, Mark, 2007

<sup>48</sup> Ibid.

as opposed to the \$40 billion commitment.<sup>49</sup> In short, the IMF's structural reforms were in many cases economically unsound and they failed to bring market confidence in the region.

Those countries could have fared better if they resorted to different solutions such as refusing the aid offered by the IMF. Malaysia stood out as a model in this alternative scenario; the country implemented many policies in completely opposite direction compared to the policies adopted by other Asian countries under the IMF supervision. Instead of further opening its economy, Malaysia instituted various task force agencies for capital controls, in an effort to reduce speculative trading in its currency. In order to revitalize the economy, Malaysia made massive government spending instead of taking severe budget cuts. Finally, the Malaysian central bank, Bank Negara Malaysia, instituted a low interest rate (as opposed to high interest rates suggested by the IMF) policy to ease domestic credit and spur economic activity. Thanks to these policies, economic growth settled at slow yet sustainable pace. Malaysia had GDP growth of 5.6 percent in 1999 from -7.5 percent in 1998, and massive current account deficit gradually became a fairly substantial surplus.<sup>50</sup>

#### d. The Role of the Crisis in East Asian Regionalism

The 1997-98 Asian Financial Crisis created economic and social chaos in several East Asian countries, but it nevertheless boosted the awareness of East Asia as a region. This realization came about in three ways.

First, the crisis emphasized the vulnerability of East Asian economies as they became exposed to the decisions and whims of 'international investment cartel' beyond national control; contagion effects fueled by speculation and herd behavior of foreign investors threw more and more countries into financial mayhem. The crisis provided political will to engage in further

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<sup>49</sup> Radelet, Steven and Jeffrey Sachs. 1998b.

<sup>50</sup> Asian Development Bank, "Asian Development Outlook 2000 Update: Malaysia," September 2000. <[www.adb.org/documents/books/ado/2000/Update/Malaysia\\_update.pdf](http://www.adb.org/documents/books/ado/2000/Update/Malaysia_update.pdf)>

economic integration and build a cooperative regional financial institution to prevent similar crisis in the future.

Secondly, the crisis aroused renewed concern over the lack of a stable long-term debt market, which can serve as a main avenue of investment for high savings enjoyed by many East Asian countries. According to Jennifer Amyx, a professor from University of Pennsylvania, East Asian countries failed to take advantage of their own high levels of savings because the savings deposited into local banks tend to be redirected to international financial centers mostly based in Europe and the U.S., and then come back into the region as short-term dollar-denominated loans.<sup>51</sup> As mentioned above, these short-term debts greatly contributed to the instability of many Asian currencies while making economies susceptible to the herd mentality that often manifests itself among global fund managers. A well-developed regional organization such as the proposed Asian Monetary Fund could provide more financial instruments to better mobilize East Asia's vast amounts of savings, guaranteeing 'safer' investments.

Thirdly, the crisis made intraregional trade to become ever more important for regional economic growth. Roberto F. de Ocampo<sup>52</sup> argues that the growing intra-regional trade helped the East Asian economies to recover more quickly following the crisis as Japanese and American market went through economic slumps. By 2005, intraregional trade had grown to more than 40 percent of total trade, comparable to that of the North American Free Trade Area, becoming an effective mechanism to diversify the region's export destination.<sup>53</sup>

Overall, the Asian financial crisis was a driving force behind increasing regional cooperation in East Asia. Initially, the material and psychological consequences of the 1997

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<sup>51</sup> Beeson, Mark (2007), pp. 214.

<sup>52</sup> Roberto F. de Ocampo<sup>52</sup> is the president of the Asian Institute of Management. As secretary of finance (1994-98), he was widely recognized as the main architect of resurgence in the Philippine economy.

<sup>53</sup> Gill, Huang, and Kharas, editors, 2007, pp. 59.

crisis drove many affected countries to have defensive motivations to guard their countries against capital interests outside the region. The depth of resentment against the intrusive, insensitive role-played by the IMF and the US (which de facto largely dictates the IMF's policies) intensified in those countries. Not only did it come too late, but its 'one size fits all' attitude with 'structural adjustment policy' prescription created much political and economic anguish in countries like Indonesia, Philippines, Thailand, and South Korea who accepted IMF loans, while Malaysia, which did not accept the loans, escaped this anguish. However as times went by, the idea of East Asian regional community had been increasingly shaped by an intraregional desire to deal with common concerns. All countries shared a desire to strengthen regional financial architecture to promote further deepening of economic interactions that began following the Plaza Accord in 1985. According to Solingen, regional organizations are most likely to emerge when government leaders in geographically proximate countries share and pursue common internationalizing agendas that lead them to conclude that cross-border cooperation will be to their collective benefit.<sup>54</sup> The crisis was a trigger for regional policymakers to realize such benefit of regional cooperation to manage financial globalization and prevent future crisis.

## 2.2. 2007-2008 Global Financial Crisis and Asia-Pacific Response

The 1997 Asian Financial Crisis tested the economic cooperation of ASEAN member states. During the 2007 Global Financial Crisis, the ASEAN economies, except Japan, were not heavily hit hard in comparison to their Western counterparts (Figure 1). According to the Asian Development Bank, the overall growth in Asia tumbled from its impressive peak of 9.5% in 2007 to 6.3% in 2008 to 3.4% in 2009.<sup>55</sup> The cause of this decrease was the collapse in trade, business, and consumer confidence in the United States, Europe, and Japan. Among the countries

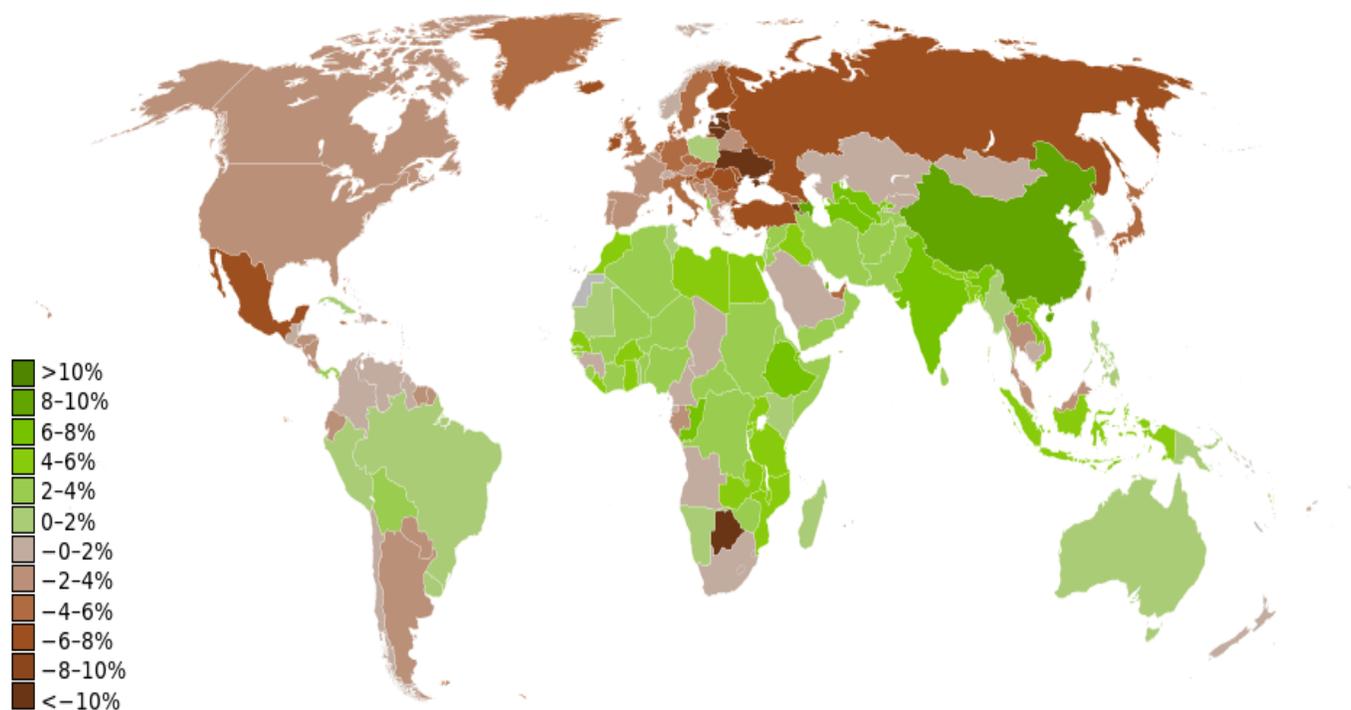
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<sup>54</sup> Pempel, T.J., editor, 2005, pp. 132.

<sup>55</sup> Asian Development Bank, "The Global Economic Crisis: Challenges for Developing Asia and ADB's Response." April 2009.

in Asia, Japan was heavily hit because “90% of Japanese exports consist of highly income-elastic industrial supplies, capital goods, and consumer durables.”<sup>56</sup> Because of this, the collapse of European and American markets influenced to the negative impact of Japanese exports.

Figure 1: 2009 Real GDP Growth Rates<sup>57</sup>  
(Countries in brown were in recession)



As Asia-Pacific region saw the United States struggle with the financial crisis, high-level policy dialogues were organized to discuss how to tackle the crisis and exchange ideas in strengthening the resilience of the region in the future financial crisis. High-level officials attended the first dialogue from seventeen Asia-Pacific countries, including officials from all ASEAN member states and China.<sup>58</sup> Subsequent policy discussions continued through the years

<sup>56</sup> Ibid.

<sup>57</sup> Central Intelligence Agency, “The World Factbook: Real GDP Growth Rates for 2009.” <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2003rank.html>. Accessed 01 May 2015.

<sup>58</sup> Isgut, Alberto (edited), UN Economic and Social Commission for Asia and the Pacific. “Asia-Pacific Economies after the Global Financial Crisis: Lesson Learned and Way Forward.” 2014.

to further prepare the region in the future. Other policy discussions include: external debt management (Dhaka), strategies to boost competitiveness (Phnom Penh), G-20 agenda perspective (Manila), energy security (Nadi), and infrastructure financing (Yogyakarta and Almaty).<sup>59</sup> These interactive dialogues not only show the commitment in assisting other countries by sharing ideas and experiences in responding to crises, but also show the effective partnerships of ASEAN member states and other Asia-Pacific countries.

#### a. China and East Asia after the Global Financial Crisis

During the Global Financial Crisis, China's growth remained one of the highest in the world. In early 2015, the Chinese government released its annual economic report and the 2014 report shows the lowest growth rate since the 1990s (Figure 2). China's growth slowdown does not implicate to its relationship with East Asia. The economic growth is easing due to lower demand, slowing industrial production and declining exports, which is a global phenomenon. Moreover, the "continued measures to contain local government debt, contain shadow banking, reduce excess capacity, curb energy demand, and control pollution will reduce investment and manufacturing growth [in China]."<sup>60</sup> The World Bank forecasts the economic slowdown not only in China but also in the region.<sup>61</sup> Based on the economic forecasts of international financial institutions, the slowdown in global economic growth will not necessary influence economic relationship with other Asian countries. To boost Chinese influence in the region, the Chinese government's effort is promoting internationalization of the Chinese Renminbi (RMB), which is widely accepted by South East Asian countries as cross-border trade transactions are traded in

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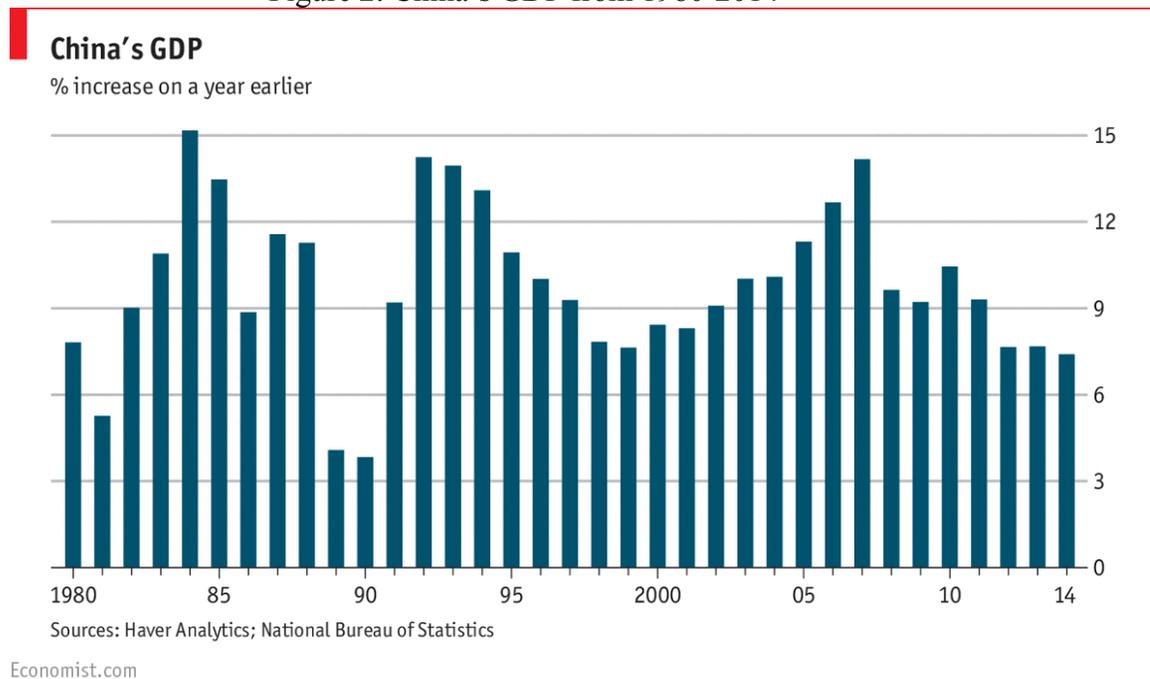
<sup>59</sup> Ibid.

<sup>60</sup> Noble, Josh. "World Bank trims east Asia growth forecasts." Financial Times. 13 April 2015. <<http://www.ft.com/intl/cms/s/0/119b58d6-e18e-11e4-9b30-00144feab7de.html#axzz3ZPgSfc3q>>.

<sup>61</sup> Ibid.

RMB.<sup>62</sup> With the effort to promote the relationship of China to the West, with the approval from the Chinese government, the United Kingdom is the first non-Chinese sovereign to offer RMB bond, in “a move to the currency’s global appeal and the UK’s desire for London to be the major offshore renminbi hub.”<sup>63</sup> The influence of the RMB arises from China’s trading partners in the region and the rest of the world.

Figure 2: China’s GDP from 1980-2014<sup>64</sup>



To further increase the influence of China in the region, the establishment of the Asian Infrastructure Investment Bank (AIIB) in 2014 by the Chinese government is the turning point in strengthening its trade and diplomatic relationships. The development of the bank is caused by the refusal of China to have more say in the World Bank and the IMF. As a World Bank de facto, the AIIB will assist in financing infrastructure projects in the Asian region. Opposed by the

<sup>62</sup> Shu, Chang, Dong He and Xiaoqiang Cheng . “One currency, two markets: the renminbi’s growing influence in Asia-Pacific.” Bank for International Settlements. April 2014 <<http://www.bis.org/publ/work446.pdf>>.

<sup>63</sup> Turner, Michael and Helene Durand. “UK opens sovereign offshore renminbi market.” Reuters International, 14 October 2014. <<http://www.reuters.com/article/2014/10/14/uk-dim-sum-idUSL6N0S91YN20141014>>.

<sup>64</sup> S.R, “China’s Slowdown from a Very Big Base.” The Economist. 20 January 2015 <<http://www.economist.com/blogs/freexchange/2015/01/chinas-slowdown>>.

United States because of its labor and environmental concerns and lack of transparency, the AIIB received an overwhelming number of members from U.S. allies, including Australia, New Zealand, the Philippines, South Korea, France, Germany, and the United Kingdom.<sup>65</sup> The decision of the United States “screwed up” for its refusal to join the AIIB according to former Secretary of State Madeleine Albright.<sup>66</sup> While at its development stage, member-states do not see any lack of transparency in setting the rules as major players in the international community (i.e. the United Kingdom and France) will have a say as part of the founding members. The implication of the development of the AIIB signifies the commitment of China in Asia, particularly in East Asia, by using it as its soft power strategy, which in turn makes the establishment of the East Asian Community more feasible.

### 2.3. Economic Benefits of Establishing an East Asian Community

The positive and visionary part of creating an East Asian Community includes benefits of increased intraregional trade, financial security, and stabilization of exchange rates in the region.

#### a. Trade

East Asian Community can intensify the force of *intraregional economic interdependence*. The benefits of this force are: reducing tariffs, administrative procedures, testing requirements and other transaction costs; improving the protection of intellectual property rights and the transparency of various government regulations; and strengthening economic linkages between high- and low-growth areas in order to improve the economic performance of the region as a whole and help facilitate the “catch-up” process of developing member states through technology transfer. Increasing economic interaction can also contribute to political

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<sup>65</sup> Panda, Ankit. “Australia To Join China-led Asian Infrastructure Investment Bank.” The Diplomat, 30 March 2014. < <http://thediplomat.com/2015/03/australia-to-join-china-led-asian-infrastructure-investment-bank/>>.

<sup>66</sup> Rapoza, Kenneth. “Washington’s Lobbying Efforts Against China’s World Bank Fail As Italy, France Welcome Aboard.” Forbes. 03 April 2015. < <http://www.forbes.com/sites/kenrapoza/2015/04/03/washingtons-lobbying-efforts-against-chinas-world-bank-fail-as-italy-france-welcomed-aboard/>>.

stability and harmonious diplomatic relations among member states, thereby providing a basis for institutionalized intergovernmental cooperation. In short, the EAC can boost intraregional trade through a systematic approach to target various problems that jeopardize the effectiveness of cross-border business operations.<sup>67</sup>

The EAC can further the intra-regional trade by creating an East Asian Free Trade Economic Zone which can lower the costs of international trades among Asian countries even more. It will make production networks in the region more competitive and attractive to foreign investments. It can also meet the desire of export-oriented economies to have diverse markets in the world as the domestic demand in the region, particularly consumer spending, rises. The important caveat here is that East Asia will *not* likely become a self-sufficient economic block at least in the *immediate* future despite of the overwhelming evidence of growing regional trade. Because East Asia's dependence on final demand from extra-regional industrial countries, the U.S. and Euro-zone members provides a strong incentive to be open to other regions in the world. According to the study done by the Monetary Authority of Singapore in 2001, approximately 78 percent of exports of East Asian economies excluding Japan were directly or indirectly bound for markets outside of the region.<sup>68</sup> This economic reliance makes the idea of building protectionist regional trades block in East Asia almost equivalent to an economic suicide. Therefore, the first step for an East Asian FTA will not be to pursue a self-contained market, but rather to establish a complementary regional market on top of existing global export destinations.

#### b. Financial Security

On top of trade facilitation, the East Asian Community can also serve functions of financial surveillance and cooperation. It can fill the gap void left by the IMF, which lacks speed

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<sup>67</sup> Munakata, 2006, pp. 29.

<sup>68</sup> Economic Policy Department, Monetary Authority of Singapore, *Macroeconomic Review 2* (January, 2003): 64-65. <[www.mas.gov.sg/resource/download/MRJan2003\\_upload.pdf](http://www.mas.gov.sg/resource/download/MRJan2003_upload.pdf)>

and flexibility in handling financial difficulties specific to East Asia as demonstrated by disastrous IMF prescription of the Asian financial crisis via the ‘structural adjustment policy.’

The main concern shared by East Asian countries is to avoid a similar financial crisis to that experienced in 1997. Many initiatives have been proposed so far to address this common concern.

These are founded on three major goals:

- Creation of a regional liquidity support facility through the Chiang Mai Initiative;
- Establishment of economic surveillance, particularly through the ASEAN + 3 Economic Review and Policy Dialogue process; and
- Development of Asian bond markets.

First, Chiang Mai Initiative (CMI) was introduced at the ASEAN+3 Finance Ministers’ Meeting in Chiang Mai, Thailand, in May 2000. It was the first regional financing agreement aimed to establish a network of currency swaps to help members deal with future crisis. The thirteen member countries agreed to set up bilateral exchanges of hard currency reserves. This liquidity support facility was designed to manage regional currency attacks and contagion effects, thus defending member economies from “speculative attacks and avert liquidity crisis stemming from unexpected outflows of foreign capitals.”<sup>69</sup> The CMI is comprised of two elements—the expansion of the existing ASEAN Swap Arrangement (ASA) – augmented to US \$1 billion- and the creation of a new network of bilateral swap arrangements (BSAs) among ASEAN + 3 members. Two member states in particular, China and Japan, were expected to be regional anchors in this currency-swap scheme with their monumental foreign-exchange reserves. By 2007, they had reserves of \$1.2 trillion and \$900 billion respectively.<sup>70</sup> In 2007, East Asia as a whole had the world’s largest reserves at about \$3 trillion, or roughly two-thirds of the world’s

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<sup>69</sup> Gill, Huang, and Kharas, editors, 2007, pp. 38

<sup>70</sup> Hisane, Masaki, “Japan, China as anchors of financial stability,” Asia Times Online, May 8, 2007. [http://www.atimes.com/atimes/Asian\\_Economy/IE08Dk01.html](http://www.atimes.com/atimes/Asian_Economy/IE08Dk01.html)

total.<sup>71</sup> By pooling these reserves together to guarantee financial stability in the region, Chiang Mai initiative could be seen as a concrete step towards the creation of an Asian Monetary Fund—a quashed proposal due to fierce objection from the IMF and the US in 1997. But the CMI initiative still has much room for improvement. One noticeable short-fall of CMI is that members could only receive 10 percent of short term financial assistance requested directly from the fund; the remaining 90 percent is provided to the requestor under the IMF supervision and its tough conditionality such as the “structural adjustment policy.”<sup>72</sup> East Asian governments should gradually increase the percentages of the award directly from the CMI assistance fund, and reduce the reliance on the IMF supervision of the CMI fund over time.

Secondly, efforts to improve regulation and supervision in the financial sector had also been made via ASEAN+3 Economic Review and Policy Dialogue (ERPD). Introduced in 1993, it was by far the region’s most advanced and prominent forum which aims to manage the risks involved with increased capital flows and provide an early warning of potential crisis.<sup>73</sup> Region-wide surveillance was crucial as financial trouble in one country can elicit massive investor panic and spill over to neighboring countries as shown in 1997 crisis. Thus, ERPD was a valuable avenue to collect timely and reliable data and conduct objective analysis of member economies’ conditions, risks and vulnerabilities. It could also identify various policy options to reduce risks and irregularities. ERPD works through mutual monitoring and sharing of information on short-term capital movements in the vicinity among East Asian countries. Moreover, it facilitated exchanges of views, and collaboration on financial, monetary, and fiscal issues based on

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<sup>71</sup> Ibid.

<sup>72</sup> Kawai, Masahiro, 2005. “East Asian economic regionalism: progress and challenges” *Journal of Asian Economics*, Elsevier, vol. 16(1), pages 25-55, February.

<sup>73</sup> Kawai and Houser, “Evolving ASEAN+3 ERPD: Towards Peer Reviews or Due Diligence?” Discussion Paper 79. Asian Development Bank Institute  
<http://www.adbi.org/discussionpaper/2007/09/20/2363.asean3.regional.financial.cooperation/asean3.economic.review.and.policy.dialogue/>

common interests in general.<sup>74</sup> ERPD was currently studying an effective mechanism to encourage the country in trouble to take appropriate policy actions. On the whole, it was gradually evolving into a centrally administered regional financial forum that can ultimately be more independent of the IMF. One clear benefit of a successful ERPD process would be *lessening of financial burden to stock up huge foreign currency assets*. The memory of the Asian crisis encouraged several East Asian countries to develop self-assurance arrangement against the potential currency crisis. They had accumulated large foreign exchange reserves, mostly in U.S. Treasury bonds, at high cost: low interest rates accrued to the bonds and the decline of the dollar. With improved financial security through cooperative forum such as ERPD, countries could afford to invest their savings to more productive fields.

Thirdly, initiatives have been taken to further develop Asian bond market in order to channel a vast pool of savings to long-term investment for growth within East Asia. This effort intends to reduce the dependence on external financing based on foreign-currency, encouraging development of national and regional capital, especially bonds, and markets. Such an effect can mitigate the “double mismatch” problem prevalent in East Asian capital market prior to the Asian financial crisis; most of the debts were denominated in foreign currency and had short term-maturity, resulting in a dangerous mismatch for financing long-term projects. In 2003, ASEAN+3 launched the Asian Bond Markets Initiative to provide the much-needed infrastructure for a well-functioning regional bond market.<sup>75</sup> The initiative includes two types of markets: (1). Asian Bond Fund I invests in dollar-denominated bonds and limited access to East Asia-Pacific Central Banks (EMEAP), which is a group of the eleven central banks and monetary authorities of Australia, China, Hong Kong, Indonesia, Japan, Korea, Malaysia, New

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<sup>74</sup> Ibid.

<sup>75</sup> Gill, Huang, and Kharas, editors, 2007, pp. 123

Zealand, the Philippines, Singapore, and Thailand. (2). Asian Bond Fund II, introduced in 2005, invests in local-currency-denominated bonds and is accessible to private investors.<sup>76</sup> Financial ministers of member countries aim to further develop the second type of regional bond market as it can successfully resolve the “double mismatch” problem by issuing bonds denominated in a basket of Asian currencies. Establishing infrastructures like regional bond guarantee agency and the regional rating agencies can make improvement to Asian bond market.<sup>77</sup>

### c. Exchange Rate Policy Coordination

The third economic benefit of establishing the East Asian Community is that it can provide institutional support to maintain intra-regionally stable exchange rates. A step-by-step approach to regional exchange rate policy is recommended, as there is no such coordination in the region as of now. The idea of establishing joint-exchange rate stabilization arose because, even though the region has around \$3 trillion in reserves, economic activities are mostly conducted in non-regional currencies, particularly the U.S. dollar. This dependence makes the Asian economy susceptible to fluctuations in the dollar exchange rate to domestic currencies.

Once the region exhibits greater economic and political convergence, a multi-track discussion of constructing a basket of regional currencies of the ASEAN+3 countries can begin. The weights of the regional currencies in the basket would reflect the relative economic importance of each country in the region, and a common Asian currency unit can be derived in that way which can be used to “denominate economic transactions (trade and capital flows) and asset stocks (foreign exchange reserves and cross-border bonds), as well as to measure the degree of each currency’s exchange rate deviation from the regional average.”<sup>78</sup> Ultimately, this movement will improve coordination of regional economic policies and intra-regional exchange

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<sup>76</sup> Gill, Huang, and Kharas, editors, 2007, pp. 63

<sup>77</sup> Kawai, M. (2005)

<sup>78</sup> Gill, Huang, and Kharas, editors, 2007 pp. 64

rate stability. Establishing a common basket of currencies seems more realistic in the near future than choosing yen or yuan as the region's monetary anchor. The yen's power is expected to decline along with Japan's declining relative economic size and import absorptive capacity in comparison with Chinese Yuan's. Despite of its growing international role, the *yuan* is also not ready to become the monetary anchor because many Asian economies with open capital accounts find the yuan to possess limited usefulness in international settlement, clearance, financing and liquidity holding.<sup>79</sup> Hence, the Asian Development Bank is currently studying the idea of a "notional composite currency unit" that would be a representative indicator of Asian currencies as the first step to coordinate exchange rates in the region, instead of pursuing one regional monetary anchor.<sup>80</sup>

### Conclusion

The role of the financial crises testifies the economic need of the EAC. Establishment of an East Asian Community can yield many economic benefits derived from increased financial cooperation. Initiatives including a region-wide system of currency swaps, financial regulatory body, and Asian bond market can all help members deal with future financial crises. Institutionalized regional cooperation cannot only advance on-the-ground intraregional trade, but it can also coordinate 'safe' financing of the vast production network and investment opportunities. Common currency baskets and joint crisis intervention arrangements can potentially replace both the risky dollar pegs of the past, and the reliance on the U.S.-led international monetary organizations. The establishment of the AIIB East Asian Community is expected to be the new driver of economic growth by complementing global and national efforts.

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<sup>79</sup> Kawai, Masahiro. "The Role of an Asian Currency Unit for Asian Monetary Integration," Asian Development Bank Institute, paper for conference "Beyond Breton Woods: The Transnational Economy in Search of New Institutions," held in Mexico City on 15-17 October 2008.

<sup>80</sup> Ibid.

### **3. Political Challenges in the *pre-crisis* East Asia**

The economic benefits of building a regional institution to advance the production, trade, and investment network foundations are clear. An East Asian Community can be useful in managing regional issues (particularly in regards to finance) that have arisen from this increased economic interdependence and also in developing bargaining power with global institutions and governments, especially the U.S. and the European Union. Considering that China is a regional hegemon, what are the political challenges that East Asian leaders are experiencing in advancing to the creating of the EAC? What inhibits the establishment of the EAC? Serious *political* efforts towards regionalism only took off after the 1997-98 Asian financial crisis. I argue that the aspirations for building multilateral regional institution are constrained by political realities that existed in East Asia of the pre-1997 financial crisis. There are four main political challenges lying at the pathway: diversity, rivalry between China and Japan, South Korea, and ASEAN countries, Cold-war structure, and the U.S. opposition.

#### 3.1 Diversity

From military-ruled Burma, with a per capita income on par with sub-Saharan Africa, to democratic Japan, the world's second-largest economy, diversity and heterogeneity are indeed the leitmotif of East Asia. East Asia's diversity and heterogeneity in social, economic, political developments stood as formidable barriers against collective state-led regional efforts. Socially, countries differ from each other widely with their Sinic, Shinto, Islamic, Buddhist, Muslim, Confucius, and Christian traditions. East Asian citizens remain highly diverse on normative identities, including religious, ethnic, linguistic and cultural self-definitions. Economically, countries differ widely in per capita incomes, industrial and financial structures, institutional and

human capacities, trade openness and patterns, scope and extent of exchange and capital controls.<sup>81</sup>

The gap between low- and high-income countries has constituted an impediment to state-driven regionalism in East Asia as they have different economic policy objectives and priorities. The developmental gaps among the partners of NAFTA and the European Union were much smaller than those within East Asia. The U.S. per capita income at the time of NAFTA inception was six times that of Mexico. Similarly, Luxembourg's per capita income was 16 times larger than that of Turkey when Turkey entered into a customs union with the EU at the beginning of 1996.<sup>82</sup> In East Asia, by contrast, Japan's nominal per capita income (approx. \$40,000) was fifty times larger than that of Cambodia (approx. \$782) in 2009.

On top of economic developmental differences, East Asian states differ from each other on other criteria of national capabilities. Prof. Paul F. Diehl of the University of Illinois has compared the power distributions among members of the ASEAN+3 regional grouping with members of the EU using the latest figures from 2001. National capabilities are measured along three dimensions with two indicators each: military (expenditures and personnel), economic (iron/steel production and energy consumption), and demographic (total and urban population). Table 1 provides a measure of the relative symmetry of group members for each of these six indicators as well as for a composite measure (equally weighted aggregation of the six indicators): this is the ratio of the value or score for the largest state in the group to the smallest state. The greater the ratio, the more asymmetric is the regional association. The finding of the table below shows that ASEAN+3 has more asymmetric power distributions than the EU.

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<sup>81</sup> Kawai, M. (2005)

<sup>82</sup> Munakata (2006), pp. 32

TABLE 1 Power/National Capability Ratios\* ATP and EU (2001)

Indicator	APT	EU
Composite	830.87	651.24
Military Expenditure	2,423.63	1446.42
Military Personnel	385	308
Energy Consumption	4,927.31	575.11
Iron/Steel	152,260	44,803
Total Population	3,895.35	211.36
Urban Population	240,091	52,930

\*Ratio is the largest state vs. the smallest state in the groups

Source: Diehl Paul F. "Can East Asia be Like Europe? Exploring Selected Conditions for Regional Integration" in *The Emerging East Asian Community*. Kuala Lumpur: Penerbit University, 2006, pp. 51. Originally calculated from data at <<http://correlatesofwar.org>>

Politically, the institutional differences have made it difficult for East Asian economies to enforce institutional frameworks. A mixture of democracies, dictatorships, capitalist tax havens and communist states led to very little agreement on the fundamental principles of regional institutional structure in East Asia.

In analyzing different regime types, I adopt the Polity IV Project scale of democracy-autocracy used by Prof. Paul F. Diehl, where the scale is designed that ranges from *negative* 10 (pure autocracy) to *positive* 10 (pure democracy) and it reflects the public participation in a state's political institution. Diehl uses the standard for democratic states with scores of positive 6 or 7. According to this scheme, all EU member states are considered to be democratic. However, the results are less uniform with respect to the ASEAN+3 members. Only five (Indonesia,

Philippines, Thailand, Japan, and South Korea) of the thirteen states are considered democratic countries. Other states fall in wide spectrum from score of -9 to +4.<sup>83</sup>

One and whole, lack of symmetry in social, economic, and political capabilities across member states have remained as an impediment to reaching political consensus for regional integration in East Asia.

### 3.2. Rivalry between China and Japan

Another main political challenge that hindered governmental efforts towards regionalism is the intense antagonism between China and Japan. The Sino-Japan relationship has been going through a difficult period for two reasons: One is the unsolved historical issue from Imperial Japan's wartime crimes and the apparent denial by rightwing Japanese of the crimes in the past. Another one is growing Japanese anxiety of its declining economic and political power position as compared to China's in the world. These political hardships that exist between the two regional powers have blocked them from reaching a reasonable level of mutual trust in most part of the 20<sup>th</sup> century. Although the two countries have seen expanding trade and investment ties, membership in formal bodies, and informal links including joint military visits and exchanges of top government officials, the two political challenges work against the creation of deeper and more formalized regional links.

On the first point, distrust resulting from Japanese imperial crimes before and during the Second World War runs deep and wide. As late as in 2002, an opinion poll conducted by the Institute of Japanese Studies at the Chinese Academy of Social Sciences reported 43.3 percent of the Chinese respondents thought Japan 'unfriendly.' The polls also showed that 53.5 percent of respondents answered the Japanese military invasion of China as their first image of Japan. On

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<sup>83</sup> Diehl, Paul F. (2006) pp. 51

the other hand, the number of Japanese respondents who think China ‘unfriendly’ reached 48.4 percent in Japan.<sup>84</sup>

China’s negative perception of Japan is largely based on Japan’s war crimes during the period of Japanese imperialism. In *War without Mercy*, John W. Dower explains several broad categories that characterized Japanese atrocities:

“massacres of noncombatants, the maltreatment and killing of prisoners, routinized torture, forced labor, and institutionalized murder in the form of lethal medical experiments operated... on a large scale in Manchuria (under the murderous contingent of scientists known as “Unit 731”)<sup>85</sup>

From the late 19<sup>th</sup> century to the defeat of the Empire of Japan in 1945, Japanese military forces were responsible for killings and other crimes against millions of civilians all across East Asia. According to the historian Chalmers Johnson, the Japanese killed as many as 30 million Filipinos, Malays, Vietnamese, Cambodians, Indonesians, Burmese, Chinese, and Koreans. Japan also plundered the countries it conquered on a monumental scale; it took away not only natural resources but also people, enslaving millions and exploiting them as forced laborers – sometimes as ‘comfort women’ who were forced to serve as prostitutes for front-line troops.<sup>86</sup> Japanese imperial atrocities are comparable to that of Nazi Germany that killed six million Jews and 20 million Soviet citizens. However, the difference lied in their post-1945 efforts for reparations. The German government made serious gestures towards restitution, paying more than \$45 billion in compensation so far. Japan, on the other hand, had given its victims a meager

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<sup>84</sup> Yang, Jian. "East Asian Community: surmounting the history issue: Jian Yang discusses the significance of identity and historical differences in regional integration." *New Zealand International Review*. 32.6 (Nov-Dec 2007): 10(4). *Expanded Academic ASAP*. Gale. 29 September 2009

<sup>85</sup> Dower, John W. (1993, c.1986) pp. 42

<sup>86</sup> Johnson, Chalmers. “The Looting of Asia.” *The London Review of Books*. Vol. 25 No. 22. 20 Noveber 2003, [www.lrb.co.uk/v25/n22/chalmers-johnson/the-looting-of-asia](http://www.lrb.co.uk/v25/n22/chalmers-johnson/the-looting-of-asia).

\$3 billion, while compensating its own Japanese nationals around \$400 billion for war losses.<sup>87</sup> Thus, there was a widespread perception in East Asia that the Japanese government had not accepted the legal responsibility for fully compensating individual victims of Japanese atrocities. Many people were also aggrieved by the fact that the official apologies from the Japanese government have merely expressed “regret” or “remorse.”<sup>88</sup> This view was further strengthened by an incident on October 2006, where more than eighty Japanese lawmakers from the ruling Liberal Democratic Party visited the Yasukuni Shrine – an imperial shrine with thousands of Class-A, B, C war criminals’ enshrinement and a museum honoring Japanese war heroes - while Prime Minister Shinzo Abe expressed an apology for the damage caused by Japanese aggression.<sup>89</sup>

The concept of the Greater East Asian Co-Prosperty Sphere created and promulgated by the imperial Japan in the early 20<sup>th</sup> century had also contributed to the Chinese apprehension towards the Japan-led regionalism in East Asia. The idea heavily influenced Japan’s foreign policy from 1895 (Japan’s annexation of Taiwan) until 1945 (Japan’s defeat in World War II). The goal was that by 1950 Japan would achieve economic self-sufficiency by uniting itself with Manchukuo and Korea as “one link;” some countries in Southeast Asia would join the link to complete Japan’s national defense economy.<sup>90</sup> Japan claimed that Asians were able to achieve “enlightenment and civilization” only via becoming the imperial citizens of the Japanese empire by joining the Sphere. Influenced by social Darwinian racism, Japan also argued that the Sphere

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<sup>87</sup> Ibid.

<sup>88</sup> PBS. Online NewsHour. “I’m Sorry?” December 1, 1998, [http://www.pbs.org/newshour/bb/asia/july-dec98/china\\_12-1.html](http://www.pbs.org/newshour/bb/asia/july-dec98/china_12-1.html).

<sup>89</sup> Johnson, Chalmers.

<sup>90</sup> Armstrong, Charles K. *Korea at the center: dynamics of regionalism in Northeast Asia*/edited by Charles K. Armstrong... [et al.] M.E. Sharpe, Armonk, N.Y.: 2006, pp. 100

was intended to protect the “yellow” race from the “white” race.<sup>91</sup> Japan’s imperial pursuit for geographical and ethnic identity failed due to an innately closed system created by brute military force and racist policies.

On the second point, China’s growing economic, political, and military strengths have certainly led to increasing Japanese apprehension about China’s role in East Asia. China’s active regional diplomacy, especially in Southeast Asia, has helped the country to gradually replace Japan as the key trading partner and an important source for investment and overseas development assistance. Beijing has also committed itself to support the development of ASEAN members through the provision of loans, grants, credit facilities, debt relief, and technical assistance. In addition to state apparatus, China has also urged state-owned enterprises and private entrepreneurs to invest in Southeast Asia.<sup>92</sup> As a result, Japan’s importance as a destination of ASEAN exports experienced a relative decline in comparison to China’s.<sup>93</sup> Similarly, Japan’s investment links with its Asian neighbors have also declined. Furthermore, Japan is apprehensive about China’s growing voice in international political arena as demonstrated by China’s successful opposition to Japan’s bid to become a permanent member of the UN Security Council. Forty-four million Chinese signed a petition against Japan’s bid, prohibiting Japan from expanding its influence and power in the world.<sup>94</sup> Finally, Japan is wary of China’s growing military budget, which has grown approximately 10 percent annually over

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<sup>91</sup> Shin, Gi-wook and Sneider, Daniel C. and Walter H. Shorenstein Asia-Pacific Research Center. *Cross Currents: Regionalism and Nationalism in Northeast Asia* / edited by Gi-Wook Shin and Daniel C. Sneider, Stanford University; Brookings Institution Press, Stanford, CA: Washington, D.C. : 2007, pp. 14

<sup>92</sup> Frost, S. 2004. Chinese Outward Direct Investment in South East Asia: How big are the flows and what does it mean for the region. *The Pacific Review* 17(3): 323-340.

<sup>93</sup> Lincoln, Edward J. and Council on Foreign Relations. *East Asian Economic Regionalism* / Edward J. Lincoln, Brookings Institution Press; Council on Foreign Relations, Washington, D.C.; New York: 2004

<sup>94</sup> Yang, Jian. "East Asian Community: surmounting the history issue: Jian Yang discusses the significance of identity and historical differences in regional integration."

the last fifteen years.<sup>95</sup> In the early 1990s, China tried to use its military strength to intimidate other countries in East Asia, employing aggressive tactics such as sending armed ships to disputed islands in the South China Sea.<sup>96</sup> Such moves by China aggravated Japan's negative perception of China's rising military might.

Because of these conflicts over historical issues and power politics in the region, China and Japan have not been successful in establishing a reasonable level of mutual trust. The acrimony between China and Japan based upon strong nationalist sentiments has posed a real check on the development of political consensus towards East Asian regionalism.

### 3.3. Rivalry between China and South Korea

Besides the conflict between China and Japan, China and South Korea's relationship had been unstable due to the diplomatic relationships of each. To trace China-South Korea relations during the second half of the 20<sup>th</sup> century (1950 – 1992), I will begin by analyzing the two countries' roles in the Cold War structure of the 1950s and 1960s. During these two decades of the post-Korean War period, Sino-Korean relations were the product of the great-power rivalry between the Soviet Union and the U.S. Ideological norms rather than strategic rationale dominated diplomatic relations. Military tensions between Seoul and Beijing were constantly reinforced by the conflicts within the U.S.-Soviet bipolar structure.<sup>97</sup>

In the 1950s, China and North Korea's strategic alignment with the Soviet Union, as well as South Korea and Taiwan's relationship with the United States were both parts of the Cold-War structure.<sup>98</sup> China and South Korea's urgent need for survival was compounded by the

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<sup>95</sup> Office of the Secretary of Defense, Annual Report to Congress 2007: Military Power of the People's Republic of China, p. 25, [www.defense.gov/pubs/pdfs/070523-China-Military-Power-final.pdf](http://www.defense.gov/pubs/pdfs/070523-China-Military-Power-final.pdf).

<sup>96</sup> Kurlantzick, Joshua. "Pax Asia-Pacific? East Asian integration and its implications for the United States" *The Washington Quarterly* 30.3 (Summer 2007): 4(12).

<sup>97</sup> Armstrong, Charles K., edit. *Korea at the Center*. New York: M.E. Sharpe, 2006. p 202

<sup>98</sup> Ibid.

framework of ideological confrontation characterized by “conquer thy neighbor or be conquered by it”.<sup>99</sup> The Korean War was an excellent example of this kind of political atmosphere during that time. The expansion of the Cold War into Asia was manifested in the long, bloody battle between the South Korean force supported by the U.S. and the North Korean force supported by China and the Soviet Union. By late October in 1950, Chinese troops had been secretly deployed to engage with American and South Korean troops. At that time, the top general of the U.S.-Korea forces, General MacArthur, was launching a final drive to unify the whole Korean peninsular. However, his triumphant drive was shattered by the Chinese offensive of 200,000 troops who pushed the American troops back into South Korea. By early 1950s, the total number of Chinese troops in Korea reached 1.35 million.<sup>100</sup> Chinese forces, with their massed formations resembling a “human sea”, proved to be the main source of opposition in the peninsula, and successfully pushed back the advance of U.S.-Korea forces. The heavy resistance from China ultimately led to the signing of an armistice agreement that divided the Korean peninsular along the Thirty-eighth Parallel.<sup>101</sup> The Korean War illustrated the open conflict between the “northern” alliance (the Soviet Union, China, and North Korea) and the “southern” counterpart (the U.S. and South Korea). Therefore, the hostile relationship between China and South Korea during that time was imbedded in a larger global ideological confrontation between the Soviet-led socialist bloc and the U.S.-led capitalist bloc.

During the 1960s, China’s radicalization of communist ideology under Mao brought some changes to the political economic environment in the region. One of the major changes was China’s emphasis on the amicable relationship with North Korea. China, at that time, was determined to go against not only the U.S. but also the Soviet Union. This determination was

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<sup>99</sup> Ibid.

<sup>100</sup> Scott, David. *China Stands Up: The PRC and the International System*. New York: Routledge, 2007. p 27

<sup>101</sup> Ibid.

manifested in China's "self-reliance (zili gengsheng)" principle emphasized during the Great Leap Forward along the line of antagonizing the Soviet Union and also along the line of criticizing the Soviet Union for its pursuit of a "peaceful coexistence" with the U.S.<sup>102</sup> After the Sino-Soviet split, China's radicalization of Communist ideology began to emphasize a bond with North Korea, which went as far as being called an "alliance sealed in blood (xiemeng)".<sup>103</sup> This change further exacerbated China's confrontational approach towards South Korea compared to that of during the 1950s. South Korea responded to China's radicalization of ideology and its increased ties with North Korea (South Korea's archenemy) with a strong anticommunist stance and its amicable relationship with Taiwan (China's archenemy). In January of 1967, South Korean president Park Chung-Hee passed a new Foreign Trade Laws that prohibited all business transactions with Communist countries. This law has effectively blocked economic interaction between South Korea and China throughout the 1960s.<sup>104</sup> South Korea also continued to recognize Taiwan as the sole legitimate government of China and kept its strong alliance with the United States.

During the 1980's, the rapprochement process between South Korea and China reached a new level, signaling a possible meltdown of the diplomatic tensions between the two states that existed in the last three decades. Starting around this time, both nations began to voice interest towards greater economic interaction through bilateral trade. This fundamental shift in foreign policy marked the beginning of a new bilateral relationship in East Asia.

In the early 1980's, Friedrich List's book, *The National System of Political Economy*, had been generating many heated discussions in Chinese academia regarding its path towards

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<sup>102</sup> Ibid.

<sup>103</sup> Armstrong, Charles K., edit. *Korea at the Center*. New York: M.E. Sharpe, 2006. p 204

<sup>104</sup> Freezone: Korea's Political Discussion Website. "President Park Chung Hee and the Discussion about Export." Retrieved from: <http://www.freezone.co.kr/cafebbs/view.html?bid=free&cate=c01&gid=fz&pid=176555> (translation).

modernization, where he argued that the strong state-centered developmental model is needed to “grease the wheels of industrialization,” and that late industrializers cannot afford to just leave their economies at the mercy of the invisible hand of free market.<sup>105</sup> Chinese leaders indeed saw with their own eyes the continuing success of South Korea’s strong state-centered developmental model. During the 1980s, South Korea was experiencing one of the best periods in its economic history, having its GNP (Gross National Product) growth at an annual rate of 9.9 percent and the highest level of trade surplus in Korea’s history (\$8.8 billion).<sup>106</sup> Inspired by Korea’s economic success, China showed its keen interest in learning more about South Korea’s developmental model. Its interest was shown in the establishment of the Chinese Academy of Social Sciences, which had a small research group specifically studying the Korean model with emphasis on the incorporated export-oriented strategy.<sup>107</sup>

China also showed interest in emulating some of the targets for economic development from the Korean model. For example, Deng Xiaoping’s comment to the Central Advisory Commission of the Chinese Communist Party included the projection of quadrupling China’s GNP in 2000 which was closely linked to President Park Chung Hee’s projection figure in South Korea.<sup>108</sup> China’s deep interest in the Korean economic model was one of the reasons for its increasing reception to more economic exchanges with South Korea. The other reason was China’s search for foreign capital and technology. China thought that South Korea could be a beneficial economic partner who would offer both, especially the much-needed intermediate-level technology for the development of heavy industry.<sup>109</sup> This gesture of China’s “opening”

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<sup>105</sup> Hu, Weixing. *China’s International Relations in the 21<sup>st</sup> Century: Dynamics of Paradigm Shifts*. p. 51

<sup>106</sup> Chung, Kae H., Hak Chong Lee, Ku Hyun Jung. *Korean Management: Global Strategy and Cultural Transformation*. New York: Walter de Gruyter. p. 32

<sup>107</sup> Armstrong, Charles K., edit. *Korea at the Center*. New York: M.E. Sharpe, 2006. p 207

<sup>108</sup> Scott, David. *China Stands Up: The PRC and the International System*. p. 78

<sup>109</sup> PIPasset Blog. “International Forum on Korea-China Economic Exchange.” Posted on April, 17, 2008. Retrieved from: <http://cafe.daum.net/pipasset/HML1/101> (translation).

attitude towards economic interaction with South Korea was well received by the Korean government who was relentlessly searching for oversea markets where Korea could sell its exports and utilize the abundant industrial resources which Korea lacked significantly.<sup>110</sup>

#### 3.4. Rivalry between China and other ASEAN member states

Territorial disputes in the South China Sea are one of the most controversial conflicts between China and several ASEAN countries. Territorial dispute is a very sensitive topic in the region, as China becomes a regional hegemony in both military and economic. Besides China, Taiwan, Malaysia, the Philippines, Brunei, and Vietnam claim the Paracel and Spratley Islands. Moreover, Japan, China, and Taiwan claim the Senkaku Islands. The disputed islands are important economically as there is large amount of unexplored oil and natural gas. China and Taiwan are basing their claims based on history while the others with the United Nations Convention of the Law of Sea, where it states that sovereign jurisdiction of the land shall not exceed beyond the 200 nautical miles from the baseline of the shore.<sup>111</sup> In 2014, China's military presence in the region is strong as it imposed fishing permits, including using force against Vietnamese and Chinese naval ships, in the South China Sea.<sup>112</sup> Even though China uses its economic power to leverage the protests of neighboring countries with its territorial claims, the inevitable response of the ASEAN member states in the 2014 ASEAN Summit forced China to be in compliance with the Declaration on the Conduct of Parties in the South China Sea, where it shows that ASEAN member states against China shows that there is a strong cooperation among other countries that are also claiming the islands. Since China is a major trading partner of

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<sup>110</sup> Ibid.

<sup>111</sup> Scott, Snider, "The South China Sea Dispute: Prospects for Preventive Diplomacy", United States Institute of Peace. August 1996. [http://www.usip.org/pubs/specialreports/early/snyder/South\\_China\\_Sea2.html](http://www.usip.org/pubs/specialreports/early/snyder/South_China_Sea2.html).

<sup>112</sup> Branigan, Tania, "Beijing brushes off U.S. criticism of its tough new fishing rules." The Guardian, 10 January 2014.

ASEAN members, unilateral actions may heighten the tension, which may lead to jeopardizing trade partnerships and humanitarian assistance from member states of developing countries.

Economic interdependence promotes effective foreign government connections and economic relationships, which increase the cooperation of governments in promoting prosperous economies. States with strong economies, those that enjoy prosperity and are experiencing economic growth, may be disinclined to fight.<sup>113</sup> They argue that people are inclined to be engaged in military conflict if there is a higher rate of economic growth. The core goal of states with strong economies is economic prosperity than military power. Countries with high economic growth focus more in strengthening their trading partnerships between states because cooperation plays an important role in developing and maintaining economic relations, which means that economic power weighs more than military power. The likelihood of a dispute is much lower when states are dependent on bilateral trade.”<sup>114</sup> A military conflict can jeopardize economic partnerships, which can paralyze the economy of either of the states. Though the military presence of China to the disputed territories is high, it is less likely that military force will be used in claiming the territories as it may affect China’s economic independence with not only with ASEAN countries but also with the international community.

### 3.5. The Cold War Structure

Since the late 19<sup>th</sup> Century, Asia has fallen under the prevailing global and regional influences of the Western powers, colonialism, and military conquests. Following the Second World War, the region’s fragmentation continued in two ways:

#### (a). Decolonization

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<sup>113</sup> Russett, Bruce. *Triangular Peace: Democracy, Interdependence, and International Organizations*. W.W. Norton & Company, Inc: New York, 2001: 126-155.

<sup>114</sup> *Ibid.*

Most countries in East Asia have only gained their sovereignty very recently. Therefore, most governmental efforts went towards national building: “the creation of stable armies and police forces, the consolidation of domestic bureaucratic system and its extractive capabilities, the inculcation of a spirit of national loyalty, the securing of national borders, and the promotion of economic development.”<sup>115</sup> National interests and national identity posed as powerful forces against pressures of regionalism that required relinquishment of some sovereignty of individual nation. Furthermore, a century or more of social, cultural, and political fragmentation hindered reaching commonly agreed-upon goals across the region.

(b). The Cold War

Soon after the end of the Second World War, the onset of the Cold War geopolitical forces has greatly influenced the shaping of diplomatic relations among nations in East Asia. A network of American bilateral security alliances with Japan, South Korea, Taiwan, and later Thailand and the Philippines, had three primary objectives: to maintain a stable balance of power in the region, to contain the military and ideological challenge of the Soviet Union and Communist China, and to ensure commercial access to Asian markets.<sup>116</sup> These U.S. centered pan-Pacific linkages tied these countries economically and strategically to the U.S. and have effectively created the ‘hub–and–spoke’ system; the image of multiple Asian countries all separately linked to the US can be paralleled to the image of many ‘spokes’ connected to the ‘hub’ in a wheel. The US bilateral system was more or less put in place after President Truman approved the large-scale US rearmament envisaged in National Security Council document 68 in 1950. The NSC document called for annual expenditures 300 percent above that originally requested by the Pentagon for

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<sup>115</sup> Pempel, T.J., editor, 2005, pp. 257

<sup>116</sup> Shin, et.al., pp. 259

1950. The bill was swiftly passed in the Congress after the outbreak of the Korean War in that same year.<sup>117</sup>

During the Cold War, East Asia was effectively divided between the American alliance and the Soviet Union-influenced alliance including countries such as the People's Republic of China, North Korea, and North Vietnam. These two separate Cold War-era alliances provided very little basis for the formation of integrated Asia. The divisive residues of the Cold War were manifested by the cleavage of Korea at its midpoint by the U.S. and the USSR and the separation within "greater China." The Cold War had also indirectly induced many territorial border disputes in the South China Sea and internal fragmentation in several Southeast Asian countries as demonstrated by Indochina in the mid-1960s experiencing the Cold War-inspired bloodbath.

### 3.6. The U.S. Opposition

The Cold-War legacy of the U.S. bilateral security alliance restricted exercising a consistent American policy on intraregional cooperation within East Asia. Further, Washington has tried to forestall intra-Asian integration that appeared to exclude the U.S. in fear of losing its balance of power in the region. As a country that has great political and economic influence in the region, the U.S.' strong reaction to the movement towards East Asian regionalism led many Asian government leaders to abandon state-driven regional integration during the 1990s.

Following the disappointing progress of the Uruguay Round Ministerial meeting in December 1990 and emergence of preferential regional trade arrangements in North America, Malaysian Prime Minister Mahathir Mohamad proposed the vision of the East Asian Economic Group (EAEG) concept which called for the formation of a regional trade grouping – comprised of ASEAN countries, Japan, China, Korea and Hong Kong. The Bush administration vehemently

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<sup>117</sup> Arrighi, Giovanni. 2007 *Adam Smith in Beijing: lineages of the twenty-first century*/ Giovanni Arrighi Verso, London: New York, pp. 176.

opposed to this proposal on the grounds that it was promoting the notion of a *restrictive trading bloc* not consistent with General Agreement on Tariffs and Trade (GATT).<sup>118</sup> In response to the American reaction, Malaysia changed the name of the proposal to the East Asian Economic Caucus (EAEC) after consultation with other ASEAN members in October 1991, and it made clear the nature of the group to be a *loose* form of regional forum on regional economic issues, *not an institutionalized entity nor a trading block* to which the U.S. objected.<sup>119</sup> Despite the effort to avoid any misinterpretation of the proposal, American opposition remained. In November 1991, Baker was asked to provide specific reasons behind the U.S. objection to the EAEC. He answered; “We would have absolutely no objection whatsoever, none in the world, to a free trade agreement that was consistent with the GATT that embraced the same membership as was contemplated for the EAEC... But a consultative or policymaking body, that is, a regional sub-grouping that draws the line down the Pacific... would (undermine the effectiveness and the efficacy of APEC, to which the U.S. is part of).”<sup>120</sup> U.S. Secretary of State James Baker made further controversial comments in a behind-the-scenes American campaign against the EAEC proposal. According to an article from *Washington Post* entitled “U.S. Lobbies against Malaysian Trade Plan,” Baker “unusually blunt admonition” to South Korea’s foreign minister Lee Sang Ock regarding the Korean government opinion of the Malaysian plan. He later noted, “My message was simple: All the countries are *not* equal. The South Koreans got it, and did not press for an EAEG.”<sup>121</sup> After hearing Baker’s account of the U.S. opposition to the plan, many Asian leaders thought that Washington was using double standards; the U.S. welcomed the

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<sup>118</sup> Munakata, 2006, pp. 72

<sup>119</sup> Ibid.

<sup>120</sup> Text of Joint Ministerial Press Conference, Third AEC Ministerial Meeting. As released by the U.S. Department of State, Office of the Assistant Secretary/Spokesman, Shilla Hotel, Seoul, Korea, Federal News Service, November 14, 1991.

<sup>121</sup> Munakata, 2006, pp. 211

creation of NAFTA but not EAEC, which called for a much looser form of regionalism than NAFTA did. This reasoning of the U.S. diplomatic action inevitably left uncomfortable feelings among Asian nations; they wondered why the U.S. had to restrict their freedom to meet and talk with other country leaders.

Instead of the East Asian Community, the Obama Administration is pushing towards the Trans-Pacific Partnership (TPP), which is a trade deal between the United States, Latin America, and Asia. Obama stressed that “if we don’t write the rules, China will write the rules out in the region... we will be shut-out that will mean a loss of U.S. jobs.”<sup>122</sup> Besides the economic incentive of the TPP, Obama’s push towards the partnership is a political strategy of the administration. Power distribution is one of the major concerns for the United States as China becomes politically involve in international organizations. Moreover, as its economic prosperity continues to increase, China's influence in the international community continues to grow. As China expands its influence in East Asia, Africa and part of Western Asia, the U.S. fears that it will affect global order.

In terms of international order, liberals argue that the rising powers will use their growing influence in order to reshape the rules to serve their interests, where the declining power will see the rising power nation as a security threat. Even though some scholars argue that China will be unlikely to use force during the transition of power, the U.S should strategize its policies in order to maintain its power. The United States should build an effective international order by focusing more in strengthening its policies on foreign assistance rather than military force. In a liberal perspective, the United States should continue to encourage free trade particularly to developing countries. Moreover, it should also provide financial and educational assistance to developing

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<sup>122</sup> Feib, Gerald. “Obama Presses Case for Asia Trade Deal, Warns Failure Would Benefit China” The Wall Street Journal. 27 April 2015.

economies particularly in East Asia, where China is trying to build partnerships to East Asian countries to build effective relationships with its neighbors. The U.S. Government should strengthen its Peace Corps and USAID programs because they are effective and valuable programs in establishing partnerships with other countries.

Besides strengthening the United States' policy in foreign assistance, it should assist rising nations in strengthening international security policies during the transition of power. The U.S. has influenced China's multilateral policies in bringing security in the East Asian region. Xuefeng states "China and the United States collectively applied pressure upon North Korea... to surrender its nuclear weapons and terminate its nuclear tests."<sup>123</sup> This action shows the partnership of China with the U.S. government in terms of regional security. China and North Korea are allies in the region, but the action showed by the Chinese government shows that there is a limitation within the alliance when global order is at risk.

According to Shambough's article on containment and engagement in China, "the PRC (People's Republic of China) is unwilling to use force to achieve its aims in Asia. China's preferred tactics is to command respect and obeisance through patronage and preponderant power."<sup>124</sup> As the China's economic power continues to grow, we will see its strong influence in the international arena. Its involvement in international organizations will more like to increase. Moreover, other states will show their respect and promote effective alliances with China. Military conflicts, on the other hand, are less likely to happen because the role of economic interdependence and international organizations are very strong. Though it will be very difficult

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<sup>123</sup> Xuefeng, Sun. The efficiency of China's multilateral policies in East Asia . *International Relations of the Asia-Pacific*, 2010, 515-541.

<sup>124</sup> Shambaugh, David. Containment or Engagement of China? Calculating Beijing's Responses. *International Security* , 1996. 180-209.

for China to adopt the Western style of leadership because of cultural differences, the Chinese government will be able to perform its responsibilities as a superpower nation.

### Conclusion

This chapter asked for the political challenges that the EAC may experience prior its establishment. I looked at the various sets of political challenges that have obstructed and may still be affecting the forming of an intra-regional cooperative body such as EAC in pre-1997 crisis East Asia. Those challenges were: differences existing in the political, economic and cultural atmosphere of East Asia, prevailing Cold War alliances leading to regional fragmentation, historical animosity between Asian powers (China, Japan, and South Korea), and the U.S. confrontation with the idea of an EAC. Based on the analysis in this chapter, I found out that the major cause of these political challenges is the influence of the U.S. to the two major players (Japan and South Korea). Because of strong opposition from the U.S., which was suspicious of Mahathir's protectionist disposition along with ambivalence from Japan and many other East Asian countries (they did not want to jeopardize their bilateral relations with the US), interest in the EAEG/EAEC proposal died out eventually.<sup>125</sup> The failure of the EAEC plan left a long-lasting impression that Washington was simply against an EAEC that did not include the U.S, and that it assumed such forum would *always* work against the U.S. interests.

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<sup>125</sup> Zhang, Yumei. (2002) pp. 142

#### 4. Overcoming Political Challenges

Over the past twenty to thirty years, many of the previous political and cultural barriers against East Asian cooperation have disappeared and the region's economic, political leverage within the world grew. Considering this, how realistic is regional integration in East Asia having China being a major political player?

Today's broader political economic climate became more conducive to *state-driven* regional cooperation. Due to the expanding regional trade networks promoted by Japan's "flying geese" economic investment model and the shock wave caused by the 1997 Asian Financial Crisis, Asian political leaders today recite the slogans of regional unity and harmony. Thus, at the 1999 ASEAN +3 meeting, Philippine President Joseph Estrada spoke of "the dream" of "an East Asian Common Market, and East Asian currency and one East Asian community." The South Korean president talked of the need to find ways to "nurture East Asia into a single community of cooperation" and to promote an "East Asian Economic Cooperation System." The Chinese premier indicated his preference for "closer East Asian cooperation" to "strengthen and deepen" what he called this "effective dialogue mechanism."<sup>126</sup> In his speech to the General Assembly of the United Nations in 2009, then-newly elected Japanese Prime Minister Yukio Hatoyama claimed that building an East Asian community is on top of his agenda as "there is no way Japan can develop without deeply involving itself in the Asia and the Pacific region."<sup>127</sup> There are four developing political realities that have helped to generate an awareness of regional commonalities and the need for a regional institution:

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<sup>126</sup> Pempel, T.J., editor, 2005, pp. 259

<sup>127</sup> Ministry of Foreign Affairs of Japan, "Address by H.E. DR. Yukio Hatoyama Prime Minister of Japan at the Sixty-fourth session of the General Assembly of the United Nations," Sep. 24, 2009. Source: [www.mofa.go.jp/policy/un/assembly2009/pm0924-2.html](http://www.mofa.go.jp/policy/un/assembly2009/pm0924-2.html)

1. Rising cosmopolitan middle class who share similar mind-set thanks to the expanding pan-Asian collaborative cultural production network;
2. Signs of increasing cooperation between China and Japan, South Korea and ASEAN countries.
3. Transition to post-Cold War political structure in East Asia; and
4. Possibility of the U.S. co-opting the idea of an East Asian community.

#### 4.1 Diversity → Homogeneity

Growing economic integration spurred by East Asia-wide trade and production networks has not only brought down the costs of cross-border business and transaction costs, but also helped to promote increasing intra-regional contacts within East Asia. We have seen an increasing density of social communications in East Asia in areas such as telephone and mail communication, shipping and aviation, tourism, television and satellite broadcasts, and legal and illegal migration.<sup>128</sup> This social network has generated pan-Asian cultural commonalities and new perceptions of community at the popular, rather than the elite, level.<sup>129</sup>

The implications of this growing pan-Asian satellite networks are two-folds. First, rising urban middle classes across East Asia have begun to share a similar mind-set via consuming increasingly homogenous pop-culture goods. In television and music, the sweeping fever for Korean pop culture, dubbed “Korean wave” or “Hallyu,” has enjoyed large popularity across China, Japan, and Southeast Asia starting in the late 1990s. The Korean TV dramas such as *Winter Sonata*, *Full House* and *Dae Jang Geum* have helped the total exports of Korean cultural

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<sup>128</sup> Cohen 2002, Cohen, Stephen S. 2002. “Mapping Asian Integration: Transnational Transactions in the Pacific Rim.” *American Asian Review* 20, 3 (Fall): 1-30.

<sup>129</sup> Deutsch, Karl W. 1966. *Nationalism and Social Communication: An Inquiry into the Foundation of Nationality*. 2<sup>nd</sup> ed. Cambridge, MA: MIT Press

products to reach over \$20 billion in 2005.<sup>130</sup> These Korean TV dramas greatly appealed to local audiences, thanks to cultural affinities Korea shared with other Asian countries. In China, dramas starring actor Ahn Jae-wook and actress Kim Hee-sun long dominated the primetime airwaves. In Vietnam, Korean actor Jang Dong-gun and actress Kim Nam-ju have reached the status of national celebrities; the Korean government even felt compelled to invite them to an official dinner for Vietnamese President Tran Duc Luong during his state visit to Korea in 2001.<sup>131</sup> The Korea wave was further bolstered by Korean pop music, which appeals to young local fans with dynamic rhythms, flashy dance moves, and heart-throbbing lyrics. A Korean idol group, Tohoshinki, the most popular K-pop group in Asia nowadays, has broken plenty of records in Japanese music industry, topping Japanese Oricon charts' daily, weekly, and monthly rankings. The release of their twenty-ninth single, "Break Out!" in 2010 made them the first foreign artist to have seven number-one singles on the Oricon. Another album "Best Selection 2010" reached double platinum status in Japan, selling more than 500,000 copies in mere 11 days after its release.<sup>132</sup> Japanese popular culture has also attracted millions of people across Asia. J-pop dominates much of Taiwan's music market as demonstrated by Hikaru Utada, a Japanese female singer, who sold millions of copies in Taiwan. Another Japanese idol singer, Noriko Sakai, sells more albums in Asia than in her home country. She sold over 6.5 million albums in Asia, and became a familiar face from her participation in TV dramas, commercials for Panasonic and Canon corporations, and concert tours throughout Asia.<sup>133</sup> Another popular facet of J-pop is

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<sup>130</sup> Kim, Sue-young, "Korean wave 'Hallyu' abroad waning," *The Korea Times*, May 5, 2008.

Source: [www.koreatimes.co.kr/www/news/special/2008/05/180\\_23641.html](http://www.koreatimes.co.kr/www/news/special/2008/05/180_23641.html)

<sup>131</sup> Korean pop culture sets pace in East Asia; Cultural affinity, (2002, June 28). *Korea Herald*, p.1. Retrieved March 31, 2010, from International Newspapers. (Document ID: 130272131).

<sup>132</sup> Hicap, Jonathan M., "TVXQ'S 'Best Selection' hits Double Platinum in Japan," *Manila Bulletin Publishing Corporation*, March 12, 2010.

Source: [www.mb.com.ph/articles/247374/tvxq-s-best-selection-hits-double-platinum-japan](http://www.mb.com.ph/articles/247374/tvxq-s-best-selection-hits-double-platinum-japan)

<sup>133</sup> Steve McClure. (2000, January). Japanese pop sweeps across Asia. *Billboard*, 112(2), 42, 86. Retrieved March 31, 2010 from Platinum Periodicals. (Document ID: 47721414).

animation and character industry. The mega-popular Pokemon and Japanese toymaker Sanrio's "Hello Kitty" have achieved iconic status across Asia as the prime example of cuteness.

Second, as Asian youth are beginning to find cultural icons in their own backyards, new industries based on Asia-wide collaboration advertise and market the cultural products geared towards the Asia's urban middle classes. Thus, pan-Asian satellite networks not only finds increasing homogenization of popular culture in the region, but it also finds cultural production networks spread across East Asia in film, television, print, video games, and radio industries. In film, directors such as South Korea's Ji-woon Kim and Thailand's Pen-ek Ratanaruang, have collaborated on various pan-Asian productions such as "Last Life in the Universe."<sup>134</sup> Released in 2006, the movie "Battle of Wits" was based on the Chinese Three Kingdom history depicted in a popular Japanese Manga, and it was later created into a movie by a director from Hong Kong. The movie also has two influential Korean actors as important characters. In television, the Japan Broadcasting Co. (NHK), Japan's equivalent of Britain's BBC, started to collaborate with other countries' news agencies to air regional events/issues in sports, fashion, music and culture. MTV Asia, broadcasted by Star TV of Hong Kong, began airing programs highlighting the best regional album and music video by compiling popularity ratings of each Asian artist in East Asia. Other forms of art are also produced by Asia-wide collaborative efforts. Asian art biennales and new Asian art museums typically feature regional themes, and open exhibitions in different places of Asia every year.<sup>135</sup> A pop operetta titled "Nagrland" featuring a theme about breaking away from Western culture to pursue an Asian identity, debuted across East Asia. A

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<sup>134</sup> Robert Albritton and Thawilwadee Bureekul, "Social and Cultural Supports for Plural Democracy in Eight Asian Nations: A Cross-National, Within-Nation Analysis," *Asian Barometer Working Paper Series*, no. 31 (2005),

<sup>135</sup> Hanna Kite, "Arts and Minds," *Times*, September 25, 2006, p. 70  
Source: [www.time.com/time/magazine/article/0,9171,1535867,00.html](http://www.time.com/time/magazine/article/0,9171,1535867,00.html)

Japanese producer, an Indonesian director, a Singaporean costume designer and a Malaysian choreographer created the musical.<sup>136</sup>

The ‘cosmopolitan culture school’ argues there are distinctive responses of a region to universal processes such as globalization.<sup>137</sup> The “Asianization” of pop culture is an example of how East Asia is weaved into broader consumerist and economic trends worldwide while it still fosters some sense of East Asian distinctiveness. Today, this phenomenon yields large impact as more than half of the region’s population is comprised of people under the age of twenty-four who are the most active consumer group of pop culture. The distinctive development of consumer/production pan-Asian network of pop culture is inherently different from globalization phenomenon in other countries; it is a form of regionalism. Why is that Korean dramas and TV shows yet to have found a large audience outside of Asia, such as North America for example? How about various Asian singers who topped every Asian music sales record eventually end up in a mediocre place in Billboard chart when they enter the U.S. music market? There must be some special elements to why Asian pop-culture circulates around and succeed within Asian sphere but not so well in other regions of the world. The reasons for its rather limited success can be cultural affinity and familiarity to the values (e.g. Confucian or Buddhist) ingrained in the Asian pop-art *or* economic ease of circulating the cultural items within the region thanks to the vast collaborative pan-Asian cultural production networks. Regardless of what the reason is, the expanding social network of Asian pop-culture has helped to cement links between Asia’s rising urban middle classes, and decrease the sense of fragmentation that once divided East Asia. The task now is to keep up with the trends of cultural and economic integration in East Asia, and

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<sup>136</sup> Teresa Watanabe. “Toward a new Asian order: a word report special section, culture in the East, pop audiences gets icons of its own.” *Los Angeles Times*, May 19, 1992, p. 2. Retrieved March 31, 2010 from Los Angeles Times. (Document ID: 61622288).

<sup>137</sup> Pempel, T.J., editor, 2005, pp. 208

prepare regional institutions (e.g. an East Asian Community) to give space entitled to the emerging cosmopolitan generation of Asians.

#### 4.2. Rivalry between China and Japan → Signs of Increasing Cooperation

There are signs of historical and territorial tensions easing between China and Japan, thus creating opportunities to overcome the ghosts of a troubled history and move forward East Asian integration. Economic and political motivations have set the tone for closer bilateral relationship. Japan has been China's biggest trading partner, surpassing the United States. In 2006, Sino-Japan trade surpassed \$200 billion, and the total Japanese investment in China has reached \$58 billion in the same year.<sup>138</sup> The grounds for cautious optimism in increasing interdependence between two countries are based on the realization that both countries can take in monumental economic political benefits by promoting cooperation based on mutual economic, security interests. In order to do so, building trustworthy relationship by resolving counterproductive historical/security issues is essential.

There were several noteworthy changes that took shape of developing trend of Sino-Japan cooperation. First, China's attitude towards its neighbors has also taken dramatic shifts to adopt a new priority of regional cooperation. Towards its neighbors, China adopted aggressive foreign policy in 90s especially in regards to issues in South China Sea. In the years after 2000, however, China had turned around as a friendly neighbor, recreating its image as an enthusiastic proponent of Asian integration. New initiatives, such as Boao Forum for Asia, were launched in order to bring together Asian opinion leaders to the common development goals in informal summits.<sup>139</sup> The Chinese government started to lessen its pressure over historical issues in hopes

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<sup>138</sup> Ministry of Foreign Affairs of Japan, Regional Affairs: China, "Building a Mutually Beneficial Relationship Based on Common Strategic Interests" (Pamphlet). February 2010. <[www.mofa.go.jp/region/asia-paci/China/index.html](http://www.mofa.go.jp/region/asia-paci/China/index.html)>

<sup>139</sup> Kurlantzick, Joshua. "Pax Asia-Pacific? East Asian integration and its implications for the United States"

of stopping the continuous deterioration of important Sino-Japanese relations. Jiang Zemin's 1998 visit to Japan was characterized by bitter feelings on both sides after Jiang lectured on wartime past in front of the Japanese emperor. Beijing's foreign policy leaders realized that although a strong position on the issue might serve it well domestically, it could exacerbate Japan's intransigence and further strengthen Japanese right-wing hardliners and resentment against 'apology diplomacy.'<sup>140</sup> This concern formed the basis of Zhu Rongji's efforts to tone down the history issue in his visit to Japan in October 2002. In addition, China announced that it would stop demanding public apologies from the Japanese government.<sup>141</sup> Leaders in Beijing realized that bilateral relation with Japan is crucial for Chinese strategy towards the U.S. In order to promote the concept of 'China's peaceful rise' or 'China's peaceful development,' it was beneficial for China to have a friendly relation with Japan, the major ally of the U.S. in the Far East.

From Japan's point of view, the decline of its conceived importance of the US since the end of the Second World War coupled with rising economic integration with China provided 'a turning point' in renewing Sino-Japan bilateral relation. For decades, Japan's defense and foreign policies had been highly dependent on the US. However, in recent years especially after the September 11 terrorist attacks, the US has been concentrating on the Middle East and its confrontation with the Taliban and al-Qaeda. Japan increasingly feels that its national security was not safeguarded due to the lack of US interest in East Asia. Hence, Japan now seeks more independent relationship with the US to promote its national interests and influence in East Asia. Renewing its sour relationship with China was crucial in its political efforts to (re)integrate with Asia. The new Democratic Party of Japan (DPJ)'s 2005 election manifesto supported the idea of

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<sup>140</sup> Yang, Jian. "East Asian Community: surmounting the history issue: Jian Yang discusses the significance of identity and historical differences in regional integration"

<sup>141</sup> Ibid

an East Asian Community and advances in energy and environment cooperation with major countries in East Asia such as China. Like its Chinese counterpart, Japanese government also tried to avoid historical animosity when it came to strategically improving bilateral relationship. For example, Japan's newly elected Prime Minister Shinzo Abe chose China as his first foreign destination in 2006. China reciprocated Japan's friendly gesture by agreeing to welcome Abe without first obtaining his guarantee not to visit Yasukuni Shrine as the new Prime Minister.

In short, increasing signs of cooperation between China and Japan have arisen out of fear that *cold politics may eventually have an impact on hot economics*. Michael Yahuda, a London School of Economics professor, argues; "there are limits to how far economic inter-dependence between China and Japan can compensate for the 'thinness' of other aspects of the relationship. It is impossible to separate political considerations from economic activity."<sup>142</sup> Aware of this danger, both China and Japan have shown their determination to disentangle security/historical issues, which have bred political distrust. The Japan-China Comprehensive Policy Conference begun in May 2005 at the level of the respective Vice-Ministers of Foreign Affairs. Both countries presented the conference as "an opportunity to engage in a frank exchange of viewpoints and such, from a medium to long-term perspective."<sup>143</sup> It is a big step for both countries to recognize that dialogue can be an effective mechanism for deterring future violence and misunderstanding. Additionally, the two governments set up the China-Japan Joint History Research Committee to work out differences in historical views in December 2006.<sup>144</sup> Such effort is a welcome sign for the development of an East Asian Community, as the concept has been much hindered by the deep-rooted political distrust between two great powers in East Asia.

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<sup>142</sup> Michael Yahuda, 'The Limits of Economic Interdependence: Sino-Japanese Relations,' ISA conference paper, 2001 <[www.isanet.org/zrchive/yahu da.doc](http://www.isanet.org/zrchive/yahu_da.doc),> accessed December 14, 2012.

<sup>143</sup> Shin, et al., 2007, pp. 238

<sup>144</sup> Yang, Jian. "East Asian Community: surmounting the history issue: Jian Yang discusses the significance of identity and historical differences in regional integration"

#### 4.3. Rivalry between China and South Korea → Diplomatic Normalization

The shift in foreign policy focus in the 70's and 80's has indeed given China and South Korea more confidence in building flexible diplomacy based on mutual interests. Their increasing confidence was manifested through the positive changes in their rhetoric, policies and willingness to engage in positive dialogue. Both China and South Korea took initiatives to markedly improve their overall bilateral relations. The rapprochement process between the two countries went through three major events in the early 1990s that ultimately produced the 1992 Sino-Korea diplomatic normalization.

##### a. China's Enrollment into the APEC

China's enrollment into the Asia-Pacific Economic Cooperation (APEC) in 1991 was a major event that provided both China and South Korea an official channel of communication. South Korea, already member of the organization, paid special attention in helping China to obtain the membership. The Chinese government did not forget this cooperative gesture. By presenting an opportunity to affirm both sides' position on the improvement of the diplomatic relationship, China's enrollment into the APEC was an important first step towards the 1992 normalization.

The APEC was established in 1989 to facilitate economic growth, cooperation, trade and investment in the Asia-Pacific region. By 1991, there were twelve member states including the U.S., Canada, Australia, New Zealand, and South Korea.<sup>145</sup> South Korea, which was to host the third ministerial meeting in 1991, was particularly interested in getting China into the organization before the meeting in Seoul. With an important objective of promoting more contacts with China that could further the normalization effort, South Korea did all it could to help China become a member.

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<sup>145</sup> APEC official website. "About APEC." Retrieved from: [http://www.apec.org/content/apec/about\\_apec.html](http://www.apec.org/content/apec/about_apec.html).

There were many twists and challenges for China's participation in APEC. China had only agreed to join the APEC if certain conditions were met: above all, Taiwan was to be barred from full membership as a sovereign country. There must be only one China – the People's Republic of China – who would join APEC as a sovereign country, while Taiwan would join as a regional economy. Taiwan, however, steadfastly refused to join APEC under the name of "Taiwan, China" and it also refused to discuss this issue directly with China.<sup>146</sup> To solve this deadlock, South Korea's assistant foreign minister, Lee See Young, repeatedly made trips to China and Taiwan, trying to work out a compromise. Only after Lee allegedly threatened Taiwan – saying that if it still refused to compromise, APEC would admit China first, - did Taiwan eventually give in. In the memorandum that made the compromise official, Taiwan was required to use the name "Chinese Taipei," and only the minister for economic affairs could attend the meetings.<sup>147</sup> South Korea also struck a deal with China that it will not allow Taiwan's ambassador in Seoul to participate in any activities related to the third APEC meeting.<sup>148</sup>

China's participation of the APEC meeting in Seoul indeed provided an important opportunity for engaging in talks between the Chinese delegation and the Korean official who affirmed mutual desire to improve the diplomatic relationship. South Korean President, Roh Tae Woo, discussed the relations between South Korea and China, conveying his hopes to improve Korea's ties with China to the extent of establishing diplomatic relations. The Chinese foreign minister, Qian Qichen, also conveying China's wish to achieve greater development in its relationship with South Korea, responded his remark.<sup>149</sup> Exchanging both sides' positive perspective on establishing possible diplomatic ties, the official meeting between two countries'

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<sup>146</sup> Qian, Qichen. *Ten Episodes in China's Diplomacy*. New York: HarperCollins Publishers, 2005. p. 109

<sup>147</sup> Taipei Times editorial. "Editorial: What's Chen up to this time?" *Taipei Times*, July 23, 2005.

<sup>148</sup> Ibid.

<sup>149</sup> Ibid.

representatives had a crucial role in building the necessary trust and cooperation for the 1992 normalization.

#### b. Two Koreas' Admission to the UN

North and South Korea's simultaneous admission to the United Nations in 1991 was another major event that laid down a stepping-stone towards the 1992 normalization.

This event resolved a challenge faced by the Chinese government that dealt with how to justify recognizing "two Koreas" while maintaining the "One China" policy towards its cross-strait problem.

The Chinese government faced a political difficulty in starting official diplomatic relations with South Korea, because it meant China's decision to recognize both North and South Korea's legitimacy. Such decision could be viewed as a sign of its potential toleration of Republic of China (Taiwan) in gaining the status as the legitimate government of China. In order to preserve its "One China" framework, China had to separate these two issues as if they had no correlation.<sup>150</sup> One possible way to do this was through "following" the international "norms" and not through its own initial "decision" which would involve some harming effect on the legitimacy of "One China" policy. If an international organization were to recognize two Koreas first, then China could use the rhetoric of only abiding by the norms of international law when it wanted to recognize the two Koreas. China would not have to contradict its own decision to not recognize both China and Taiwan's legitimacy. This way, China could draw a clear distinction in its foreign policy towards the two Koreas issue and the China-Taiwan cross-strait problem, which would also preserve the consistency of its "One China" policy.

Therefore, the Chinese government exerted every possible effort to persuade North Korea and the international community to support the admission of both Koreas into the UN at the same

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<sup>150</sup> Armstrong, Charles K., edit. *Korea at the Center*. p. 209

time. China's effort involved having multiple talks with the North Korean government to persuade President Kim Il Sung that it was in North Korea's best interest to be admitted to the UN along with South Korea. At that time, both South Korea and North Korea had UN observer status. However, South Korea had been making efforts all along to join the UN as a full member, and more and more UN member states were ready to support it. North Korea, on the other hand, always opposed admitting both Koreas into the UN as full members, fearing that this decision would give sovereign status to both Koreas in the world, which could effectively "perpetuate" the divide between them.<sup>151</sup> China's first chance to persuade North Korea came when the Chinese premier, Li Peng, visited it in May 1991. Premier Li said to the North Korean prime minister that if South Korea proposed again to join the UN during the Assembly that year, it would be very difficult for China to oppose this. Premier Li further said that once South Korea becomes a full member of the UN, it would be very hard for North Korea to join the UN. After Premier Li's visit, President Kim Il Sung stated that North Korea would "cooperate" with China to work on the simultaneous admission of both Koreas to the UN.<sup>152</sup> The only concern North Korea still had on this issue, President Kim mentioned, was the possibility of the denial of its application by the veto power of the U.S. who would demand to inspect North Korea's nuclear facilities before letting it into the UN. In response to this comment, China assured North Korea that it would "consult the relevant countries," and try to persuade them to be "cooperative" on this issue. China's effort finally bore its fruit on September 17, 1991, with the adoption of a resolution at the UN General Assembly, admitting the two Koreas to membership simultaneously.<sup>153</sup> Admission of both Koreas into the UN finally gave China the chance to adhere to the "One China" policy towards its cross-strait problem while still "following" the

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<sup>151</sup> Qian, Qichen. *Ten Episodes in China's Diplomacy*. p. 118

<sup>152</sup> Ibid.

<sup>153</sup> United Nations official website. "List of Member States." Retrieved from: <http://www.un.org/members/list.shtml>.

“international norm” of recognizing both Koreas that included starting an official relationship with South Korea.

A series of negotiations between China and South Korea from May to June in 1992 finally shaped the official terms of the 1992 Sino-Korea normalization. Three rounds of talks between the two sides offered them an opportunity to view each other’s preconditions for establishing the normalization.

The first round of negotiation was held in Beijing, a city that could safeguard secrecy of the talk better than Seoul could. Each side had six or seven people, including a chief representative at the vice-ministerial-level and a deputy chief representative at the ambassadorial level. The talk was mainly focused on China’s intentions on the prerequisites of the normalization. The Chinese delegation explicitly demanded South Korea to sever diplomatic relations with Taiwan, put an end to all its treaties with Taiwan, and withdraw Taiwan’s embassy. In response to this demand, the Korean delegation proposed to demote Taiwan’s embassy to a “liaison office.” The Chinese side rejected this suggestion, and thus ended the first round of talks.<sup>154</sup> The second round of negotiation was also held in Beijing. This time, South Korea emphasized its precondition for the normalization. The Korean delegation said that since the relationship between Taiwan and Korea lasted for a long time, they wanted China to support that South Korea could maintain special relations with Taiwan after establishing normalization with China. However, China adhered to its original guideline, which demanded South Korea to sever all its ties with Taiwan. In the third round of negotiation held in Seoul, South Korea retreated from its original position and accepted China’s precondition for the normalization, and both sides reached an agreement on the issue.<sup>155</sup> These three rounds of talks have established both China

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<sup>154</sup> Qian, Qichen. *Ten Episodes in China’s Diplomacy*. p. 121

<sup>155</sup> Ibid.

and South Korea's agreement to the necessary preconditions for establishing official diplomatic ties, thereby offering a final stepping stone towards the 1992 Sino-Korea normalization.

On August 24, 1992, both China and South Korea's foreign ministers officially signed the communiqué for the establishment of the diplomatic normalization between the two countries.<sup>156</sup> The 1992 normalization was a tangible fruit of over two decades in accumulated effort of building cooperation. Since the 1970's, China-South Korea relations have experienced a progressive de-linking process from ideological dogmatism and superpower rivalry that dominated much of the previous two decades. Overcoming their long-held ideological tensions, South Korea and China both moved towards identifying the benefits of building proactive cooperation based on political, economic mutual interests. The three major events during the 1990s also solidified the two states' trust and confidence in each other, and ultimately shaped the road towards the establishment of diplomatic relations between them. In just forty years since the end of the Korean War, they went from being hostile enemy to being close partners. As of today, over fifteen years have passed since the two countries established diplomatic relations. During that time, this bilateral relation has gone beyond the extent anyone could have imagined. The leaders of both countries frequently paid official visits to each other, building further cooperation and promising for more exchanges. In 2005, the two-way trade volume reached over \$100 billion. China, which in 2005 received \$2.6 billion of investment from Korea, became Korea's largest investment destination. Korea also became China's third largest trading partner.<sup>157</sup> Behind China and South Korea's ongoing success at improving their ties after the diplomatic normalization, there is the solid foundation that they laid at the very beginning and throughout their relationship in the last four decades.

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<sup>156</sup> Armstrong, Charles K., edit. *Korea at the Center*. p. 209

<sup>157</sup> Cheng, Young-rok. "Impact of China on South Korea's Economy." Paper presented at the symposium for the Korea Economic Institute of America, Harvard University, September 25-27, 2006 (translation).

#### 4.4. Rivalry between China and other East Asian Countries and territorial disputes → Soft Power

Despite the territorial conflict in South China Sea, China maintained its relationship with South East Asian countries by increasing its trade partnerships and foreign assistance. In the 2014 ASEAN Summit, China offers \$20 billion in loans in Southeast Asia for regional infrastructure development.<sup>158</sup> With the exerted effort in reaffirming the importance of maintaining maritime security in the region, ASEAN member states “agreed to designate the year 2015 as the ASEAN-China Year of Maritime Cooperation, welcoming China’s comprehensive plan for utilizing the ASEAN-China Maritime Cooperation Fund to provide financial support for their cooperation in the areas of maritime connectivity, marine science and technology, as well as maritime scientific research, search and rescue, disaster management and navigation safety.”<sup>159</sup> This promise between ASEAN member states and China showed that political actors agree to the importance of effective cooperation in the region.

As China was basing its claims on historical information, other ASEAN member states, Vietnam and the Philippines in particular, were basing their claims to the United Nations Convention on the Law of the Sea.<sup>160</sup> According to Fravel, the continued economic growth of China was partnered with its stronger military influence. Considering that China’s military was considered as the most powerful in the region, the formation of the East Asian Community could be the most effective non-military force solution to end the territorial conflict. With the EAC alliance, an EAC Commission may handle the disputed territories, where all EAC members equally share the resources available in the disputed islands, including research and development. Maritime rights would be equally granted to member states. Rather than individual states keeping

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<sup>158</sup> Tiezze, Shannon. “China Offers \$20 billion in loans to ASEAN” The Diplomat <http://thediplomat.com/2014/11/china-offers-20-billion-in-loans-to-asean/> 15 November 2014.

<sup>159</sup> Ibid.

<sup>160</sup> Fravel, Taylor . “Maritime Security in the South China Sea and the Competition over Maritime rights.” Center for a New American Security. January 2012.

any revenues from the resources of the islands, the EAC commission would be allocating any revenues to specific EAC programs or allocate them as emergency funds. In return to this peaceful governance of the territories, any member state that needed any financial assistance or humanitarian aid due to a natural disaster could request assistance to the EAC Commission.

Besides the disputed territories in East Asia, China relationship with its neighbors are strong with regards to assisting them with foreign aids. Since 1950, China's very first material assistance to the Democratic People's Republic of Korea (DPRK) and Vietnam, China's foreign aid program has grown both in breadth and depth. China is now regularly providing bilateral assistance to 123 developing nations in eight major forms: complete projects, goods and materials, technical cooperation, human resource development cooperation, medical teams sent abroad, emergency humanitarian aid, volunteer programs in foreign countries, and debt relief.<sup>161</sup> By the end of 2009, China had provided a total of 256.29 billion RMB (\$4.03 billion) in aid to foreign countries, including 106.2 billion RMB (41.4%) in grants, 76.54 billion RMB (29.9%) in interest-free loans and 73.55 billion RMB (28.7%) in concessional loans.<sup>162</sup> China's foreign aid expenditure in 2009 alone was 13,296 million RMB (\$2.08 billion).<sup>163</sup>

By the end of 2009, China had helped developing countries construct over 2,000 complete projects, run over 4,000 training sessions of different types for 120,000 people from developing countries, sent over 21,000 medical workers to treat 260 million patients in the recipient countries, provided on nearly 200 occasions emergency aid to foreign countries, dispatched to 19 developing countries 405 young volunteers and 7,590 Chinese-language

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<sup>161</sup> Ministry of Commerce, Ministry of Foreign Affairs, Ministry of Finance, the People's Republic of China. *60 years of China's overseas aid* (2010), <http://yuanwaizhan.mofcom.gov.cn>, (accessed December 3, 2011) .

<sup>162</sup> State Council Information Office. White paper: China's foreign aid.

<sup>163</sup> Ministry of Commerce, "Main Items of Budgetary Expenditure of Central and Local Governments" *China Statistical Yearbook*, 2010.

teachers to over 70 countries. China had also signed debt relief protocols with 50 countries, where almost half are from East Asian countries, canceling 380 mature debts totaling 25.58 billion RMB.<sup>164</sup>

The recipients of China's foreign aid include most developing countries in Asia, Africa, Latin America, the Caribbean, Oceania and Eastern Europe. About two-thirds of China's aid always goes to the least developed countries and other low-income countries. By the end of 2009, China had aided 161 countries and more than 30 international and regional organizations, including the 123 developing countries that receive aid from China regularly. Of them, 30 are in Asia, 51 in Africa, 18 in Latin America and the Caribbean, 12 in Oceania and 12 in Eastern Europe. Asia and Africa, home to World's the largest poor population, have received about 80% of China's foreign aid.<sup>165</sup> In Asia, in particular, China has provided East Asian countries, such as Vietnam, Indonesia and the Philippines, humanitarian assistance to assist recipient countries affected by natural disasters. Major highlights of Chinese foreign assistance for the past five years include: counter trafficking of persons and drugs (Laos), elections (Cambodia), and historical preservation (Philippines and Cambodia).<sup>166</sup> China has also financed infrastructure, energy-related projects such as hydropower development in Myanmar, railway project in the Philippines, steel plants in Thailand and power plant and mining in Vietnam.<sup>167</sup>

China does see it as its responsibility as a strong nation to help less developed nations. Responsibility comes from the help it received from other nations during its development both domestically and internationally, and is reinforced by the political benefits, economic benefits and soft power it has obtained through aid. China's soft power will not only strengthen its

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<sup>164</sup> State Council Information Office. White paper: China's foreign aid.

<sup>165</sup> Ibid.

<sup>166</sup> Congressional Research Service. "China's Foreign Aid Activities in Africa, Latin America, and South East Asia." 25 February 2009.

<sup>167</sup> Ibid.

relationship with its neighbors but also it signifies peaceful development in building an East Asian Community.

#### 4.5 The Cold War Structure → Post-Cold War Structure

The American-led alliance dubbed as “hub-and-spoke” system and the USSR-influenced alliance have underpinned the regional economic/security order during the Cold War. However, the post-Cold War East Asia shows undeniable trends that show delinking of Asia from the U.S. - (or now dissolved Soviet Union) dominated Cold-War structure. Many significant geopolitical changes have taken place including the US withdrawal from Vietnam, Japan’s come-back as a major industrial power after World War II, South Korea’s democratization, the Soviet empire’s collapse in the early 1990s, and China’s success as a regional and global power. Among these, three striking trends have shaped the postwar East Asia in a fundamentally different way from the divisive Cold-War structure.

First and foremost, the region became enormously rich with added political economic leverage in the world. As a result, more Asian countries demanded a revamp of the old American dominated bilateral economic relations to multilateral relations; the countries argued that the ‘spoke-economies’ (i.e. American allies in East Asia) had been left at a serious disadvantage by the U.S. unilateral pressure from time to time. Asia as a whole has accomplished great economic success of catching up with industrialized nations in North America and Europe. In 1960, Asia accounted for only 4 - 5 percent of the world Gross National Product (GNP) in contrast with 37 percent for the U.S., Canada and Mexico combined. Merely three decades later, by the early 90s, the combined economies of Japan, South Korea, Taiwan, the ASEAN countries, and greater China took roughly 30 percent of world’s GNP, approximately the same share as that added by

North America and Western Europe.<sup>168</sup> However, East Asia's rapid economic growth had not always been reflected in the subsequent change in the allocation of influence in international organizations such as the IMF, the World Bank, and the UN. In order to enhance its collective global influence, East Asian countries were increasingly focused on forming an integrated regional body instead of relying upon the U.S. through separate bilateral relations.

Secondly, China's rapid economic development along with its "peripheral diplomacy" helped to advance its image as an attractive partner in the cooperative regional scheme among countries in East Asia, rivaling that of America. China's surging economy can now offer substantial economic benefits to America's important Asian allies. Japan's rebound after the 'lost-decade' of 1990s was mainly due to its exports to China; amid the sluggish US and European economies, China became Japan's biggest export destination outstripping the U.S. of its long-held rank.<sup>169</sup> In 2007, China also became South Korea's largest trading partner at trade volume of \$140.5 billion. South Korea's exports to China reached \$80 billion, making China its biggest export destination.<sup>170</sup> In 2008, China's trade with Southeast Asian nations topped \$192 billion volume, more than three times the amount exchanged in the U.S-ASEAN trade. With China-ASEAN Free Trade Area that took effect in 2010, the trade volume reached an unprecedented level as most goods became tariff-free, making it as the third of largest free trade agreement.<sup>171</sup> China's change in foreign policy also had significant impact on its geopolitical image in East Asia. In the early 1990s, China adopted aggressive policy by using military strength to intimidate other countries in Asia. The strategy involving sending several naval ships

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<sup>168</sup> Pempel, T.J., editor, 2005, pp. 214

<sup>169</sup> McCurry, Justin, "China replaces US as Japan's biggest export destination," *Guardian*, August 21, 2008, <[www.guardian.co.uk/world/2008/aug/22/japan.china](http://www.guardian.co.uk/world/2008/aug/22/japan.china)>, accessed December 15, 2012.

<sup>170</sup> Shah, Arun, "China is Korea's Largest Trading Partner, India 16<sup>th</sup> in Korean Imports," *Andhranet*, January 17, 2008, <[www.andhranews.net/India/2008/January/17-China-Korea-30055.asp](http://www.andhranews.net/India/2008/January/17-China-Korea-30055.asp)>, accessed December 15, 2012,.

<sup>171</sup> Walker, Andrew, "China and Asean free trade deal begins," *BBC News*, January 1, 2010, <<http://news.bbc.co.uk/2/hi/business/8436772.stm>>, accessed December 15, 2012.

to contested areas in the South China Sea eventually backfired, leading the President of the Philippines to condemn Beijing's belligerent behavior and step up Philippine's military links with the U.S.<sup>172</sup>

However in 2003, China's image in the eyes of neighboring governments went through a radical change. The new perception was that China was trying its best to assist and accommodate its Asian neighbors while the U.S. was perceived as unilaterally setting its own foreign policy and strong-arming everyone onto that plan without much consideration of other countries.<sup>173</sup> China proposed a "bilateral joint development" model to explore the contested areas in the South China Sea for oil with Vietnam and the Philippines. Beijing also signed to the Treaty of Amity and Cooperation, a document that confirmed the signer's respect for the sovereignty and equality of the ASEAN members. Southeast Asian leaders who traditionally looked for the U.S. as the "anchor of regional security," were considering the need to foster stronger economic/political relationships with Beijing.<sup>174</sup>

Thirdly, the region had been more peaceful as conflicts among states in East Asia had been ameliorated. The fall of the Soviet Union in the early 1990s has challenged the ideological divide (capitalism versus communism) and left a room for new political thinking. Gradually, promotion of economic interests through international trade arose as the new driving force shaping international relations in the region. Hence, East Asian countries seen less incentive to engage in hostile activities, and as a result the magnitude of political tension was significantly reduced compared to those before 1980s. Two examples were quite noteworthy: signs of easing tensions between the PRC and Taiwan, and between North and South Korea. After decades of

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<sup>172</sup> Kurlantzick, Joshua. "Pax Asia-Pacifica? East Asian integration and its implications for the United States."

<sup>173</sup> Arrighi, Giovanni (2007), pp. 205

<sup>174</sup> D. Greenlees, "Asean Hails the Benefits of Friendship with China –Asia – Pacific – International Herald Tribune" *New York Times*, November 1, 2006, <[www.nytimes.com/2006/11/01/world/asia/01iht-asean.3356137.html](http://www.nytimes.com/2006/11/01/world/asia/01iht-asean.3356137.html)>, accessed December 13 2012.

mutual animosity, the Communist Party in Mainland China and the Nationalist Party in Taiwan began high-level contact towards reconciliation by having a meeting between President Hu Jintao and Chairman Lien Chan in April 2005.<sup>175</sup> Since then, direct postal, transportation, and trade links across the Cross Strait had been established under the name “Three Links” on December 2008. In 2009, approximately one million Chinese mainlanders visited Taiwan. Currently, there are more than 270 direct flights per week linking the two sides. According to Taiwan statistics, the PRC is Taiwan’s largest trading partner with trade volume totaling \$110 billion in 2009.<sup>176</sup>

There was increasing possibility of peace in the Korean peninsula as well. Although the reconciliation progress in Korea was not comparable to that of the Cross Strait relations, both North and South Korea began to engage in high-level talks in 2000 including first Inter-Korean Summit between Kim Jong-il and Kim Dae-jung.<sup>177</sup> Since then, family reunions and another Inter-Korean Summit followed, reaffirming peace on the peninsula. Despite of some naval clashes and North Korea’s nuclear test, there were relatively fewer skirmishes between the two sides nowadays compared to the Cold War period. There had been some attempts by both Koreas to put aside different ideological beliefs and develop cooperation for common economic benefits. A good example was the Kaesong Industrial Park, which opened in December 2004. Located ten kilometers north of the Korean Demilitarized Zone, it was the first cooperative project with the goal of achieving win-win economic gains for both Koreas. Hyundai Asan, a division of South Korean conglomerate Hyundai, had been in charge of developing the industrial park and

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<sup>175</sup> “Taiwan Opposition Leader in China,” *BBC World*, April 26, 2005, <<http://news.bbc.co.uk/2/hi/asia-pacific/4482617.stm>>, accessed December 16, 2012.

<sup>176</sup> Shear, David B, “China-Taiwan: Recent Economic, Political and Military Developments across the Strait and Implications for the States,” Testimony before the U.S.-China Economic and Security Review Commission, U.S. Department of State, March 18, 2010. <[www.state.gov/p/eap/rls/rm/2010/03/138547.htm](http://www.state.gov/p/eap/rls/rm/2010/03/138547.htm)>, accessed December 16, 2012.

<sup>177</sup> Chon, Hyun-joon, “The Inter-Korean Summit: Evaluation and Tasks Ahead,” *East Asian Review*, Vol. 14, No. 2, Summer 2002, pp. 3-16. <[www.ieas.or.kr/vol14\\_2/14\\_2\\_1.pdf](http://www.ieas.or.kr/vol14_2/14_2_1.pdf)>

employed as many as 40,000 DPRK (Democratic People's Republic of Korea, i.e. North Korea) workers as of 2009, providing much needed employment opportunities. On the other hand, South Korean firms benefit from this venture by taking advantage of cheap labor available in the North.<sup>178</sup> Economic motivation could influence even the long-time enemies to shake hands together.

The synergistic connections among these three trends have led East Asia away from the disruptive Cold-War alignment and towards an interlinked regional collective arrangement. Today, growing number of governmental and quasi-governmental efforts are being made to enhance regional ties, and consequently collective peace and prosperity.

#### 4.6. The U.S. Opposition → Possible Cooptation of the EAC

As emphasized in Chapter 4, the U.S. has an important role in the development of an East Asian Community as it has extensive political, security and economic relations with many East Asian countries. In 1990, during the first George Bush's administration, U.S. officials strongly objected the initial Mahathir proposal for an East Asian Economic Grouping. However, in 2000s, U.S.'s high-level officials have not voiced out serious concern over the ASEAN+3 process and the East Asian dialogue channels accompanying it. I argue three reasons why co-opting the EAC might be the best option for the U.S.

First, the EAC does not plan in promoting protectionist policy, but rather hope to play a complementary role to the existing international bodies governing global economy. Even with rapidly increasing intra-regional demand and investment by the development of EAC, East Asian reliance on final demand from extra-regional markets, most prominently the US market, will *not* subside easily. As the largest or second largest market for the exports of nearly a dozen Asian

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<sup>178</sup> Moon, Ihlwan, "Bridging the Korean Economic Divide," *Businessweek*, March 7, 2006, <[http://www.businessweek.com/globalbiz/content/mar2006/gb20060307\\_843108.htm](http://www.businessweek.com/globalbiz/content/mar2006/gb20060307_843108.htm)>, accessed December 22, 2012.

countries, the U.S. has consistently taken in between 23 and 33 percent of the region's exports. Further, close to 30 percent of U.S. exports enter the ASEAN, South Korea, China, Japan, and Taiwan.<sup>179</sup> If the EAC threatens to become a self-sufficient economic block in the near future, it will be an economic suicide. East Asian governments in no way promote inward-looking policies as evidenced by the fact that many of them are pursuing FTAs with countries outside the region.<sup>180</sup> As shown by the number of countries currently on the negotiation process for bilateral FTAs with the US (e.g. South Korea, Singapore, and Japan), East Asian regionalism values US involvement in the region. With open regionalism in mind, the EAC plans to take on regional issues, which do not receive serious consideration in the existing global frameworks for trade/investment liberalization (WTO) and international financial management (IMF). Rather than depending on international bodies / organizations, promoting regional economic/financial security lies the root of the EAC idea. Through the EAC, the region as a whole also wants to have an independent voice in the global economy, a willpower intensified by the widespread opinion of the IMF's mishandling of the 1997 financial crisis.<sup>181</sup>

Secondly, there is increasing doubt whether the US has political/economic means to oppose the EAC formation process as it did in 1990. During the 1990s, the U.S. pursued 'financial liberalization' throughout East Asia in order to make the region to be "highly dependent on the US dollar for exchange rate stabilization, trade invoicing, external asset denomination, foreign exchange reserve holding, and external liabilities."<sup>182</sup> One consequence of this policy was the massive purchases of US treasury bonds and build-up of huge dollar-

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<sup>179</sup> Pempel, T.J., editor, 2005, pp. 271

<sup>180</sup> The FTAs in effect as of 2010 are Singapore-New Zealand (January 2001), Singapore-USA (January 2004), South Korea-Chile (April 2004), Japan-Mexico (September 2004), Thailand-Australia (January 2005), South Korea-USA (June 2007, pending Congressional approval). Source: Kawai 2005b.

<sup>181</sup> Zhang, Yumei. (2002) pp. 143

<sup>182</sup> Kawai, M., (2005)

denominated foreign exchange reserves by many Asian governments. By August 2006, Japan (\$664 billion) was the largest foreign holder of US treasuries, followed by China (\$339 billion). Exceeding over 1 trillion US dollars in reserves, Japan and China's total holdings were more than three times the combined holdings of Britain, Germany, and Canada (\$300 billion).<sup>183</sup> Additionally, East Asian governments have been the most important financiers for the U.S. campaign of 'War on Terror' launched after the 9/11 attack in 2001. The National Priorities Project estimated the total costs of wars in Iraq and Afghanistan at around \$1.05 trillion by counting all Congress- approved funds since the fiscal year 2001.<sup>184</sup> In October 2007, Congressional Budget Office Director, Peter Orszag, stated in his testimony that the 'War on Terror' may cost up to \$2.4 trillion until 2017. This gargantuan sum did not even include the Pentagon's normal fiscal year spending which was about \$450 billion in 2007.<sup>185</sup> In sum, the U.S. is the world's biggest debtor by wide margin with ever-escalating deficits in its current account. Growing financial dependence on foreign governments, especially those in East Asia, to cover those deficits can necessarily constrain the US ability to directly oppose the multilateral negotiations promoting East Asian integration.

Thirdly, increasing East Asian economic and cultural integration is an inevitable trend at least in the near future. Over the next decade, the integration will only accelerate as the trade patterns center within the region. As explained in the first chapter, intraregional trade/production network has been expanding rapidly since the Plaza Accord of 1985. The exponential rise of bilateral free trade agreements between Asian countries serves as conspicuous evidence.

ASEAN-China FTA came into effect in January 2010, and their bilateral trade volume exceeded

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<sup>183</sup> Arrighi, Giovanni. (2007) pp. 193

<sup>184</sup> National Priorities Project, "National Priorities Project Tallies Cost of War through September 30, 2010," January 11, 2010. <[www.nationalpriorities.org/2009/1/11/Cost-of-war-tallies-through-FY2010](http://www.nationalpriorities.org/2009/1/11/Cost-of-war-tallies-through-FY2010)>.

<sup>185</sup> Hargreaves, Steve, "'War on Terror' may cost \$2.4 trillion," *CNNMoney*, October 24, 2007, <[http://money.cnn.com/2007/10/24/news/economy/cbo\\_testimony/index/htm](http://money.cnn.com/2007/10/24/news/economy/cbo_testimony/index/htm)>, accessed December 22, 2012.

\$200 billion.<sup>186</sup> Japan also made multiple Comprehensive Economic Cooperation Agreements with ASEAN countries such as Indonesia, Brunei, Thailand, Philippines, Malaysia, and Singapore. South Korea-ASEAN FTA came into effect in June 2007 with most of tariff reduction started in 2010.<sup>187</sup> As East Asia becomes more dependent on intraregional trade and consumption, the U.S. influence in the region as the main consumer and trader will gradually subside.

These three reasons demonstrate how co-opting the development of an East Asian Community can be an effective choice for the U.S. Furthermore, the co-option can potentially revitalize American public diplomacy in the region by improving its heavily damaged image. It can help lessen the growing anti-Americanism fueled by the angry public opinion toward the US-led financial liberalization during 1990s, its inappropriate response to the 1997 financial crisis, and its war on terrorism since 2001. The U.S. should give East Asia the same priority as it does to Europe, and it should also facilitate closer interaction between Asian governments. To do so, Washington should task U.S. embassies to reinvigorate their cooperation with leading Asian cultural, economic, and political organizations. Indeed, U.S. President Obama perhaps understands that co-option of an EAC can render Washington in better position to shape the future of East Asia. In response to the Japanese Prime Minister Hatoyama's concept of East Asian Community, President Obama said in November 2009 that he looks forward to engaging with the *East Asia Summit* more formally in the future.<sup>188</sup>

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<sup>186</sup> Walker, Andrew, "China and Asean free trade deal begins." *BBC News*, January 1, 2010, <<http://news.bbc.co.uk/2/hi/8436772.stm>>, accessed December 22, 2012.

<sup>187</sup> Singapore FTA Network, "Overview of ASEAN Korea(AKFTA)," <[www.fta.gov.sg/fta\\_akfta.asp?hl=3](http://www.fta.gov.sg/fta_akfta.asp?hl=3)>, accessed December 22, 2012.

<sup>188</sup> "Transcript of Obama's Asian-policy speech in Tokyo," *The Washington Post*, November 13, 2009. <<http://voices.washingtonpost.com/44/2009/11/transcript-of-obamas-asian-pol.html>>

Obama's use of the concept "East Asia Summit (three more members added to the ASEAN+3 grouping)" instead of "East Asian Community (ASEAN+3, 13 potential members)" is interesting as the former term indicates the addition of three more potential members on top of the latter term's membership; those three members are India, Australia, and New Zealand. However, the fact that Obama did not openly challenge the concept of Hatoyama's EAC proposal indicates a possible co-option of the idea from the U.S.

### Conclusion

Political challenges play a role in regionalizing the East Asia. The relationship of China with its neighbors and the influence of the United States to the major players (Japan and South Korea) in the region shape the formation of the East Asian Community. As China becomes a regional hegemon, economically and politically, the U.S places a major concern to the role of China in maintaining peace in the region, opposing the formation of the EAC. However, based on the analysis in this chapter, the political environment have changed over time in East Asia, and the political challenges described in this chapter can be overcome by a gradual process of establishing cooperative norms and practices, especially that of economic, in the region.

## 5. What's Next?

### 5.1. Auspicious Signs for the EAC Formation

Two achievements in state-driven East Asian cooperation stand out as they bring forward the development of an East Asian Community. The first one is the explosive growth in number of bilateral FTAs between East Asian countries. The idea is that these separate FTAs can support the process of negotiating multilateral FTA encompassing the whole East Asia. A simple outline towards an EAC looks like this:

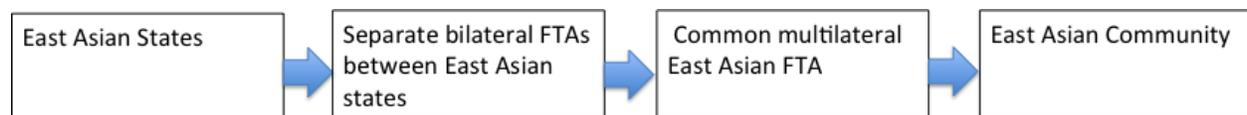


Table 2. FTA/EPA Initiatives in East Asia (as of September 2004)

<b>In effect</b>	<b>Under official negotiation</b>	<b>Under consultation/study</b>
Bangkok Treaty (1976)	China–ASEAN	China–New Zealand
Laos–Thailand (1991)	Hong Kong–New Zealand	China–Australia
ASEAN FTA (1992)	Japan–Mexico (signed in September 2004)	Japan–Australia
Singapore–New Zealand (January 2001)	Japan–Korea	Japan–ASEAN
Japan–Singapore (November 2002)	Japan–Thailand	Japan–Indonesia
Singapore–Australia (2003)	Japan–Philippines (almost concluded)	Japan–China–Korea
Singapore–EFTA (January 2003)	Japan–Malaysia	Japan–Chile
Singapore–USA (January 2004)	Korea–Singapore (concluded)	Korea–ASEAN

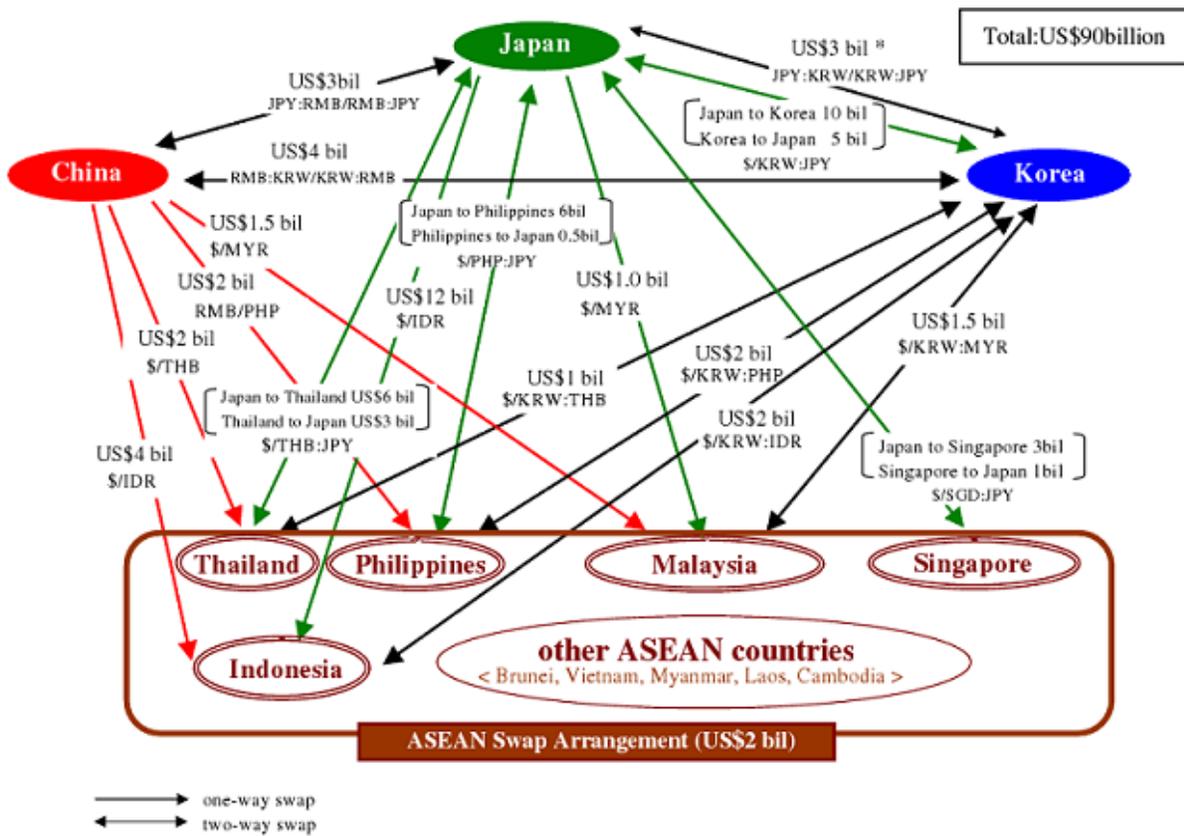
China–Hong Kong (January 2004)	Singapore–Canada	Korea–Mexico
China–Macao (January 2004)	Singapore–Mexico	Singapore–Taiwan
Korea–Chile (April 2004)	Singapore-P3 (Australia, Chile, New Zealand)	ASEAN–CER (Australia, New Zealand)
Taiwan–Panama (2004)	Singapore–India	ASEAN–EU
Thailand–Australia (January 2005)	Thailand–India	ASEAN (bilateral)–USA
	ASEAN–India	

Source: Kawai M. “East Asian economic regionalism: Progress and challenges” (2005), *Journal of Asian Economics*, 16 (1), pp. 29-55

Note: From 2005 until March 2010, several new FTAs under official negotiation or study have formally come into force: Japan-Malaysia (May 2005), Korea-ASEAN (March 2006), Japan-Thailand (November 2007), Japan-Philippines (December 2008), China-ASEAN (January 2010), and Hong Kong–New Zealand (March 2010). In October 2010 at the APT Summit in Hanoi, leaders of APT agreed to consider, review and identify the future of APT cooperation.

Another important achievement towards building an EAC is the extensive bilateral swap agreements (BSA) between East Asian countries. As mentioned in Chapter 3, the Chiang Mai Initiative (CMI) introduced in May 2000 consisted of multilateral/bilateral currency swap agreements among the ten ASEAN members, China, Japan, and South Korea. By October 2009, the CMI network included 16 bilateral agreements with amounts totaling \$90 billion. The wide-ranging crisscross pattern of arrangements between ASEAN+3 countries is shown in the image below:

**The Agreement on the Swap Arrangement under the Chiang Mai Initiative (as of October 16, 2009)**



Note: Total amount includes those under negotiation for renewal but does not include ASEAN swap arrangement.

\* The maximum amount of the bilateral JPY/KRW swap arrangement has been increased as a temporary measure effective until February 1, 2010, from three billion US dollars equivalent to twenty billion US dollars equivalent.

Source: "The Agreement on the Swap Arrangement under the Chiang Mai Initiative (as of October 16, 2009)" (PDF). *Bank of Japan*. 16 October 2009. Retrieved April 1, 2010. <[www.boj.or.jp/en/type/release/zuiji07/data/un0707a.pdf](http://www.boj.or.jp/en/type/release/zuiji07/data/un0707a.pdf)>

On top of the \$90 billion swaps, additional \$7.5 billion commitments had been made under the New Miyazawa Initiative which was a Japanese government initiative to provide short-term financing facility to the crisis-hit Malaysia, Korea, and the Philippines in 1999.<sup>189</sup>

Both achievements brought the idea of building a politically/ financially cooperative regional body closer to reality. Encouraged by these accomplishments, both China and Japan

<sup>189</sup> Kawai, M. (2005), 16 (1)

have tasked special diplomatic efforts to promote an EAC took off. In September 2003, China hosted the first annual conference of the Track II Network of East Asian Think Tanks (NEAT) to identify tangible steps to build an EAC. At the 8<sup>th</sup> ASEAN+3 meeting in Vientiane, Premier Wen Jiabao has taken the initiative to launch the feasibility study of the East Asia-wide FTA. He indicated that China was ready to financially support a joint study on the potential EAC financial and monetary cooperation.<sup>190</sup> The then newly-elected Japanese Prime Minister Yukio Hatoyama had repeatedly spoken of his determination to shift Japan's focus from a more America-centric foreign policy to a more Asia-focused policy. He was an enthusiastic supporter of deepening regional economic integration; he promised to try his best to build an East Asian free trade zone by 2020.<sup>191</sup> He believed that dynamic intra-regional trade in East Asia is crucial to Japan's long-term growth strategy. Other leaders in East Asia shared this aspiration. In the fifth ASEAN+3 Summit in November 2001, the leaders of thirteen nations represented have endorsed the East Asian Free Trade Agreement (EAFTA), however with no given goal-year in mind.<sup>192</sup> The challenge lied at converging a proliferate number of bilateral Free Trade Agreements/Economic Partnership Agreements existing in the region. Consolidating different trade arrangements towards identical rules and common tariff rates will surely not be an easy task.

## 5.2 Policy Suggestions for the EAC efforts

There are three policy suggestions I propose to East Asian leaders to promote the goal of establishing an East Asian Community:

1. Developmental assistance;

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<sup>190</sup> Wen Jiabao. 2004. Strengthening Cooperation for Mutual Benefit and a Win-Win Result. Vientiane, 29 November 29, 2004. <[www.fmprc.gov.cn/eng/topics/wenjiabaoASEANeng/t172730.htm](http://www.fmprc.gov.cn/eng/topics/wenjiabaoASEANeng/t172730.htm)>

<sup>191</sup> Tabuchi, Hiroko. "Japan Unveils Plan for Growth. Emphasizing Free Trade in Asia." *The New York Times*. December 30, 2009, <[www.nytimes.com/2009/12/31/business/global/31yen/html](http://www.nytimes.com/2009/12/31/business/global/31yen/html)>, accessed December 22, 2012.

<sup>192</sup> Association of Southeast Asian Nations, "Press Statement by the Chairman of the 7<sup>th</sup> ASEAN Summit and the 5<sup>th</sup> ASEAN+3 Summit Brunei Darussalam, 5 November 2001." <[www.aseansec.org/5467.htm](http://www.aseansec.org/5467.htm)>

2. Expansion of regional student exchange program; and
3. Cooperation for common security concerns.

First, I argue that the member countries of ASEAN+3 should incorporate institutional developmental assistance policy in order to facilitate economic convergence between developed and less-developed economies in the region. This policy will be able to help less-developed economies to build a capacity to participate in regional arrangement such as an East Asia-wide FTA. The European Union has the model called the Common Structural Policies (CSP), which accounted for almost one third of the total EU budget in the 2000-2006 periods. The CSP includes the European Reconstruction and Development Funds (ERDF) given to countries whose GDP per capita is less than 75 percent of the EU average, or that are very remote in terms of geographic location, or that have very low population density.<sup>193</sup> Both the contributing and receiving countries of this developmental fund can benefit as the structural aid stimulates the whole region's economic development.<sup>194</sup> This implies that the more industrialized countries in the region such as Japan, Singapore, and South Korea – which will probably be the main contributors to the proposed budget – can profit when structural transfers foster economic growth and political stabilization in less-industrialized member states in the southern part of East Asia. Using GDP per capita measure to determine the aid is probably not apt in the East Asian case because it does not accurately capture individual country's economic power. For example, a big economic power like China has even lower figure (\$6,500) than that of relatively smaller economy like Thailand (\$8,000).<sup>195</sup> Although, the exact method of determining the amount of

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<sup>193</sup> Schneider, Christina J. *Conflict, negotiation and European union enlargement*, Cambridge University Press, Cambridge ; New York: 2009, pp. 121

<sup>194</sup> *Ibid.*

<sup>195</sup> World Economic Outlook Database “Gross domestic product based on purchasing-power parity (PPP) per capita” – October 2009, International Monetary Fund, accessed on December 22, 2012

contribution and aid should be discussed further, the policy can promote more intense economic cooperation by closing the economic gap between northern and southern parts of East Asia.

Secondly, East Asian governments should actively help to expand the intra-regional university exchange student programs. These programs can boost intellectual and cultural integration among young adults who can be the main drivers of rising East Asian regionalism. The European Union student exchange program called the ERASMUS (European Region Action Scheme for the Mobility of University Students) Program was established in 1987, and it helped over 1.6 million students to carry out a study period at 2,199 higher education institutions abroad across thirty-one European countries.<sup>196</sup> The program has two main features: (1). the program guarantees that the study abroad period of at least three months to an academic year in another European country is recognized by the student's original institution; (2). European Commission provides funding for student participants so that they do not pay extra tuition fees to the host university. Modeled after the ERASMUS program, the Asia-Pacific Association for International Education (APAIE) was established by a committee of thirteen countries' university representatives from the Asia-Pacific region on 03 December 2004, at Korea University in Seoul, South Korea. The APAIE network aims to facilitate exchanges of courses, professors and students among institutions from different universities as well as promoting joint-degree programs.<sup>197</sup> Government leaders should support these exchange student initiatives to foster not only intellectual learning and understanding of the host country but also a sense of community among students from different countries.

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<sup>196</sup> Europa, "Frequently Asked Questions: Erasmus Programme, how does it work?" December 7, 2006. <<http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/06/466&format=HTML&aged=0&language=EN&guiLanguage=en>>

<sup>197</sup> APAIE.org, Intro and History. <[www.apaie.org](http://www.apaie.org)>

Thirdly, the governments of ASEAN+3 should cooperate more vigorously with each other on common security concerns. One such concern is securing energy supply. Professor Paul Kennedy, the Director of the International Security Studies program at Yale University, repeatedly pointed out the buildup of navies in Korea, Japan, China, India, and Indonesia. The focus on strengthening naval forces comes partly because these countries want to protect their petroleum supply lines from the Persian Gulf.<sup>198</sup> The increasing budget spending on naval projects had made them rising sea powers, and at the same time produced sources of potential conflicts. Hence, there should be an installation of hot lines between all top political leaders of thirteen East Asian governments so that they can find immediate political/diplomatic solutions when one country's naval ships trespass another country's territorial waters. Furthermore, the governments should foster deeper political connections on other regional security issues such as cooperative sea resource explorations, damage control for natural disasters, and cooperative efforts to address environmental problems such as global warming that pose serious threat to the region.

### 5.3. Conclusion

An Jung-geun's concept of "Citizen's Asia" sheds much light upon the positive direction for an East Asian community to evolve in the future. A regional organization run and represented by civic forces is arguably the greatest form of multilateralism in forming an international body. His vision of multilateralism invites leadership from relatively smaller countries like Korea and ASEAN nations, and it can dispel much fear about Asia being dominated either by China or Japan. After Kim young-ho finished his lecture in Tokyo, a former Japanese ambassador to the United Nations came up to him and said: "When China or Japan come out talking about an Asian

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<sup>198</sup> The Leigh Bureau, "Threats to the West," an interview with Paul Kennedy conducted by Xiaohang Liu. <[www.leighbureau.com/speaker\\_documents.asp?view=article&id=98](http://www.leighbureau.com/speaker_documents.asp?view=article&id=98)>

community, everyone guards against it. It becomes more of a possibility if it is Korea who brings up the idea, and if Korea promotes An Jung-geun's vision."<sup>199</sup> Korea's role in building an East Asian community has already been noted in Korean President Kim Dae-jung's proposal to establish the East Asia Vision Group and the East Asia Study Group in December 1998 and November 2000 respectively. Eminent intellectuals from the 13 ASEAN+3 countries participate in two groups, and each year they submit reports to ASEAN+3 Summit on implementable concrete measures for establishing an EAC, reasons for their selection, and their expected benefits.<sup>200</sup> In addition to Korea, ASEAN has also taken a leading role in the East Asian institutionalization via the ASEAN+3 process that began in 1999. Similar to Brussel's role in the EU, ASEAN has increasingly become a neutral broker between East Asia's giants, and help countries to come together to address common concerns.

With the help of power-balancing roles of Korea and the ASEAN, the idea of an EAC has made substantial progress over a decade to become "open" multilateral regional body. As I have argued in Chapter 3 "Economic needs realized in the *post-crisis* East Asia," the economic crisis of 1997 solidified political concerns about the regional financial security, and intensified state desires to form an organization that can supplement the bottom-up groundwork of trade/production/investment networks in the region. In the words of one: "The contours of post-financial crisis regionalism are, by state design, aimed at restoring to Asia a greater degree of political power and autonomy vis-à-vis the rest of the world, and the U.S. and the international

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<sup>199</sup> Ibid.

<sup>200</sup> Ministry of Foreign Affairs of Japan, Japan-ASEAN Relations, "Final Report of the East Asia Study Group" Submitted to ASEAN+3 Summit, 4 November 2002, Phnom Penh, Cambodia. <[www.mofa.go.jp/region/asia-paci/asean/pmv0211/report.pdf](http://www.mofa.go.jp/region/asia-paci/asean/pmv0211/report.pdf)>

financial institutions it controls, in particular.”<sup>201</sup> However, it seems unlikely to expect that a more mature East Asian arrangement will materialize in the *immediate* future. Even the strongest supporters of the EAC admit that East Asian regionalism is at a modest infant stage of development; it still faces many obstacles, and it can take several different paths along the way. One increasing possibility is that the Community may include three more countries albeit not of East Asian origin: India, Australia, and New Zealand. The grouping (i.e. ASEAN+3 plus India, Australia, and New Zealand) started its official forum with the name “the East Asian Summit (EAS)” in Kuala Lumpur, Malaysia on December 14, 2005. The EAS was more enthusiastically promoted by Japan and some ASEAN states to circumvent a Sino-centric regional dominance. The concept of East Asian Community thus has come to have two groupings both overlapping one another. However, the EAC idea had its new beginning when both China and India declared on November 2006 that the community would arise through a two-phase process with ASEAN+3 as the first and the EAS as the second phase.<sup>202</sup>

Whatever geographical boundaries the East Asian Community will have, the real challenge is how to establish an *effective* regional institution. Since the 1997 financial crisis, East Asian governments have shown increasingly strong *political will* to create such an institution. Many people still evince strong doubt that an EAC will ever arise. However, regardless of what grouping it will first follow, I believe that the political will towards building an East Asian Community will be more robust as times go because there is a clear economic logic for strengthening regional frameworks – it helps the on-the-ground trade/investment integration and develops new methods of regional financial management. The large benefits of further economic

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<sup>201</sup> Bowles, Paul. 2002. “Asia’s Post-Crisis Regionalism: Bringing the State Back in, Keeping the (United) States Out.” *Review of International Political Economy* 9, 2 (May): 230-56

<sup>202</sup> Press Information Bureau, Government of India, “Joint Declaration by the Republic of India and the People’s Republic of China,” November 21, 2006. <<http://pib.nic.in/release/release.asp?relid=22168>>

integration and its institutionalization greatly outweigh the political costs of not doing so. By implementing various norms, rules, and procedures that fit regional conditions, an East Asian Community will greatly contribute to the welfare of East Asia and help one cohesive voice of East Asia heard in international political economic policymaking.

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