South China Sea Dispute and Institutional Balancing: ASEAN, TPP and AIIB

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Introduction

China, the largest trading partner for more than 125 nations in the world, is in the position to use its economic clout to realise its political and strategic interests. Economic interdependence, chiefly intensified by China’s trade and aid growth in the region, can thus act as a means of achieving China’s national interest, including its assertion in the South China Sea, as seen in China’s massive flow of aid to Laos and Cambodia that has been instrumental in dividing ASEAN members on the South China Sea dispute. Therefore, deepening interdependence does not lead to the political stability in East Asia. It appears imperative for the other claimants in Southeast Asia, as well as the United States and Japan, which also have condemned China’s aggressive and illegal actions in the South China Sea including the construction of artificial islands. ASEAN has, however, failed to take an effective means against these Chinese maritime behaviors, casting a stronger doubt on the organization’s usefulness for the regional security. It has been growingly difficult for any nation, which has increased their trade and, for some, aid, reliance on China, to pass strictures on China’s policy approach, and China has capitalized on the economic influence over some members for manipulating moves concerning the South China Sea in ASEAN-sponsored meetings. Accordingly, it appears rational to diversify trade and aid destinations of ASEAN member states if ASEAN can become more an effective institution for the contested maritime issues. Identifying excessive economic interdependence with China as a major source of its influence over ASEAN, this paper examines potential roles which regional economic institutions, especially the TPP, can play in terms of reducing the regional economic dependence on China. It argues that if implemented, TPP’s substantial liberalisation, mostly via high standards for trade and investment can depicted as catalysing interconnections in pursuit of common markets and shared economic rules that would ultimately reduce export dependence on China, a key factor in making many states susceptible to Chinese political influence.

1. Regionalism and soft institutional balancing

The balance of power is one of the tenets of realism in international relations theory, and realists consider that states largely take a hard-balancing act, such as military build-ups and alliance formation, so as to preserve their survival and sovereign independence in the international system, and so as not to permit the emergence of preponderant states (Paul, 2005: 51). However, states in the Asia-Pacific region have not adopted such hard-balancing strategy neither against the United States, the preponderant state (Pape 2005, Paul 2005), nor China, the rising state (He and Feng 2008), in the post-Cold War era. Rather, regional states have tended to take a ‘soft’-balancing act against their pressures
or potential threats, by way of, for instance, institutional balancing, which refers to “the activity of restraining a dominant country and reining in its activities in a multifaceted manner by engaging in the establishment, formation, or development of rules, international institutions, and forums of various kinds” (Tokyo Foundation 2011: 34). It is neo-liberal institutionalism that emphasises the need of policy coordination to manage the political complexities arising from growing economic interdependence, and that stresses the importance of international institutions to promote the process towards mutual gains. Yet, regional institutions also encourage a separation of inner and outer status and this network externality causes an unease to outer countries, and some states become tempted to capitalise on this discriminatory nature of regional institutions for its own interests, so realists can also see international and regional institutions as a potential significant tool in power-based international relations.

Institutional balancing takes the form of inclusive or exclusive approach, depending on whether states’ balancing acts include a target state within the institution or excludes it from the institution. Inclusive institutional balancing means ‘states practice norm/rule-building to constrain other states’ behaviour or control and manipulate agendas to address issues related to their interests in multilateral institutions’, while exclusive institutional balancing implies ‘states consolidate their political and economic unity to resist pressures from outsiders’ (He 2008). In short, institutional rules can become a balancing device, particularly if member countries seek to use them in order to shape a regional order and set common rules, which the targeted state finds difficult to accept or involve.

A key mechanism in institutional-balancing, especially designed to exercise an influence on the targeted states through economic agendas is trade diversion from the exclusive nature of Free Trade Agreements (FTAs). Benefits brought to a party to an FTA, such as the elimination of tariffs, generally victimise a third country not included in the agreement. This means a third country’s products that are more competitive in terms of quality and price will be replaced by the FTA country’s less competitive products thanks to the FTA, which will negatively affect consumers of the FTA countries, while exports from the third country to the FTA countries will be blocked and reduced. While tariff-free privileges will be granted to companies in the FTA countries, third country companies will be placed at a competitive disadvantage. The crux of this argument is the difference in economic power of FTA negotiating countries. As Bhagwat (2008: 43-48) indicates, all countries do not wield an equal amount of power; one country may be a major power in a military or economic sense, and thus have greater influence on another, so we often see a pattern where FTAs move forward due to the interest and influence of such hegemonic powers. In the case of FTAs signed by powerful countries, since certain third countries will have their market access inhibited, trade diversion concerns become clearer, which motivate another country to conclude an FTA with the same major power. In this sense, even if small
and medium-sized countries conclude an FTA together, this will not necessarily cause trade diversion concerns, and even if a major economic power were inhibited as a third country, this major power can be said to have few motivations to conclude FTAs with these small and medium-sized countries. In other words, trade institutional-balancing effect would be more influential only when a large-economy takes an initiative. The following sections examine ASEAN, TPP, AIIB and RCEP as an institutional-balancing function, while China has capitalised on its economic prowess for its political and strategic purposes.

2. China’s economic strategy in relation to the South China Sea

The 2000s witnessed China’s charm offensive diplomacy in Southeast Asia, as seen in its engagement in the signing of the ASEAN+1 Free Trade Agreement (FTA) and ASEAN’s Treaty of Amity and Cooperation (TAC) ahead of any other regional country, laying the foundation for China to exercise its economic influence subsequently. In fact, the influence of China’s charm and amicable diplomacy in East Asia made a conspicuous difference compared to Japan’s regional diplomacy, which primarily evolved around the alliance with the United States, especially when Koizumi and Abe were prime ministers (Terada 2010). China’s chief motive behind such an active ASEAN diplomacy lay in its effort to remove the threat perception towards its regionally expanding military and economic influence; a desecuritisation of its rise (Goh 2007). According to Khoo (2011), the extremely high level of precaution against China’s military rise exists as fait accompli in East Asia as a whole, and he concludes that the regional countries’ anxieties on how China would use its growing military capabilities encouraged their support for US continued presence in the region.

Another motive behind China’s active ASEAN diplomacy is seen in its commitment to ASEAN’s economic development to help narrow the developmental gap, then called “ASEAN divide”, between under-developed Indochina counties and the original members of ASEAN. For instance, China, especially Yunnan Province and the Guangxi Zhuang Autonomous Region, engaged in the “Greater Mekong Sub-region Economic Cooperation Program”, with four Indochina countries and Thailand, and actively delivered aid to the advancement of infrastructure and transportation sectors in the region. Consequently, China accomplished the deepening economic interdependence with and the region, as seen in the trade volumes of the two provinces of China soaring 5-fold with Myanmar, 11-fold with Laos, and 6.5-fold with Thailand (Su 2012).

China also endeavoured through its active good neighbourhood diplomacy to make Southeast Asia a cordial region for China, serving as a shield from pressures exerted by other great powers, especially the United States (Zhang and Tang 2005). Any effort to promote economic ties in
ASEAN was viewed as one of the essential approaches for this goal. Former Deputy Assistant Secretary of State, Ellen Frost (2007), coined China’s economic diplomacy as “commercial diplomacy”, arguing that the purpose was to increase its influences on the non-economic sectors, including security, through the exercise of economic power that would provide the access to foreign markets. In fact, the trade dependence on China among US allies in East Asia has skyrocketed. For instance, whereas Japan’s trade with the US decreased from 27.1% to 13.7% between 1999 and 2009, the trade with China rapidly surged from 9.1% to 20.5%. Likewise, China’s trade proportions in South Korea increased from 8.6% to 20.2%, and in Australia from 5.7% to 19.7%, while the US presence in South Korea declined from 20.7% to 9.6%, and in Australia from 15.8% to 8.1% (Yamamoto 2012). In other words, the trade situation of major US allies in the region reversed between China and the US in 10 years in the 2000s. As the then Chinese Foreign Minister Li Zhaoxing expressed, this approach was aimed at “building good neighbourly relationships and partnerships” and “implementing the policy of creating an amicable, secure and prosperous neighbourhood” (People’s Daily, 23 August 2005). Hence, assuring the favourable international environment for economic development, especially through constructing amicable relationships with neighbouring countries, was a critical goal of China’s regional diplomacy (Aoyama 2011).

In 2006, new political concepts, such as sovereignty and security, began to be embedded into the discourse on China’s national interests in which the economic development remained a top priority. As Aoyama (2011) points out, the former President Hu Jintao’s proclamation that “Chinese diplomacy should play a role in protecting the country’s sovereignty, security, and developmental interests” at the Central Meeting on Foreign Affairs Work held in Beijing in August 2006 led to a new slogan of China’s national goal, “protecting the country’s sovereignty, security, and developmental interests”, adopted by the 17th National Congress of the Communist Party of China in the following year.

As the Chinese government revealed guidelines for “developing and implementing a maritime development strategy, improving maritime development and control capabilities, and strengthening integrated maritime management” in the 12th Five-Year Plan published in March 2011 (National Institute for Defense Studies, Japan 2011), it stressed the significance of the ocean for sustainable economic development. For example, as China acknowledged, the reliance on external sources for oils would exceed 50%, a situation which was unacceptable because China esteemed self-sufficiency in national resources indispensable for sustainable economic growth (Masuda 2012). The internal document of the Ministry of Land and Resources of China estimates the potential oil endowment in the region at 2.3 billion to 3.0 billion tons, accounting for one-
third of China’s total oil reserves. Therefore, there are voices in China, deeming the area one of the four largest offshore oil fields in the world and urging its active development. Since the annual average growth rate of China’s primary energy consumption has surpassed 10% for 10 years from 2001 (Nihon Keizai Shimbun; January 1, 2012), the potentially rich resources in the South China Sea has been viewed as essential in this goal. As a result, China has attempted to protect its interests in the South China Sea by any means, even though it occasionally harms its relationships with neighbouring countries. For example, it was reported that Chinese vessels cut a Vietnamese survey ship’s cables in May 2011, and they continued to harass Vietnamese survey ships the next month. Meanwhile, half of the seaborne trade, constituting 90% of the total trade in terms of volume, passes through the South China Sea. Not only coastal nations but also non-claimants of sovereignty in the region – including the US, Japan, South Korea, Australia, and India – pay close attention to the security and freedom of navigation for their trade and energy interests. Consequently, China’s assertive maritime behaviour led to encourage the US to promote multinational security.

It was the survey ship USNS Impeccable were surrounded by Chinese vessels and required to leave the area in its routine operations in international waters in the South China Sea in March 2009 that forced the United States to face China’s assertive attitude in the Asian ocean (Marciel 2009). Although US interest has been securing freedom of navigation in the South China Sea, as well as in the Yellow Sea and the East China Sea, for maintaining the American Navy’s maritime operations, the high officials of the Department of State have never officially mentioned the South China Sea as American foreign policy interest before March 2010 when China was said to refer to it as its “core interest”. Bader (2012) confessed that it was in 2010 when the US acknowledged China’s behaviour on the South China Sea as unprecedentedly different. A regional institution which the US chose as a way of coalition-building for American maritime interest was the EAS.

3. China’s strategic use of economic interdependence

China’s interest in capitalizing on its predominant economic, especially trade, position in other states, for moving the South China Sea issue in its favour, can be found in the following editorial of the Global Times (30 July 2016). In the wake of Australia’s support for the arbitration ruling result with its claim that China must abide by it and the launch of a joint declaration with the US and Japan, the newspaper condemned Australian approach:

Australia has inked a free trade agreement with China, its biggest trading partner, which makes its move of disturbing the South China Sea waters surprising to many…it also intends to suppress China so as to gain a bargaining chip for economic interests. China must take revenge and let it know it's wrong. Australia’s power means nothing compared
to the security of China. If Australia steps into the South China Sea waters, it will be an ideal target for China to warn and strike…Australia is not even a “paper tiger,” it's only a “paper cat” at best.

Connotating the possible use of damaging its economic ties including the FTA, the *Global Times* editorial remained that China actually used its economic clout as a leverage for political purposes. For instance, soon after Lee Hsien Loong, then the Deputy Prime Minister of Singapore, visited Taiwan in July 2004, China suspended all official negotiations with Singapore including the ongoing bilateral FTA negotiations. FTAs are Singapore’s key tool for surviving as a trading nation and thus far singed 20 FTAs with 31 its trading partners, and China’s tactical suspension of FTA negotiations with Singapore substantially delayed the completion with its largest trading partner, threatening Singapore’s independent foreign policy approach. Lee Kuan Yew, then senior minister recalled: ‘Beijing uses its economic and political clout to counteract what it sees as against its interests’ (*Channel News Asia*, 9 May 2008), and, as a result, Lee Hsien Loong has never visited Taiwan since then.

China’s FTA with the offer of its huge market was also effective in driving a wedge into the U.S.-led alliance network in the Asia-Pacific by creating regional institutions that favour its economic strengths. In 2015, China signed FTAs with two key US allies—namely, Australia and South Korea—whose substantial export dependence upon China, at roughly 33% and 25% each, has sustained their enthusiasm for the establishment of preferential trading relations with China via FTAs. Such political vulnerability stemming from excessive trade reliance on the Chinese market has in effect helped Australia and South Korea to dispel US pressure to not participate in the AIIB. China’s strategy of establishing more bilateral FTAs, especially with TPP members, would create more like-minded states that could be mobilised to help China’s political and strategic interests, as demonstrated by China’s massive flow of aid to Laos and Cambodia that has been instrumental in dividing ASEAN members on the South China Sea dispute.

Japan was not an exception, although its economic and technological advantage made it possible for it to eventually frustrate China’s ambition. When a Chinese fishing boat collided with Japanese coastguard ships near the Japan-controlled Senkaku Islands in September 2010 and Japan captured a Chinese fishing boat captain who had encroached on the Senkaku Islands. Japan had relied for more than 90 percent of its imports of rare earth metals, retaliated against Japanese charges by banning their export to Japan. China subsequently then launched a series of protests including postponement of talks with Japan about gas issues in the East China Sea; suspension of ministerial meetings and Sino-Japanese higher-level exchanges; summoning the Japanese ambassador to China five times, once at an undiplomatically early hour of the morning; and the arrest of four Japanese civilians on suspicion of entering a military zone without authorization (*Wall Street Journal*, September 24, 2010). As this
strategy damaged Japanese private sectors, especially the automobile companies which then heavily relied on Chinese rare earth exports, they swiftly worked to develop alternative materials and discovered new procurement routes with other countries including Mongolia and Australia. As a result, the international prices in major rare earth materials substantially dropped and Chinese exporting companies faced difficulty in finding alternative buyers, many of whom eventually went to bankruptcy. This case illustrates the importance of diversifying trade destinations and reducing the heavy reliance on Chinese market to minimize the negative impacts when China uses it for political and strategic purposes. Institutional balancing act sounds effective in this aim.

4. Institutional-Balancing and Ineffective ASEAN-Sponsored Dialogues

While China, the Philippines, Vietnam, Taiwan, Malaysia, and Brunei claim their sovereignty over waters and islands across the Sea, China demands the so-called “9-dashed line”, an area encompassing virtually 90% of the entire South China Sea, based on its historical legitimacy. China has disclosed its intention of neither making a compromise on the territorial disputes related to sovereignty nor following the United Nations Convention on the Law of the Sea (UNCLOS) despite the area in question being widely overlapped with other claimants’ Exclusive Economic Zone (EEZ). Given China’s powerful challengers, such as the United States and Japan who saw China’s claims as groundless and forceful, are geographical “outsiders”, they, as well as claimants from Southeast Asia, under the concept of the rule of laws, have used regional institutions to put collective pressures on China to abide by the rule concerning maritime disputes over the South China Sea. Yet, regional institutions, such as the East Asian Summit (EAS), the ASEAN Regional Forum (ARF) and the ASEAN Defence Ministers’ Meeting (ADMM-Plus) meetings, in which ASEAN takes a responsibility to organise, hardly function to make China attentive to their allegation over the South China Sea. Let me examine the institutional balancing moves against China, the targeted states, in these security and defence dialogues which ASEAN member states rotationally chair, and identify the insufficient effect due mainly to the ASEAN-way as a guiding rule and, more significantly, China’s tactics of nullifying these efforts based on its tactics to use its dominant economic position against the other claimants.

The aforementioned regional security and defence dialogues simply reveals the ASEAN’s incapability to serve as an agenda-setter or to sit in the driver’s seat to lead the wider Asian regional cooperative which can be demonstrated through the following three points. The first is the ASEAN’s ‘talk shop’ metaphor, which connotates that regular meetings of leaders and ministers involving the big outsiders are held with pomp, ceremony and noncommittal statements. ARF and EAS in recent years simply disclosed a habit of disagreement in the process of making joint statements, in which China and the U.S./Japan are at loggerheads over their agendas related to maritime territorial disputes. The second point is the ineffectiveness of ‘ASEAN Way’ formula, which stipulate a consensus-based, decision-
making, non-binding and non-interference principle. This non-commitment attitude to hard issues, including maritime territorial disputes, makes it difficult for the ASEAN to take a united approach and results in it not acting as an effective shield to protect the interests of some member states in the South China Sea. The third and final point is the ASEAN divide reality, one that features divergences in economic performance, industrial structure, infrastructure and the level of privatization among members, as seen in below. This renders least-developed members rely on external powers such as China, rather than ASEAN fellow members, for a source of capitals and technology for their development.

**Asean Divide**

![Nominal GDP per capita, 2014](Source: IMF, World Economic Outlook 2015 Apr.)

Yet the talk shop’s value could be enhanced if delegates discussed the hard issues, regardless of whether any binding obligations ensued. Prior to Hilary Clinton’s participation as then Secretary of State in the 2010 EAS, ASEAN had never successfully acted as an effective shield to protect the interests of its members in territorial disputes. However, the United States, playing a key role in placing the disputes on the ARF agenda in the same year, confronted China over the territorial disputes in the South China Sea. Of significance was the United States claimed that both parties should provide ‘legal evidence’ to support their territorial claims. This legal-based approach to the territorial disputes, initially promoted by the Philippines, was something China had previously not paid serious attention to. The United States then saw the EAS as a useful platform in which it could put pressure on China’s maritime actions. At the 2011 EAS, furthermore, given all the participating countries, except Myanmar and Cambodia, touched on the South China Sea disputes (*Strait Times*, 27 November 2011), implying the encirclement against China through dialogue was formed. The “Declaration of the East Asia Summit on the Principles for mutually beneficial relations” stipulates the respect for International Law as the US claimed. As a result, China was forced to consider making a legally-binding “Code of
Conduct in the South China Sea” as demanded by ASEAN, in lieu of a non-binding “Declaration on the Conduct of Parties in the South China Sea” signed in 2002 (Nihon Keizai Shimbun, 20 November 2011).

As ASEAN is not a concerning party itself, however, the transformation of EAS did not fully support the US intention. For example, the “Six-Point Principles on the South China Sea”, agreed in July 2012 among ASEAN members, neither led to the resolution of the dispute, nor even influenced China’s persistent claim of a bilateral negotiation approach. More significantly, the split of ASEAN solidarity was jeopardized after Laos and Cambodia – the two ASEAN members receiving massive economic assistance from China – supported China’s proposition, which has resisted against the inclusion of the third-party voice in this dispute. For instance, Cambodia, the 2012 ASEAN chair, ran the proceedings in a direction in accordance with the wishes of China with regards to the problems in the South China Sea. This provoked a reaction from the Philippines and Vietnam, which were opposed to China’s assertions in this sea. Furthermore, ASEAN eventually became reluctant to support Japan’s 2011 proposal of the establishment of an East Asian Maritime Forum which would replace the existing ASEAN Maritime Forum, due to its fear of losing its voice in this area, disproving Japan’s attempt to build a coalition with some ASEAN states within a multilateral forum against China over maritime disputes including its own Senkaku Islets issue. This was due partly to China’s successful tactics of making Laos and Cambodia more susceptible to China’s interest through offering them massive economic assistance. Again, at the Asia-Europe Meeting held in October in 2012 in Laos, Chinese Premier Wen Jiabao, sat beside the Laotian Prime Minister, the chairperson of the meeting. This was an anomalous case in terms of the ceremonial custom which ASEAN has nurtured, indicating an exceptionally friendly relationship both nations have established, especially through China’s tactical use of its economic power for Laotian development. The ADMM-Plus meeting held in Malaysia in November 2015 was ASEAN’s another failure of adopting a joint statement due to disagreements on the South China Sea. The ADMM plus framework is a newer, expanded version of the ADMM, the flagship element of the ASEAN Security Community. The statement itself is normally unremarkable but what did have an impact was the intra-ASEAN divisions on the issue, spurred by China’s economic clout. It can clearly tarnish the ASEAN’s image – putting major powers into an ASEAN-centric regional architecture - and hinder the group from having a greater influence in regional security. For instance, while ASEAN and China have been negotiating a Code of Conduct (COC) under the auspices of the interim Declaration on the Conduct of Parties in the South China Sea (DOC) signed in 2002, which took 20 years to conclude, they have made no serious progress during the last 15 years. ASEAN has allowed China to buy time for building artificial islands, possibly turning them into military and logistical facilities, including one around the Scarborough shoal.
In short, ASEAN-sponsored security dialogues have been well manipulated by China, which has used its economic aids or markets to make ASEAN members support its territorial claims in South China Sea. As a result, ASEAN does not effectively serve as an institution which the US, Japan or Vietnam can utilise as a soft balancing mechanism.

5. **Institutional balancing act and TPP**

The Obama administration’s “Asia pivot” or “rebalancing to Asia” strategy is an attempt to reinsert the United States into regional strategic and economic games, and this shift is perhaps most evident in the administration’s focus on the Trans-Pacific Partnership (TPP) agreement. Michael Froman, U.S. Trade Representative, recently declared that the TPP was essential not only for its economic benefits, but it was also significant from a geopolitical viewpoint, stressing America’s economic engagement as the foundation for regional security which has been destabilized, according to Defence Secretary Chuck Hagel at his 2014 Shangri-la Dialogue speech, through China’s “unilateral actions asserting its claims in the South China Sea”.

Dubbed the “platinum standard,” the agreement imposes greater tariff concessions and deregulations than afforded by the WTO—WTO-plus provisions—and includes additional economic rules—WTO-extra provisions—, which affect state-owned enterprises, intellectual property, government procurement, and environmental and labor standards, the TPP emerged as a potential tool to encircle, or restrict China’s massive economic power in the region. The exclusion of China from TPP served as a major condition as an exclusive institutional balancing tool. In short, if TPP achieved the promised liberalization by reducing exemptions through high-standard rules in trade and investment, it could lead to deeper economic interdependence and interconnections among like-minded states. That result would reduce those states’ trade dependence on China and their vulnerability arising from trade and investment reliance on the Chinese market. This was a useful way to stay out of China’s attempts to exercise political influence on the basis of a substantial economic presence.

A key argument was whether the regional trade pact can help to form cohesion within institution to impose an effective pressure on China. According to Xinyuan Dai (2015), the TPP has presented a dilemma to China: if China does not enter the TPP, it would miss out on the benefits of the world-largest free trade areas as well as the opportunity to shape the rules that would hold dominant impact to regional economic governance. On the other hand, it is also problematic that China has not always wanted to follow the Western liberal rules. Having different economic systems, it would be difficult for China to embrace the ideologically different principles of the TPP, so-called ‘universal values’ such as freedom, democracy, basic human rights and the rules of law, which impose some serious challenges to China’s state capitalism. China is thus stuck in the sense that it faces two similarly undesirable
options: “joining the TPP would be painful, but saying out might be worse”.

If ratified, the TPP would raise the cost of non-participation in the partnership; outsiders would continually fail to secure maximum trade and investment benefits. The estimates made by a 2016 World Bank report support this view; Vietnam was expected to enjoy the largest gain of 30.1% increase in exports, followed by Japan at 23.2%, putting pressure on their non-participating neighbours, such as Thailand and South Korea, whose exports would decrease due to the trade diversion effects (World Bank 2016). So, whether or not China’s participation in the TPP was possible has the crux of the argument in this new era of Asian regionalism. Michael Froman, the then US Trade Representative, set the conclusion of a bilateral investment treaty with the United State as a precondition for China’s entry by declaring “it’s a good test case to see whether China is willing and able to meet the high standards that we insist on” (Wall Street Journal, 15 October 2015). Furthermore, entry into the TPP as a latecomer would also require China to accept all 30 chapters agreed upon by the 12 founding member states, including those regarding environmental standards and stronger intellectual property rights, which will leave China little room to introduce national preferences into the agreement’s structure. At this point, however, it is still difficult for China to become ready to commit to the TPP’s high-standard agendas.

Observing the TPP’s basic agreement in October 2015, Thailand, the Philippines, and Indonesia expressed interest in joining the TPP, and the US–ASEAN Summit, slated for February 2016, is aimed at bolstering US endeavours to urge those and other ASEAN members to join the TPP in the near future. China has already replaced the United States as ASEAN’s trading partner by increasing its trade proportions in ASEAN to 14% in 2013, while American share in ASEAN’s total trade volume decreased from 16% in 2000 to 8% in 2013 (Nihon Keizai Shimbun, 18 February 2016). Including those ASEAN members, the United States can expect the TPP to help ASEAN broaden and diversify its trade direction and reduce its dependence on the Chinese market.

In fact, China’s concerns about the negative impact the TPP might have on its regional integration policy, especially due to the potential trade diversion effect, were so strong that when Japan initially expressed an interest in joining the TPP, China quickly became more flexible in its own talks with Japan. For example, China accepted a proposal from Tokyo to conclude a trilateral investment agreement first among China, Japan, and South Korea (a framework that Beijing had previously resisted due partly to the required protections for Japanese and South Korean investors). China has also been moving away from its exclusive pursuit of an ASEAN+3 regional framework toward greater interest in the ASEAN+6 framework, which is Japan’s preferred arrangement. These two Chinese concessions led to the start of official negotiations on the CJK FTA and the RCEP in 2013.
6. Role of AIIB

Many ASEAN member states’ more urgent interests, however, concern the needs of infrastructural development. The AIIB, which with $100 billion USD in capital has become a pivotal component of the Chinese version of the “rebalance Asia” strategy, thus became popular among such countries. The rapidly growing demand for infrastructural development in Asia, including railways, roads, and energy—estimated to cost 8 trillion USD during 2010–2020—cannot be fulfilled by existing multilateral banks, whose burden the AIIB promises to reduce (ADBI 2010), as seen in the chart below. More importantly, however, the AIIB can serve as a critical institution whose management and administration China can dominate without US and Japanese involvement, catalysing China’s further connectedness with Asia, including many ASEAN member states through its own management and governance approaches, as Chinese Minister of Finance Lou Jiwei, indicated that China has little appetite for rules that the United States and Japan have cherished, given his claim that “the West puts forward some rules that we don’t think are optimal” (Nihon Keizai Shimbun, 22 March 2015).

A good example of Southeast Asian’s aspiration of infrastructure funds can be found in the case where Indonesia decided to offer China the Jakarta–Bandung high-speed rail project contract in September 2015, despite Japan having been involved in the project since 2008 and China for hardly more than half a year. Key components of the Chinese proposal include funding that does not require the Indonesian government to provide any guarantee or state budget and a completion timeframe of only three years, which means the project will conclude while President Joko Widodo is still in office. Moreover, China has agreed to jointly produce train cars not only for high-speed trains, but also
electric and light rail, all of which would be used in the local train system. To support the program, China has even agreed to build an aluminium plant to provide raw materials to manufacture train cars. Overall, China’s offer—perhaps only to win the bid—seems to be overkill for only 150 km of railway. From one angle, China’s generous approach to Indonesia’s high-speed railway contract is a reflection of its eagerness to realise its One Belt, One Road initiative, a strategy in which Indonesia forms the eastern edge. Moreover, encouraging some ASEAN states’ reliance on Chinese financial prowess for their infrastructure, the AIIB can also offset the TPP’s institutional balancing function to facilitate the reduction of their trade reliance on China.

**TPP’s demise and RCEP’s rise**

When newly inaugurated US President Donald Trump withdrew the United States from the TPP in January 2017, a key driver for institutional balancing tactics disappeared for nations which intended to reduce their overreliance on Chinese money and market. Owing to the TPP’s demise, RCEP has emerged as an alternative regional integration framework possibly serving as a rule-setter in the Asia-Pacific region. RCEP can be viewed as a case of intra- or inclusive institutional balancing, which some nations such as Vietnam and Japan see as a tool to constrain China’s power and influence in pursuit of rule-making within the same multilateral institutions. Yet, RCEP’s function to restrain China’s aggressive behavior through having closer institutional links with is small. China’s commitment to the RCEP is strongly oriented toward developing countries and favors more exemptions in the form of tariff elimination duties, with few deregulation requirements and consequently few reforms required of domestic economic systems. RCEP’s speed and level of liberalization is going to be based on the standard that China, India and ASEAN’s developing countries generally prefer, the so-called a “lowest common denominator” dilemma in terms of liberalization. For example, with regards to the contents of the RCEP, Singapore and Malaysia have called for wide-ranging liberalization, including not only goods but also services and investment, whereas Indonesia, which is on the receiving end of a flow of cheap Chinese goods and is concerned over a ballooning trade deficit with China, is opposed to FTAs with high liberalization rates. Within the RCEP, Japan suggested eliminating tariffs in more than 90 per cent of products within ten years, and setting three stages on tariff eliminations (immediate, within ten years, and over ten years), with the intrinsic motive of protecting its domestic agricultural sectors from liberalization. However, this agenda was received negatively by both advanced and emerging countries. Australia and New Zealand, with their intense motivation to increase agricultural exports, insisted on the no-exemption principle, whereas India, Myanmar, and Cambodia disapproved of the condition of “more than 90 per cent”, as they still maintain higher tariffs (Nihon Keizai Shimbun, 28 September 2013). RCEP would be eventually established as a low-quality FTA, offering members less strict binding-rules and less ambitious liberalisation package than the TPP, having a limited impact on the members’ trade and business relations with China.
China’s interest in the RCEP has been urged by the development of the TPP negotiations, especially after Japan’s decision to participation in it made by Prime Minister Shinzo Abe in March 2013. The exclusion from the US-led TPP was considered to be harmful on the Chinese economy through the effect of trade diversion. A source of China’s concern over the TPP and expectation towards the RCEP can be identified in a simulation study, as seen in the Table 1, which assesses that the TPP, if launched, would cause a substantial loss to Chinese economy. Yet, the losses could be offset and even overcome if RCEP were realized since it would provide China with preferential access to countries which join both the RCEP and the TPP such as Japan. This symbolises the TPP’s effectiveness as an institutional-balancing tool in reducing TPP member states’ reliance on Chinese market.

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**Conclusion**

This paper views the TPP as a potential tool for ASEAN to reduce its heavy trade reliance on China. If the TPP were ratified and the Philippines, which used to be one of the least FTA-oriented nations in East Asia, were to join the TPP, all claimants to the Spratly and Paracel Islands from ASEAN would be TPP members, illustrating the significance of United States’ commitment to Southeast Asian stability and highlighting the effectiveness of the TPP as a coalition-building mechanism to put collective pressure on China. This view was expressed by Japanese Deputy Prime Minister Taro Aso, who thought the TPP would catalyse the United States–Japan partnership, which can act as “a mega stabilizer across the Pacific” (Aso 2013), including the South China Sea.
China’s strategy of using its substantial economic presence in Southeast Asia for manipulating ASEAN’s move on the South China Sea in its favour is premised with the “ASEAN way”, which informally stipulates non-intervention, non-binding, and consensus-based decision-making approaches to regional cooperation. Should ASEAN decide to move to eliminate or modify the consensus-based decision-making approaches to be replaced by majority-based decision-making ones, China would be urged to create another scheme to make ASEAN member states more depended on its trade and aid. The ASEAN Way is considered to be an impediment to a high level of regional institutionalization, which the ASEAN Economic Community aims to accomplish, because it tends to avoid transnational cooperation which often requires the imposition of regulations and obligations on each state. Regional integration through the TPP or even RCEP, which involve legally binding provisions for the reciprocal exchange of preferences that discriminate against non-partner countries is inharmonious with the ASEAN Way. It seems that a mismatch between ASEAN norms and economic integration practices has hindered the further institutionalization of ASEAN economic cooperation and exposed its fragility to China’s pressure on the South China Sea, underlining the serious problem the ASEAN, as an actual international actor, currently faces. Now that the TPP’s fate is uncertain and US President Donald Trump has no faith in multilateralism and has paid little attention to ASEAN, it is a time for the ASEAN to change its long-retained rules and norms, including the non-intervention principle, in order to make itself more relevant to the rapidly changing regional structure, perhaps as an effective institutional balancing tool by itself.

**Bibliography**


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