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# Conflicts in the South China Sea and China- ASEAN Economic Interdependence: A Challenge to Cooperation

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## **Abstract**

This paper analyzes the absence of correlation between China-ASEAN economic interdependence and dispute settlement in the South China Sea, against liberals' prediction. It argues that there are a few trends in the dispute settlement process that reflects liberalist theory irrelevance, i.e. (1) the main feature of the dispute settlement is power politics; (2) the progress of multilateral arrangement for dispute settlement is constrained by unilateral policies; (3) the deepening economic integration and growing interdependence are intentionally maintained exclusive from and thus have little impact on the on-going disputes; and (4) the constrained multilateral arrangement through ASEAN invites further power politics between the claimants and actors from outside the region. It also argues that three factors have contributed to the trends: i.e. (1) power structure in the region; (2) divergence of each actor's geopolitical interests and strategies in the South China Sea; (3) weak regional coherence and institutional design.

Keywords: China, ASEAN, South China Sea, dispute settlement, economic interdependence, regional economic integration.

## **Biography**

Mr Meidi Kosandi (born May 13, 1976) is a researcher from the Universitas Indonesia, Jakarta. He obtained his bachelor's degree (2002) from the Universitas Indonesia; his MA (2007) from Ritsumeikan University, Kyoto; and PhD degree (2012) in International Relations from Ritsumeikan University. He served as Head of Planning and Development Office at the Universitas Indonesia (2010–2012). His recent publications include “Japan’s Diplomatic Dilemma toward North Korea” (2008), “Parallel Evolution of Practice and Research on ASEAN Economic Integration: From Paradigm Contestation to Eclectic Theorizing” (2012), and “Shifting Paradigms and the Dynamics of Indonesia-China Relations: Towards the Best Use of Theoretical Eclecticism” (2013). The latest research he conducted was on “Cooperation and Development in the South China Sea: Coping with the Potential Hindrance of East Asian Integration”, under the ASEAN-Canada Junior Research Fellowship Program 2012–2013. In 2013, he also had served as policy advisor for Indonesian National Planning and Development Agency.

## **Introduction: Integration Paradox**

It is not an exaggeration to say that the South China Sea (SCS) disputes between China and the Association of Southeast Asian Nations (ASEAN) claimants<sup>1</sup> generate paradox in the East Asian<sup>2</sup> regional integration. Although economic integration between China and ASEAN has been deepening since the 1990s in terms of trade and investments, the SCS issue remains a significant stumbling block for further integration with reference to institutional arrangement for dispute settlement mechanism. Tensions between China and two ASEAN claimants --Vietnam and the Philippines-- have recently heightened and affected their economic relations respectively.

Since the rapprochement in the early 1990s<sup>3</sup>, economic integration between China and ASEAN has been deepening. Trade between ASEAN and China boosted more than 36 times throughout 1990s and 2000s, from \$7.96 billion in 1991 to \$292.78 billion in 2010 (He Shan, 2011). In the 2000s, China had become the primary trading partner of ASEAN surpassing Japan, the United States (US) and the European Union (EU); while on the other hand, ASEAN also had become the third largest trading partner for China, surpassing Japan. ASEAN-China Free Trade Agreement (ACFTA) has been in effect since 2010 and boosted regional trade ever since. Even in the face of global economic crisis in 2008, the region is considered by international financial institutions<sup>4</sup> as the motor for global economic recovery for its sustainable high growth.

A paradox reveals as we juxtapose economic relations and the political dynamics of SCS affairs. According to many liberal theorists, increasing economic interdependence and deepening integration should reduce conflict potentials between states (Cobden, 1903: 225; Angell, 1933: 33; Keohane and Nye, 1977: 29; Rosecrance, 1986: 13-14; Copeland, 1996: 5; and Keohane, 1998: 85-86). Integration and interdependence increase incentives for cooperation and costs of conflict and defection. Liberals argue that states in an integrated regional economy tend to cooperate and avoid conflict.

What happens in the SCS has so far been quite different from what liberals might expect. Increasing economic integration and interdependence do not automatically cause cooperative gesture in solving disputes in the SCS. Quite on the contrary, tensions between

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<sup>1</sup> Six countries claimed for sovereignty on the SCS waters, islands and islets. The claimants include China, Taiwan, Vietnam, the Philippines, Malaysia, and Brunei Darussalam. This paper pays particular focus to the disputes between China and ASEAN claimants.

<sup>2</sup> East Asia in this paper refers to the broader meaning of the region, consisting both Northeast and Southeast Asia; not just referring to Northeast Asian part of the region. ASEAN, while not a single actor independent from state's policy or supranational organization, is treated as a different entity from state that facilitate regional unity and policy convergence. In the practice of diplomacy, ASEAN is also treated as a different actor in diplomacy from single memberstates. ASEAN relations is often treated differently from bilateral relations with a single member. So analyzing ASEAN as an actor in SCS diplomacy is not intended for anthropomorphizing, but only based on the fact that the Association plays a certain role that any single member does not.

<sup>3</sup> During the Cold War, China was among the outside powers that was involved in the proxy wars in the region. ASEAN on the other hand, was determined to keep the region free from great power competition as reflected in the signing of Zone of Peace, Freedom, and Neutrality (ZOPFAN) agreement. Indonesia was particularly cautious of China's involvement in communist insurgencies in the region and froze diplomatic relations in 1967. Singapore did not establish normal relations with China out of respect to Indonesia's stance. Brunei, as one of the claimants of the SCS also did not maintain diplomatic relations with China. The end of the Cold War made possible for China to normalize of relations with Indonesia in 1990, and established relations with Singapore in 1990, and Brunei in 1991.

<sup>4</sup> East Asian significant contribution to global economic growth has made many among economists consider the region as the engine of growth for the rest of the world. See for instance, Lipsky (2009) and Drysdale (2011).

China and ASEAN claimants were heightened recently, following each claimant's unilateral policies and reluctance to multilateral solutions. Multilateral efforts by ASEAN to promote peacebuilding in the region by organizing talks and agreements were at times considered progressive. The Declaration of Conduct (2002) was considered a stepping stone for further dispute settlement among the "parties". So far, this is the only institutional arrangement to solve the disputes, in which the parties can promote peace and cooperation through dialog. The effort to follow it up with the formulation of a Code of Conduct have not yet materialize after 11 years. Despite the progress in the multilateral efforts since 1990s, military clashes still occur and tensions often heightened between the claimants. Recently, China sent hundreds of its fishermen to the disputed waters, raising tension with its Philippines and Vietnamese counterpart (Asia Times, 10 April 2013). In addition, Taiwanese administration protested Philippines' attack on its fishing boat on May 9, 2013 (China Post, 10 May 2013). The aggression made 52 bullet holes on the Taiwanese fishing boat and killed one fisherman (BBC News, 12 May 2013). In general, security and stability in the SCS seems vulnerable at this point and armed conflict can abrupt anytime between the claimants.

The lack of impact of the deepening integration on peace and cooperation in the SCS provides some challenges for liberalist perspective on regional economic integration. It leads us to the question of what factors have caused the absence of integration spillover in the disputed SCS. Why economic interdependence has not reduce conflict potentials between China and Southeast Asian claimants? Why has tensions and sporadic clashes occurred despite increasing economic interdependence?

This paper discusses relation between peace and economic interdependence regarding SCS disputes between China and ASEAN claimants. If peace and cooperation is inherent in most integrated economies, this paper questions the distinctive picture that East Asian had shown in relation to the SCS disputes. Four issues are to be analyzed in the study, i.e. (1) interdependence among East Asian states; (2) tendency towards unilateral development policy in the disputed area by any single claimants; (3) reluctance to joint cooperation and development in the disputed area by two or more of the claimants; and (4) the dynamics of the bilateral and multilateral negotiations on the dispute settlement mechanism.

The economic stakes in the SCS, the strategic role of ASEAN in the region, and the transition of power structure in the region have made studies on the disputes settlement mechanism important and timely. The stakes of conflict escalation in the SCS are high to both claimants and non-claimants. Approximately 2,700 ships pass through the waters everyday. 50 % of Asia's oil supply, including 60 % of Japan's oil import, and 80 % of Asia's strategic goods also pass through the SCS (China Business - Philippines, 2011). The sea lane also utilized by approximately one third of world trade (Schofield and Storey, 2009).

ASEAN strategic role in the region is also at stake should the on-going conflict lead to a new power structure that would not ensure peace, stability and cooperation. ASEAN has been effective in maintaining peace and cooperation in Southeast Asia since its inception. Not only will it prevent intramural conflict, but it also contains the spread of great power competition to the region during the Cold War. Moreover, it plays a role in mediating and facilitating East Asian integration especially noticing the complexity of relations between the Northeast Asian states. Sustained conflict potentially leads to a new great power competition in the region and undermine ASEAN strategic role. If this is the case, international relations in the region will be shaped by the great powers, instead of East Asians collectively (Ba, 2011).

In addressing the research questions above, this paper will be organized into three sections. The first section discusses briefly the theoretical underpinnings of this research. The second section discusses on the dynamics of the SCS disputes throughout history,

states' strategies and motives in dealing with the issue. The construction of regional mechanism to deal with SCS disputes through ASEAN and its effectiveness will also be discussed in this section. Section three discusses the growing economic interdependence between the states in the region and its impact on states' attitude toward peace and cooperation. And lastly, we will conclude this paper with summary and some theoretical implications of this study.

### **Economic Interdependence in Liberalist and Realist Perspectives**

Liberalists and realists have different perspectives on the impact of economic interdependence on the tendency toward peace and cooperation. Liberalists argue that economic interdependence affects states' cooperative behavior. The theory was based on a set of assumptions. The first is that states pursue policies that serve their best interest. Second, cooperation or policy convergence should serve the best interest of states because there are incentives for cooperation and costs for defection, including crisis and losing the opportunity to gain the benefit. According to this theory, states would rather cooperate than defect.

Realists, on the other hand, argue that interdependence increase, instead of decrease, the likelihood of war. In realist perspective, in dealing with international anarchy, each state is concerned with its own security. Interdependence, on the other hand, reflects vulnerability and lack of autonomy in certain resources. Thus, in order to secure access to resources, states in interdependency relations tend to initiate war.

To both realists and liberalists, economic interdependence is not the only factor that determine the likelihood of war and peace. Liberals develop other explanations for the tendency to peace in addition to economic interdependence, such as democratic peace and international institutions (Russett and Oneal, 2011). Realists also see interdependence as one contributing factor to initiate war, as long as significant trade is present between the conflicting states. Without significant trade relations, interdependence is no longer relevant as one of the factors that lead to war. Besides interdependence, to realists there are other systemic factors that contribute to war and conflict, such as relative power/capabilities (Waltz, 1979).

The roots of liberalist theory on economic interdependence can be traced back from the 19th century (Copeland, 1996). Richard Cobden in the 1850s introduced the idea that international trade "unites" states, in which states became "equally anxious for the prosperity and happiness of both" (Cobden, 1903). Norman Angell (1933) added that states in modern world have to choose between the new system, that is benefiting from peaceful trade, and the old system of power politics. According to Angell, although war is profitable, it damages the opportunity to benefit from commerce in the long term. Modernization in taxation and finance had increased the benefits of trade and costs of war. To Angell, war is unprofitable compared to international trade, and thus occurrence of wars were affected by misperception of leaders on the benefit of war.

Keohane and Nye (1977) argue that a "complex interdependence" is characterized by multiple channels, absence of hierarchy, and the absence of use of military force and power balancing, increase the probability of peace and cooperation, instead of war and conflict. Keohane and Nye assert that the formation of complex interdependence is closely related to international organizations.

For Richard Rosecrance (1986), the two systems in the modern world after 1945 are trading system and territorial system. Trading states are concerned with promoting wealth through commerce, while territorial states are obsessed with military expansion. For Rosecrance, interdependence reduces the probability of war. On the one hand,

interdependence has dyadic impacts on two or more parties, making peace and stability as collective interests. States gained more benefit by domestic economic development and increasing trade. On the other hand, modern economy and warfare had increased the cost of war, including economic adjustment in the post-war development.

Copeland (1996) argues that leaders' expectations of future trade relations are the more important factors. When leaders perceive interdependence among states high and expect long-term benefit from sustainable trade, they would rather choose peaceful trade and avoid conflict. On the contrary, leaders who do not expect future trade have less tendency toward peace and cooperation. Copeland also shows that liberalists' assertion of the relation between interdependence and peace are internally consistent from time to time, that interdependence increase the likelihood of peace maintenance.

The roots of realist perspective on economic interdependence was even farther back to 17th century. Realist understanding of economic interdependence can be found in mercantilism (Hamilton, 1888). Mercantilist idea of imperial expansion derived from vulnerability created by dependence, whether it is mutual or asymmetric. It argues that states, responsible to maintain its power and security, have to overcome its dependence by extending its power and control over scarce resources.

Neorealists assert that interdependence increase the likelihood of war (Copeland, 2001). States, concerned with security, are at discomfort with dependence. When there is a problem in the supply, dependence on foreign factors of production can lead to domestic crisis. During oil crisis in 1970s for instance, initiated by embargo from Organization of Petroleum Exporting Countries (OPEC), many states were exposed to crisis. Therefore, it is only logical that states, from neorealist perspective, intend to control energy resources. Dependence in this case provides the impetus for waging war.

Waltz (1979), however, argued that interdependence not always lead to war. States' tendency toward war is also affected by the power structure. According to Waltz, there are three elements of power structure: i.e. (1) international order, whether it is hierarchic or anarchic; (2) characteristics of the units, whether it is functionally alike or different; (3) distribution of capabilities, which is states' relative power to each other. Interdependence in hierarchic system and highly specialized, with relatively equal distribution of capabilities, is less likely to lead to war. On the contrary, interdependence in anarchy, lack of specialization, and asymmetric relative power, will be more likely to lead to competition and in turn, war.

When faced with high level of economic interdependence, according to Joseph M. Grieco (1995), states usually opt for institutional balancing. High interdependence in the globalization era has resulted in so high cost of waging war that even a great power can not afford. Institutional balancing become a preferable strategy to balance without the necessity to engage in major wars. Institutional balancing is often called as soft balancing in neorealist discourse. According to T.V. Paul (2004) soft balancing differs from hard balancing that emphasizes deterrence. Soft balancing includes limited military build-up, ad-hoc cooperative exercises, or collaboration in regional or international institutions. Paul notifies that these policies may be converted to open, hard balancing strategies if and when security competition becomes intense and the powerful state becomes threatening. Grieco argues that the form of institutional balancing can be internal by engaging the great power or external by excluding the great power from the institutional cooperation.

In sum, virtually there seems to be an agreement among scholars from both perspectives that economic interdependence affects states' policies and strategies in international relations. The two camps differ in what effects that interdependence caused and what kind of response materialized the states' policies and strategies. In liberal perspective, economic interdependence decreases the likelihood of war, while in realist

perspective, it increases the likelihood of war. Liberals consistently argue that states in interdependence would rather choose peaceful cooperation and avoid conflict. Realist, in general denounced liberals' idea based on argument that systemic factors affect leaders' worldview, and in turn, their policy and strategic options.

Next, this paper will examine the relevance and applicability of these theories in the SCS case. Is realist argument relevant to explain SCS disputes in an integrating East Asia? Is liberal prescription to promote peace and cooperation by increasing interdependency applicable in the SCS? The next two sections of this paper discuss the answers.

### The Dynamics of SCS Disputes between China and Southeast Asian Claimants

The overlapping claims over sovereignty in the SCS are mainly driven by geopolitical interests (Thayer, 2012). There are several reasons why the SCS is geopolitically appealing to the claimants. First, energy resources in the waters are believed to be ample. The US Geological Survey (USGS) version estimates the the SCS contains 28 billion barrels of unproved potential oil resources (GlobalSecurity.org, 2013). A survey by the Chinese National Offshore Oil Company (CNOOC) in November 2012 reports an estimation that the SCS holds around 125 billion barrels of oil and 500 trillion cubic feet of natural gas (US EIA, 2013). Table 1 below shows oil production in the SCS based on EIA survey.

**Table 1. South China Sea estimated conventional hydrocarbon production**

Country	Estimated production in South China Sea (2011)		Major exploration and production areas	SCS contract holders and operators	
	Oil <sup>1</sup> 1000 barrels/day	Natural gas billion cubic feet		National oil companies	Foreign firms
Brunei	120	400	Baram Delta	PetroleumBRUNEI	BHP Billiton, ConocoPhillips, Hess Corporation, Kulczyk Oil Ventures, Mitsubishi Corporation, Murphy Oil, PETRONAS, Polyard Petroleum, QAF Brunei, Shell, Total
China	250	600	Pearl River Mouth Basin Qiongdongnan Basin	CNOOC Sinopec CNPC	BG Group, BP, Chevron, ConocoPhillips, Eni, ExxonMobil, Husky, Newfield, Shell, Total
Malaysia	500	1,800	Sabah Sarawak Malay Basin (w/ Thailand)	PETRONAS	Lundin, BHP Billiton, ConocoPhillips, ExxonMobil, Hess, KUFPEC, MDC O&G, Murphy Oil, Newfield, Nippon, Petrofac, Roc Oil, Shell, Talisman Energy
Philippines	25	100	Palawan Basin	PNOC	ExxonMobil, Shell
Vietnam	300	300	Cuu Long Basin Nam Con Son Basin	PetroVietnam	KNOC, ConocoPhillips, Geopetrol, Premier Oil, PTTEP, Santos, SK Corp, Total, Zarubezhneft

<sup>1</sup> Oil production includes lease condensate.

Sources: U.S. Energy Information Administration, Oil & Gas Journal, IHS, CNOOC, PFC Energy.

Second, the area is also contested for its rich fish productivity. The SCS waters extending from the Philippines, Indonesia and Malaysia create an interconnectivity of coral reefs conducive for marine biodiversity that increase fish productivity. In addition, it is also located in the migration path and breeding ground of yellow fin tuna. Its total commercial fishing output is around 8 percents of world's total, or seven million tons of fish with total estimated value of \$ 6.5 billion (China Business – Philippines, 2011).

Third, the waters is regarded an important route for international trade with, within, and through the region. It is a crossroads of world's major oceans and an important Sea Lines of Communication (SLOC). East-West route between Indian and Pacific oceans; and

North-South route between Australia and Northeast Asia are connected by the SCS. Every year, around 70,000 ships utilize the sea lane carrying approximately one third of world trade (Schofield and Storey, 2009; China Business – Philippines, 2011).

Although overlapping claims over the territory had occurred since colonialism era in the 19th century, many believe that the main event in history that contributed to the complexity of sovereignty disputes over the territorial waters was Japan's defeat in the World War II (WW II) and San Francisco Treaty in 1951 that forced Japan to leave the South China Sea in *vacuum* of power. The first state to ever claim the SCS was China in 1279 which drew a territorial map of its power that include the waters. The map, however, provides only weak evidence for any claim as China's power conception was based on Confucian tradition that placed the waters in the sphere of influence without definite linear boundaries (Valencia et.al., 1997). In the 19th century, Vietnam claimed Paracel islands in 1816 and built a pagoda on one of the islands in 1835 (Samuels, 1982). In 1876, China made the first documented claim on the Paracel islands and in 1883 it expelled Germans from Spratly islands (Rowan, 2005). French controlled a portion of the Paracel islands after the Sino-French war 1884-1887, while the US acquired control over Philippines from Spain after the Treaty of Paris in 1898 (Elleman, 2001).

In the first half of the 20th century, China, Japan and France claimed sovereignty of the waters. China incorporated the Paracel islands under Guangdong Province in 1902. Later in 1927, Japan joined the contest of sovereignty claim over the Paracel and Spratly islands with documented claim. In response, China in 1928 officially stated that the Paracel islands are the southernmost limits of its territory and France in 1931 also restated its claim over the Paracel Islands. However, Japan obtained control over the SCS in the first year of the World War II in 1939.

As the war ended in 1945, Japan's defeat had reinstated the vacuum of power in the SCS. The signing of the Treaty of San Francisco between Japan and the US assigned Japan to annul its control over the SCS, but there was no further clarification of who had the rightful sovereignty over the waters. The Republic of China reiterated its claim over sovereignty on the Paracel Islands as soon as 1946. In 1947 the Chinese administration made a map displaying the nine-dashed line that covers almost the entire Scarborough Shoal, Paracel and Spratly Islands. The range claimed territory is around 1000 nautical miles from the outer tip of Chinese coast, but recent development of "fisherman" bases provides the major power with capacity to project power in the area.

Vietnam's claim on sovereignty in the SCS in the Post-WW II was denoted by France in 1954. Its claim was based on historical data and continental shelf principle (Rowan, 2005). Vietnam holds Vietnamese Courts document during King Le Tanh Tong's regime (1460-97) and well documented in the maps produced in the 17th century. Vietnam also asserts that French claim of sovereignty of its colony in Vietnam which included the entire Spratly and a portion of Paracel Islands justifies its claim over the same territory. Vietnam has developed infrastructure for military presence on 9 islands, small airstrip on Spratly Island, and artificial infrastructure on Vanguard Reef, Prince Consort Bank, and Grainger Bank.

Unlike China and Vietnam, Philippines' claim is not based on Pre-War history of occupation. Philippines occupation in the disputed area started in 1947 when its businessman, Tomas Cloma, established settlement on eight islets in Spratly Islands that he called Kalayaan Islands, and later in 1974 convey the islets to the Philippines government. The government declared in 1971 and 1978 that the Kalaya'an is part of Philippines territory and reiterated it prior to the signing on to UNCLOS in 1982. According to Rowan (2005), in addition to the historical argument, Philippines claim is based on four other arguments: i.e. geographical proximity to the main Philippines islands, economic and strategic importance to

the Philippines, vacuum of power after the WW II, and recent occupation based on “discovery” or “prescriptive acquisition”.

Taiwan’s claim on the territory was based on 1947 claim of the Republic of China. It claims as the official heir of Nationalist China that claimed sovereignty in the waters in 1947. The geographical scope of Taiwan’s claim included Paracel, Spratly, Macclesfield Bank and Pratas islands. Taiwan occupies Taiping (Itu Aba), the largest islet in the Spratly and develop infrastructure for military presence and fishermen’s port. The country adopts self-restraint policy –not to claim territory that is claimed by other state(s)– for its limited capacity for power projection (Valencia et.al., 1997).

Malaysia claims 12 of Spratly Islands within their 200 nautical miles of exclusive economic zone and occupies only 6 of them. The other three are unoccupied, two are occupied by Vietnam (Amboyna Cay and Barque Canada Reef), and one by the Philippines (Commodore Reef). In the 6 occupied territory, Malaysia has developed hotel, airstrip, and facilities for scuba divers. Malaysia based its claim on the 1958 Geneva Conventions, especially regarding continental shelf and territorial waters theory. In addition, it issued its own Continental Shelf Act in 1966 and 1969, justifying claim based on continental shelf account to occupy and exploit resources in the disputed area.

Brunei claims sovereignty on Louisa Reef –also claimed by Malaysia– and Riflemen Bank –claimed by Philippines. It bases its argument on Britain’s 1954 decree of its Borneo boundaries that include continental shelf and territorial waters claims. Brunei has been emphasizing its claim on the waters and has not attempted to evict boats or vessels based on its territorial claims (Valencia et.al., 1997).

Sporadic armed clashes between the claimants, especially Chinese, Vietnamese, Filipino, and Taiwanese, are often erupted and complicate the effort for dispute settlement. The major military clashes occurred in 1974, 1988, 1992 and 1995 between China and Vietnam. China and the Philippines often engaged in small military skirmishes, including in October 20, 2011, when a Philippines’ warship struck Chinese fishing boat. Philippines’ military was also involved in an incident with Taiwanese earlier this year.

Diplomacy between the claimants as reflected by the frequency and intensity of armed incidents, has been difficult. As each claims based on weak arguments (Valencia et.al., 1997), military balance in the region is not in favor of claimants other than China (Storey, 2011); resolving the disputes through international law and bilateral arrangement has been difficult. Moreover, in cases where bilateral agreement on joint development were achieved, more often than not, the parties defected. Joint development agreement between Malaysia and China is currently operational. However, agreement between China-Vietnam (2006) and China-Philippines (2011) were defected. Each claimants is developing joint oil exploration with foreign oil companies. Recently Vietnam insists on inviting joint exploration with India (Deccan Herald, July 11, 2013), while pledge joint exploration with China after six years joint operation (Energy Tribune, July 15, 2013). Just a year before, CNOOC offered foreign oil companies joint exploration in the Gulf of Tonkin, an area within Vietnam’s 200 nautical miles EEZ. In the same year, tensions heightened following Vietnam’s allegation that China cut off the cable of PetroVietnam’s assigned vessels that were conducting seismic study.

ASEAN turned up as an alternative negotiating vehicle for Southeast Asian claimants. In 1992, the Association came up with joint declaration on the dispute, inviting all parties to the conflict to peaceful resolution, to form an international code of conduct over the SCS, and adhere to self-restraint in order to create positive climate for conflict resolution. China was reluctant to subscribe to the document then, but later willing to sign-on the DOC in 2002 in the post-crisis era, when the opportunity for demonstrating the role of responsible

great power was wide open. ASEAN role in arranging talks on COC was acceptable due to its perceived neutrality and institutional culture. The declaration, however, was non-binding with no-sanction written for non-compliance.

Track II diplomacy since 1990 has been arguably positively contributing to the multilateral process of SCS dispute settlement. The series of workshops of the Eminent Persons Group (EPG) and the Technical Working Group (TWG) were considerably productive in providing ideas of joint cooperation and development in the SCS, in order to promote peaceful settlement of disputes through preventive diplomacy (Djalal, 2012). However, as decisions are made by member states and formal security forum between states involved and interested in the issue was established in 1994, the role of track II diplomacy had been eclipsed by inter-state relations.

### **ASEAN's Role: Multilateralism or Institutional Balancing?**

Studies on the topic has unanimously shown that East Asian economic interdependence has been growing (e.g. Howe: 1990, Cossa and Khanna: 1997, Ogawa: 2002, Kai He: 2008, Petri: 2008, Masterson: 2012, and Hamilton-Hart: 2013). Since the mid 1980s, economic interdependence among East Asians has been growing. Petri (2009) argues that East Asian economic interdependence was found in history and peaked during the World War (WW) II. It declined since the end of WW II, but started to grow once again since the mid 1980s. The level of interdependence in the region, as recent studies show,<sup>5</sup> is high due to the significant increase of intra-regional trade.

The character of East Asian<sup>6</sup> economic integration has been affected by the creation of and the shifting production network, and further institutional cooperation. Massive increase of Japanese foreign direct investments (FDI) contributed significantly to the creation of production networks in the region in the 1980s. As the level of development of the so-called 'Asian Tigers' rose, the production network was shifted and the source and receiver of FDI was diversified.<sup>7</sup> Institutional arrangements aimed at mitigating financial crisis and increasing intra-regional trade through liberalization also enhanced by the mediating role of ASEAN.

It is interesting to note that institutionalization of East Asian economic cooperation is effectively conducted only by an active role of actors other than the regional major powers, such as China and Japan. Several factors contributed to this tendency. First, many among the neighbors fear China's intention and assertive behavior. Masterson (2012) found in his research on economic interdependence between China and its neighbors during 1989-2004, that China's relative power capabilities and military expenditures correlated with economic interdependence. States with equal or more power capabilities tend to grow

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<sup>5</sup> Measurement on the East Asian economic interdependence were tested statistically by studies mentioned above. Petri (2009), for instance, use gravity index to measure the level of interdependency between states in East Asia and found the trend toward interdependency since the mid 1980s to 2000s.

<sup>6</sup> East Asia in this paper refers to countries in greater East Asia, including Northeast and Southeast Asians. With East Asian integration I mean increasing economic interaction (e.g. in trade and investment) and institutional cooperation among countries in East Asia through which economic interdependence generated. Statistically speaking, trade and investment in the region has been significantly increasing in the region since the 1990s, while institutional cooperation had increased dramatically since the occurrence of 1998 financial crisis.

<sup>7</sup> Throughout the 1960s, the newly industrial countries (NICs) consisting Hong Kong, Taiwan, Singapore and South Korea were the major hosts of Japanese FDI. In the 1970s and 1980s, China and ASEAN original members except Singapore, became the new investment targets for Japan and other sources of FDI. In the 1990s, the accession of Southeast Asian formerly socialist economies into ASEAN had enlarged the production network and diversified FDI hosts.

interdependence with China, while states with lower power capabilities and military expenditures tend to have lesser economic relations with China. Vietnam and the Philippines, according to Masterson (2012) are among the states that had considerably strong power and military relative to China up to 2004, especially along the border and the SCS region. The two states had been confident in increasing economic and political relations with China.

However, as China's economy grew larger, its power capabilities and military expenditure also had grown. China's military budget in 1990 was US\$ 6 billion, rose to US\$ 106.2 billion in 2012 (SIPRI, 2013). ASEAN countries collectively only spend US\$ 25 billion on their military expenditure in 2012 (SIPRI, 2013). The recent power and military relative gap shapes threat perceptions of the SCS neighbors. With the growing gap in military and economy, combined with tough negotiation in the last two decades and recurring incidents, it is only natural that ASEAN claimants establish a firm threat perception against China. Thus, China's leadership and domination in bilateral or multilateral arrangement is less likely acceptable. Instead of adhering to Chinese pursuit of hegemonic stability, Vietnam and the Philippines tend to balance the giant by increasing defense capabilities (ASD Reports, 17 July 2013) and military cooperation with the US (Want China Times, 28 August 2012), endorsing US' presence in the multilateral dialog (Yoshimatsu, 2012), and pressing China to multilateral agreement (Reuters, 5 August 2013).

Second, there is a tendency towards a belief that economic and political relations are two different aspects that go different tracks in most of East Asian regional affairs, including in the SCS disputes. China's leadership believes that all aids and investments spent by the government has had little impact (if not none) towards dispute settlement in the SCS (Hamilton-Hart: 2013). Masterson (2012) also shows that financial interdependence in the 1990s until 2004 had no correlation with political relations. Recent development in the SCS dispute settlement also demonstrate similar picture. Despite the fact that China –as the state with largest foreign reserves in the region– contributed significantly to the creation of regional financial cooperation to mitigate crisis, tensions between the SCS claimants remain high. China's contribution to the Chiang Mai Initiative Multilateralism (CMIM) for instance, has not eased threat perception among the ASEAN claimants of the SCS.

Up to 2011, ASEAN was considered successful in managing the peace process among conflicting parties in the SCS issue. The US Secretary of State at the time, Hillary Clinton, mentioned during the 2011 ARF meeting that "This (guidelines of implementation of DoC signed on 21 July 2011) is an important first step toward achieving a Code of Conduct and reflects the progress that can be made through dialogue and multilateral diplomacy" (VOA, 2011). After a longstanding disputes since 1940s, ASEAN managed to embroil and organize multilateral talks and agreement gradually. The agreements include the 1992 Joint Statement, 2002 Declaration of Conduct, and 2011 Guidelines of Implementation of Declaration of Conduct.

The level of success that ASEAN achieved, however, was relatively modest. ASEAN did not actually successful in building confidence and peaceful relations in the SCS case, but as far as bringing the conflicting parties into negotiation table is in concern, ASEAN's role has been central. However, the lack of compliance to the agreements has undermined the value of multilateral talks, and in particular, ASEAN's centrality. The so-called "ASEAN Way" that has been considered an important base for building peace and stability in the 46 years of ASEAN's history seems to be losing relevance in the SCS dispute settlement. In the mid 2012, ASEAN was not even able to conclude a joint declaration on the issue.

The central role of ASEAN can be explained by its role in managing peace and stability in Southeast Asia for 46 years. Throughout history, ASEAN's role has been acceptable for its relative neutrality and the so-called 'ASEAN way' institutional culture.

ASEAN's neutral stance had made the Association acceptable to take part in some peacemaking in Cambodia (1991) and peacebuilding in Timor Leste (1999), for instance. ASEAN's neutrality is reflected in the establishment of Zone of Peace, Freedom, and Neutrality (ZOPFAN) in 1971, which was necessary to prevent the impact of the Cold War to the region. When ASEAN was established, it was regarded partial as an association of non-communist states in the context of Cold War. Southeast Asian socialist states accused ASEAN as part of the Cold War structure and rejected membership. The signing of ZOPFAN in 1971 included a message of neutrality from the contesting blocs, while embracing peaceful coexistence and cooperation. In time, after the demise of the Cold War, ASEAN gained confidence from the surrounding neighbors, shown by Cambodia's acceptance of its role in the country's peace making, and the accession of the four newest members; i.e. Vietnam, Myanmar, Lao, and Cambodia.

'ASEAN way' is another factor of the Association's acceptability in conflict resolution. Three main features of the institutional culture are informality, consensus based decision making, and mutual respect for domestic affairs and non-intervention principle.<sup>8</sup> Informality in ASEAN is shown by its tendency towards loose-knit institutionalization, non-binding agreements, and tolerance to diverging implementation scheme of agreements.

Decisions in the Association are made by consensus. Every decision has to be signed by all members. Without consensus and unity, ASEAN can not make an agreement. This explains the time it took to sign on free-trade agreement and recently, the DOC and COC in the South China Sea dispute. The COC agreement is not even met yet, since the DOC was signed in 2002.

Mutual respect for sovereignty and non-intervention principle has also been the norm that characterized the 'ASEAN way' which has made it more acceptable in mediating conflict resolution. ASEAN member states informally agreed that in the Association they do not interfere nor intervene domestic problems. The interpretation of this principle is even more extreme prior to the Asian financial crisis in 1998, where the member states did not even talk about domestic affairs. Recently, they started to raise their concern about domestic affairs of certain member(s), although remain reluctant to undermine the non-intervention principle.

With these institutional norms, ASEAN has been able to gradually transform Southeast Asia from originally a conflict-prone into a peaceful and stable region. The norms are necessary to ensure member and partner states' confidence in the benefit of cooperation, free from outside powers' domination, and self-efficacy. Member and partner states are at comfort and confidence in joining talks within ASEAN framework. This, among other factors, explains China's willingness to discuss the SCS disputes in ASEAN meetings.

The turn of events since 2011, however, put the idea of ASEAN centrality back into question. China's willingness to negotiate the code of conduct on SCS (bilateral) dispute settlement happened to be coincided with the 1997/8 Asian financial crisis. It is argued that China's willingness to discuss the code of conduct was because the crisis provided an opportunity for China to take the role of a responsible great power, by assuming leadership in constructing the regional financial cooperation and surveillance mechanism to mitigate crisis in an ASEAN Plus Three scheme. Part of the understanding was that both China and ASEAN will not let the SCS issue hamper the on-going and increasing economic relations (Lee Lai To, 2003). China did not try to avoid discussion over the SCS disputes in the ASEAN Regional Forum, and instead, it pledged to engage with ASEAN in formulating the COC for dispute settlement. In 1999, China agreed to put SCS issue into ASEAN-China

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<sup>8</sup> Amitav Acharya (2001) discussed in certain length the 'ASEAN way' conception among policymakers and scholars. See Acharya, *Constructing a Security Community in Southeast Asia: ASEAN and the Problem of Regional Order*, (London: Routledge, 2001) 47-79.

meeting agenda. In 2002, the two parties signed on the DOC. ASEAN centrality was seen positive then until the disputes starts worsening in 2011. Series of sporadic incidents between China and the two ASEAN claimants –namely Vietnam and the Philippines– in the last three years and ASEAN failure to convey a concerted message on the disputes since 2012 shows how ASEAN's role is losing relevance.

Despite the interesting story of chronological turn of events in the dynamics of ASEAN-China relations on the SCS issue, it is even more interesting to ask a question of whether ASEAN is losing relevance on this issue, or its irrelevance just revealed in the last few years. Was ASEAN's strategy in mediating the dispute settlement valid and reliable? Or was ASEAN used as complementary “politics of appeasement” in the strategy games between the conflicting parties?

In the current studies on the topic, there are two perspectives on ASEAN performance; liberalism-affected and realism-affected perspectives. The first perspective sees ASEAN play important role in managing the SCS dispute settlement until 2011. Studies in this perspective assume that multilateral efforts through ASEAN is crucial to manage or govern the conduct in the region and has so far been positively contributed to the construction of confidence among participants. What have been constraining the progress of ASEAN's multilateralism is the lack of confidence and incentives for cooperation, in actors' perspective. It is the actors that have been constructing stumbling block for further progress. It could be China for military build-up and provoking incidents in the last few years. It could be the Philippines for halting joint oil exploration agreement with China since the new leadership took power and arranged contract with a foreign oil company. Or it could also be the US for stationing troops in Darwin since February 2012 –declared in November 2011– and provoked further Chinese balancing act.

This perspective tends to focus on short-term policy for reducing barriers to further progress of the on-going process. The Multilateral process is believed to be effective in bringing forth the region into peace and cooperation. In this perspective, ASEAN should find a way to convince China that the dispute settlement will be conducted within China's interest. For instance, dispute settlement will be conducted in bilateral diplomacy; multilateral agreement will only set the code of conduct for bilateral negotiation between the claimants; and outside powers will not interfere the dispute settlement. On the other hand, ASEAN must also convince the US that it can trust and leave the dialog on the issue to ASEAN (Odgaard, 2003). ASEAN memberstates' support and compliance to any agreement produced must be ensured.

The problem with this perspective is that it requires China and ASEAN to comply to an agreement and build mutual trust in a short time. With relative power asymmetry and the absence of US' power in the dialogs for dispute settlement, ASEAN claimants have to put aside its inferiority and suspicion on Chinese intention, while focus on tangible results of negotiation and its consequences. The post-crisis Chinese cooperative behavior that was indicated by its participation in and support of APT and CMI had shown ASEAN countries that the giant country can act as a responsible power, in a situation where China was stronger and the opportunity given. In short, China had demonstrated that it can cooperate and it did despite relative power asymmetry.

The second perspective is convinced that ASEAN did not perform well in resolving the SCS disputes. Studies adopting this perspective are expecting to see ASEAN designs a new strategy to gradually transform the power game into cooperation and development (Snyder, 1996; Storey, 1999). In the absence of confidence among the claimants, ASEAN and China have to organize collective CBM activities that in the longer term would prevent them from recurring incidents.

In this perspective, there are a few aspects of ASEAN mediating role that has contributed to the current status of the SCS disputes. The first aspect is the paradigm of ASEAN's policy. There is a huge difference in policy paradigm between the claimants and ASEAN as an institution. As an institution, ASEAN holds liberalism in dealing with the SCS dispute. On the contrary, China and Southeast Asian claimants tend to apply realism. This gap has made ASEAN a marginal actor who deals only with rhetorics, while the claimants remain the main actors that determined the actual nature of SCS disputes. The second aspect is leadership. The fact that ASEAN is not an exclusively a third party –as it includes four of the claimants– has added complexity to the problem. To gain respect and trust from China, ASEAN needs to have a neutral and impartial image. On the other hand, in order to gain respect and trust of Southeast Asian claimants, ASEAN needs to have partiality. The dilemma for ASEAN to play a mediating role is to maintain balance between advocating its members' interests while accommodating Chinese interests at the same time. So far, this challenge has not been dealt effectively that mutual confidence between parties of the conflict is still absent.

ASEAN and the conflicting parties need to make amend if they want to save the region from deteriorating situation. The stakes for both parties are high if they can not manage the issue smartly. To China, the stakes are not only about global maritime trade highway, energy supplies, and maritime resources (Schofield and Storey, 2009), but also its campaign for 'peaceful rise' (O'Brien, 2011). To non-claimants ASEAN members, economic stakes are real as the SCS is one of the key trade routes. Conflict escalation in the region will cause contraction in Southeast Asian economies. To fix the situation, however, the first thing that the actors must do is to synchronize their diverging perspectives on the dispute settlement mechanisms. The gap between ASEAN efforts and the claimants assertive behavior needs to be bridged, if ASEAN is to maintain its relevance. Otherwise, great power rivalry will takeover and shape international relations in the region, undermining ASEAN's 46 year construction of a neutral Southeast Asia, free from great power competition.

How would this happen? If ASEAN failed to maintain its relevance to internally balance China, the member states will have to face the strategic options between bandwagon China and buckpass US' balancing strategy. ASEAN states will have to choose between joining China's camp or relying US' power to balance it. Eitherway, the international relations in the region will be shaped by the nature of rivalry between the two camps, while ASEAN states became incapable in reshaping the regional order without the great powers' influence or intervention. This is the point where the success of multilateral effort through ASEAN needs to be ensured. If autonomy and neutrality are important to ASEAN states, they need to maintain ASEAN centrality. This is also equally important to China if the latter wants to avoid direct and hard balancing against the US.

Between the aforementioned two perspectives, the second perspective –largely influenced by realism– seems to have stronger empirical basis to support a logical conclusion beyond common sense. Based on our discussion on the development of SCS dispute settlement, there are several trends that underline the lack of relevance of liberalist thesis on the correlation between interdependence and the likelihood of peace and cooperation. First, the main feature of the dispute settlement process is power politics. Each claimants tend to pursue unilateral geopolitical interests, instead of shared or collective interests. Multilateral arrangement seems to be used as a cover, politics of appeasement, instead of a mechanism for resolving collective problems.

Second, the progress of multilateral arrangement for dispute settlement is constrained by the unilateral policies of the claimants. The claimants' tendency toward unilateral strategies and institutional balancing has made the institutional process artificial and superficial. Carl Thayer, an Australian expert on SCS relation, argues that the new development in the South China Sea in July where Vietnam and China agreed to joint oil

exploration in the SCS is unlikely to be a win-win situation. The motives behind Vietnamese cooperative behavior and deference to China are image building and security assurance against potential China's use of force to solve the disputes (Energy Tribune, 15 July 2013). According to Thayer, Vietnam is trying to avoid the image of "troublemaker" in Southeast Asia, and instead, trying to build an image of peacemaker. In addition, the image building is also intended to ease public's anxiety toward potential military clash with China.

Third, deepening economic integration and growing interdependence are intentionally maintained exclusive from and thus have little impact on the on-going dispute settlement. Since the 1990s, China has been persistent on separating the SCS dispute settlement talks from economic cooperation (Lee Lai To, 2003). The motive behind Chinese insistence on exclusively separating economic cooperation from SCS dispute settlement was to avoid a situation where political and security issues could hamper pre-existing economic cooperation. China was keen to increase economic cooperation with ASEAN members and partners at the time and did not expect to see the dispute escalate (Buszinsky, 2003). However, it appears that the separation had caused economic and security issues moving in different tracks and directions. While economic integration is deepening, SCS disputes have not find significant progress so far beyond the signing of the DOC. Economic interdependence has no impact on conflict potential in the SCS whatsoever. The regional economic integration has not resulted in spill-over onto development and cooperation in the SCS.

Fourth, the constrained multilateral arrangement through ASEAN invokes further power politics between the claimants and actors from outside the region. ASEAN process found setback in the 2012 when the Association failed to conclude a joint declaration on the SCS issue. This is ironic because just a year before in 2011, ASEAN was praised for its progress in reaching agreement with China regarding the guidelines of implementation of the DOC. ASEAN's failure to move beyond the DOC after more than a decade of diplomacy affected claimants' confidence in the Association's efficacy and force them to resort to power politics and only use ASEAN process for image building to cover the actual politics. This is the case for China, Vietnam and the Philippines. China has to deal with other claimants' defections from joint development agreement several times while the balance of power in the region shifts following the increasing US military presence in the region recently, despite progress in the ASEAN led diplomacy. Vietnam and the Philippines on the other hand, while fearful of the potentials of China turning belligerent, favor unilateral policies and welcome the involvement other actors instead of China, in both joint energy cooperation or military balance of power.

Realism relevance in explaining the SCS is not found in its prescription that interdependence increases the likelihood of war. There seems to be no correlation between economic interdependence and the disputes or conflict escalations. However, realists' theories on the factors lead to conflict in international relations found its relevance in the SCS case. Three factors had contributed to the current state of SCS disputes: i.e. (1) power structure in the region; (2) divergence of each actor's geopolitical interests and strategies in the South China Sea; (3) weak regional coherence and institutional design. The power structure in the region that include the US and China has made institutional balancing an available option for ASEAN states. China's rise, on the other hand, combined with diverging neighboring states' responses had affected regional incoherence in the SCS issue. Increasing China's influence in the region enabled the rising power to divide ASEAN and stalled the multilateral process, as reflected in Phnompenh 2012. ASEAN's institutional culture that used to be the strength that ensure its acceptability to take a mediating role – through non-intervention principle, loose-knit institutionalization, and consensus based decision making– had shown weakness in resolving the conflict and reducing conflict potentials in the region. By and large, these factors indicate that realism applies, while liberal prescriptions through ASEAN needs to be evaluated.

## Closing Remarks

This paper discusses the relations between economic interdependence in East Asia and the SCS dispute settlement. It questions whether economic interdependence affects peace maintenance in accordance with liberalist perspective, or increases the likelihood of war as realist perspective suggests, and the factors that explain it.

Throughout this paper, we have discussed the trend of international relations in the SCS disputes. The SCS dispute settlement has been conducted separately from the on-going economic integration. China and ASEAN had agreed that the dynamics of SCS diplomacy would not affect the progress in economic relations. The intentional separation has made liberalist theory on economic integration only partly applies in the region, where the integration has not yet spilled over onto functional cooperation and development in the SCS. Another problem with the applicability of liberalist theories is that economic interdependence has not eased conflict potentials between China and other claimants in the SCS case. Instead of spillover, we see the states' tendency towards realism in the regional affairs. Each parties turn to unilateral policies instead of relying multilateral cooperation and consensus.

In practice, there are a few trends in the dispute settlement process that reflects liberalist theory's irrelevance, i.e. (1) that the main feature of the dispute settlement is power politics; (2) that the progress of multilateral arrangement for dispute settlement is constrained by unilateral policies; (3) that the deepening economic integration and growing interdependence are intentionally maintained exclusive from and thus have little impact on the on-going disputes; and (4) that the constrained multilateral arrangement through ASEAN invites further power politics between the claimants and actors from outside the region.

Realism relevance in explaining the SCS is not found in its prescription that interdependence increases the likelihood of war. In the SCS case, there seems to be no correlation between economic interdependence and dispute settlement. However, realists'theories on the factors leading to conflict in international relations found its relevance in the SCS. Three factors had contributed to the current state of SCS disputes: i.e. (1) power structure in the region; (2) divergence of each actor's geopolitical interests and strategies in the South China Sea; (3) weak regional coherence and institutional design.

To ASEAN, the dynamics of SCS disputes is a clear sign of its marginal efficacy in resolving such conflict. Bringing the claimants into negotiation table is a good achievement. But it is not enough, in so far agreement and compliance are absent. The tendency of the claimant states to resort to individual or unilateral actions without consulting to ASEAN to explore, mark, make new contract(s) with foreign companies from outside the region, shows strong indication toward contention, despite promotion of cooperation in ASEAN.

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