The Political Economy of the Asia Pacific

Vinod K. Aggarwal
Margaret A. T. Kenney *Editors*

Great Power Competition and Middle Power Strategies

Economic Statecraft in the Asia-Pacific Region

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Editors

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Preface

Amidst renewed tensions between the United States and China, middle powers have leveraged their geostrategic importance in the Indo-Pacific region. The US-China trade war and the pandemic, in particular, have shifted the structure of the global economy and states' objectives. Geopolitical rivalry between the United States, China, and the EU appears to be a continuing trend that will affect strategic decisions. In addition, technological changes are leading to an increased use of economic statecraft as middle powers attempt to protect key industries and supply chains from outside interference. Finally, international institutions, created to promote cooperation, are changing because of increased competition. In particular, the popularity of existing organizations is declining with the United States, China, and middle powers creating new institutions that better reflect their current preferences.

Bringing together new contributions by scholars from the United States, China, Taiwan, Japan, and South Korea, this volume seeks to contribute to these debates. In addition to our theoretical contributions in the book, the empirical chapters provide an overview of states' strategies within this unique international system via international institutions, investment, global shipping, digital trade, and renewable energy. In addition, authors provide case studies of Vietnam and South Korea's response to the power struggles in the Indo-Pacific, which can speak broadly to the role of middle powers today.

This project relied on generous support from the Japan Foundation, the Taipei Economic and Cultural Office, UC National Laboratory Fees Research Program, UC Berkeley's Institute for East Asian Studies, Chung-Ang University, and the Berkeley APEC Study Center (BASC). These sources of funding enabled us to bring together a diverse group of scholars for two days of presentations and discussions. Our conversations were greatly enriched by the contributions of our discussants: Donghui Li, Tobias Peyerl, Sarang Shah, In Tae Yoo, Yong Shin Kim, Jacob Evans, and James Lee.

In preparing the book for publication, BASC staff provided invaluable support, ranging from logistical help before and during the conference to research and editorial assistance. We also thank the undergraduate research assistants who provided practical support and research at each stage of the process, among them Janhvi

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Berkeley, CA, USA

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Contents

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Part I
Introduction

Middle Power Economic Statecraft in a World of Geoeconomic Competition

Vinod K. Aggarwal and Margaret A. T. Kenney

1 Introduction

This book addresses economic statecraft by middle powers in the context of geoeconomic competition in the Indo-Pacific, exploring both the theoretical and thematic contours of this concept and issue-specific dynamics in the areas of finance, trade, shipping, energy, and technology competition. Contributors focus on the impact of renewed great power competition between Washington and Beijing in the Indo-Pacific region, particularly regarding middle power economic statecraft strategies.

Tensions between the United States and China have risen in the last 2 years, with the acceleration of financial decoupling and threats levied to further restrict foreign investment and capital mobility. The pandemic has motivated a shift toward supply chain diversification and decoupling, which presents opportunities for middle powers to enter the competition in these emerging industries.

This chapter begins with an overview of trends in the global economy in Sect. 2, focusing on the US-China trade war as well as the COVID-19 pandemic to set the stage for recent changes in economic statecraft policies. Two critical areas that have been affected by these developments include the growing emphasis on the digital economy and climate change. The first of these has led to increasing concern among countries about how to remain competitive in semiconductors and related technologies. The race for digital supremacy has led the United States to impose sanctions on China and to create the Chip 4 alliance to restrict technology exports to China on

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a minilateral basis.[1] The second focus can be seen in the US Inflation Reduction Act, which gives strong support to the promotion of green industries. The Act is a key component of President Biden's economic strategy, providing robust backing to his commitment to combat climate change. It underscores the importance of transitioning to a green economy as a strategic means to accelerate private investment, strengthen supply chains, create domestic good-paying jobs, and sustain the US competitive edge as a global leader in "clean energy technology, manufacturing, and innovation."[2]

In Sect. 3, we review research on geoeconomics, economic statecraft, and institutional design. We consider geoeconomics as a systemic level approach to characterize growing tension between the United States and China. We next turn to a focus on "new economic statecraft," drawing on the work of Aggarwal and Reddie.[3] The focus of new economic statecraft is on trade, investment, and industrial policy. Specifically, we look at countries' policies in terms of measures that are taken behind the border, at the border, and beyond the border. Finally, we consider options for the design of international institutions and explore a variety of options to constrain and manage countries' use of economic statecraft.

In Sect. 4, we briefly describe each author's contribution. These include a focus on the United States, China, and EU as global players and efforts to create new institutions by both great powers and middle powers. In addition, the authors detail how middle powers have been engaging in important new arenas of the global economy, including digital technology, green energy, and shipping. Finally, the authors zoom in on unique middle power strategies amid this complicated global landscape; with a specific focus on Vietnam and South Korea, the authors detail these states' approaches to balancing diplomatic, economic, and security relations despite increasing competition between great powers.

Finally, we describe some common themes that emerge from the collection's diverse viewpoints in Sect. 5, focusing both on the interaction among large powers and on middle power strategies with this context.

2 Trends in the Global Economy

The global economy has experienced a remarkable shift in recent years, driven by factors such as the ongoing trade conflict between the United States and China and the COVID-19 pandemic. In addition, a growing number of countries have recognized the economic potential of working toward a digital economy. Many countries have initiated ambitious measures toward the transition to low-carbon economies as part of the global effort to combat the impact of climate change. This section aims

[1] Economist Intelligence Unit 2022

[2] The White House 2022a, b

[3] Aggarwal and Reddie 2020

to provide a comprehensive analysis of the current state of the global economy and its prospects, with a particular focus on the impact of the aforementioned events.

The ongoing US-China trade war has had far-reaching impacts on the global economy, including a slowdown in economic growth, disruptions to supply chains, and heightened geopolitical tensions. The trade war was initiated in 2018 when former US President Trump imposed tariffs on over $550 billion worth of Chinese products, citing failed negotiations to reform Beijing's economic system and address what the United States saw as unfair practices. In response, China retaliated with tariffs on around $185 billion worth of US goods.[4] The trade war has inflicted significant pain on both the United States and China in terms of national economic outputs. As of 2019, the trade war had already increased the overall US trade deficits, resulted in the loss of approximately 300,000 jobs, and decreased US real GDP by 0.3 percent.[5] On China's side, as a major exporter to the United States, the country lost around $550 billion due to US tariffs between 2018 and 2022.[6]

Focusing on the supply chain specifically, the impact of the US-China trade war has also been significant, as industries bear the burden of rising import costs, continued uncertainty, and decreased profits. As US companies are reliant on China for supplies, they must pay the price of elevated import costs, amounting to nearly $46 billion.[7] Many companies also have increased their inventory holding periods by about 8 days in anticipation of continued rising tariffs.[8] Following this increase in operating costs, companies' return on assets has experienced a 3.89 percent decline, leading to employment cuts and a shifting of supply chains to account for future changes.[9]

In the face of rising geopolitical tensions between the United States and China, an increasing number of countries have pursued policies to protect themselves and enhance their global competitiveness. For example, South Korea invested $4.4 billion in blockchain, artificial intelligence (AI), and big data in 2019. The European Union also introduced a 1 trillion-euro green deal investment plan.[10] These industrial policy interventions increasingly point to the revival of protectionism and neo-mercantilism.

Amid the trade war emerged the COVID-19 pandemic which exacerbated the already dire economic situation. During the lockdowns and turbulent domestic health crises, the United States and China were hit hard. China's swift lockdowns at the outset of the pandemic did help to limit its spread and made the country "the only major economy to report economic growth for 2020,"[11] but the subsequent

[4] Haas and Denmark 2020

[5] Haas and Denmark 2020

[6] The Economic Times 2022

[7] Haas and Denmark 2020

[8] Kmenke 2021

[9] Kmenke 2021

[10] Suberg 2018; Johnston 2023

[11] Cheng 2021

implementation of the "dynamic zero goal" and zero-COVID policies had significant economic repercussions in 2022. The increased control measures led to reduced retail sales, industrial production, and job losses, all of which negatively impacted China's economic growth.[12] Despite Beijing's efforts to support companies with tax refunds and other aid, China's GDP growth rate in 2022 plummeted to 3 percent.[13]

A similar situation occurred in the United States; millions of people lost their jobs and struggled to pay for food and rent through 2021. The pandemic also led to a 9.1 percent decrease in the US GDP in the second quarter of 2020 and quadrupled the number of labor force non-participants in just 3 months.[14] According to a White House statement, the pandemic caused commodity prices to increase by 19 percent from May 2020 to May 2021.[15] These massive shifts in global economic trends have only added to the economic hardships of the ongoing trade war.

However, some industries have benefitted from the pandemic, such as those associated with online operations and the life sciences industries. Around 11 percent of these industries reported positive effects, such as increased consumer demand and product output at 71 percent and 57 percent, respectively.[16] Remote working software companies also greatly increased their shares and user base during the pandemic. For instance, Zoom's stock share went up by 450 percent in 2020, and Microsoft Teams reached 44 million users.[17] The need for vaccines and COVID-test kits benefited the life science industries, while the transition to online work aided the rise of remote software services, making them the winners during a period of economic downturn.

The COVID-19 pandemic has accelerated the shift toward the digital economy, which encompasses all online economic activities involving people, businesses, and data.[18] This trend has been fueled by the proliferation of Internet service companies and the growing emphasis on hyperconnectivity. More countries are engaging in a race to promote the digital economy and establish global leadership in the field, with massive investments in developing advanced digital technologies such as cloud computing and 5G networks.

Notably, China's digital economic output doubled in 5 years from 2016 to 2021, reaching 22.9 trillion yuan, which accounted for 39.8 percent of GDP.[19] This growth can be attributed in part to multiple factors such as the large population, industrial policies, and technological advancement.[20]

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[12] The Associated Press 2022

[13] The World Bank 2023

[14] Center on Budget and Policy Priorities 2020

[15] Helper and Soltas 2021

[16] Harapko 2023

[17] Tenebruso 2020; Somanas 2020

[18] What is digital economy? | Deloitte Malta | Technology 2023

[19] Chu 2023

[20] Huang 2023

The development of the digital economy in China benefits the country geopolitically. The Belt and Road Initiative's digital silk road initiative, which aims to expand the country's digital economic trade, has emphasized the establishment of digital infrastructure, including 4G and 5G wireless communications, smart cities, and cross-border e-commerce with neighboring countries, to enhance China's influence in the region.[21]

The United States has also attempted to promote a digital economy on a global scale. For example, in May 2022, it launched the Indo-Pacific Economic Framework for Prosperity (IPEF) with countries in the region to strengthen economic cooperation and boost economic growth. The initiative prioritizes high standards for the digital economy, addressing trade practices and promoting ethical AI use.[22] These efforts by China and the United States signal that great powers are leading the way and setting the international standard for a transition into the digital economy.

Simultaneously, the United States has become increasingly concerned about (potential) shortages in the semiconductor supply chain, as well as increased competition in this sector with China. As a component of a broader stratagem, the US proposed the Chip 4 alliance in March 2022, aiming to bolster the "security" and "resilience" of semiconductor supply chains. This US-led coalition seeks to dilute the global dependence on chips manufactured in China.[23]

In addition, the United States has secured an agreement with the Netherlands and Japan. In January 2023, the two countries joined the United States to enact export controls on certain semiconductors and related products destined for China.[24]

The ripple effects of this geopolitical maneuvering were evident in the corporate sector. Taiwan Semiconductor Manufacturing Co., the world's preeminent chipmaker, announced an augmentation of its investment in the United States to $40 billion.[25] Concurrently, South Korea unveiled ambitious plans of its own. The SK Group committed to a substantial $15 billion investment in the semiconductor industry, encompassing research and development, material procurement, and the construction of a state-of-the-art packaging facility.[26]

The last factor affecting global economic trends is the alarming nature of climate change. Data shows that in 2020, the average temperature increased by 1.2 degrees Celsius, roughly 2 degrees Fahrenheit, compared to levels in the nineteenth century.[27] Increased temperatures are correlated with rising sea levels, more frequent wildfires, loss of biodiversity, and melting ice caps. To combat climate change, many countries including the United States, China, South Korea, and the United

[21] Xiao and Ding 2023

[22] The White House 2023

[23] Economist Intelligence Unit 2022

[24] Nikkei Asia 2023

[25] CNBC 2022

[26] Stangarone 2023

[27] Roper 2021

Kingdom are working to transition to a green, low-carbon economy by committing to carbon-neutral goals and other sustainable development practices.

As the world's largest greenhouse gas emitters, the United States and China have invested significantly in clean energies.[28] China has made substantial investments in solar and wind energy, electric vehicles, and batteries, totaling $546 billion in 2022.[29] Moreover, China dominates the low-carbon manufacturing sector, accounting for more than 90 percent of the total $79 billion invested.[30]

The United States has similarly committed to a low-carbon economy through policies such as The Federal Buy Clean Initiative, which will invest around $300 billion in the private sector to develop clean energy, electric vehicles, and related products, and the Inflation Reduction Act, which will invest $10 billion in the Qualifying Advanced Energy Project Credit Program.[31] In August 2022, President Biden also signed the Inflation Reduction Act (IRA) into law, aimed at fighting inflation and sustaining the US global leadership role in "clean energy technology, manufacturing, and innovation."[32] According to the Act, the United States will invest $369 billion in energy security and climate change.[33] While the Act is commended by EU countries, they are concerned that the tax breaks the IRA provides for electric vehicles and other clean technologies might place Europe-based companies in a disadvantaged position.[34] For example, US consumers will receive a $7500 subsidy for electric vehicles, provided they are assembled in North America. EU countries argue that this policy violates the World Trade Organization's principle of non-discrimination.[35]

Avoiding further global climate damage and achieving the net-zero 2050 goal will require countries to invest approximately $4 trillion in the clean energy sector.[36] This indicates the future of the green economy trend, in which countries will continue to seek out renewable energy sources and develop more energy-efficient technologies.

[28] Zhang 2023
[29] Schonhardt 2023
[30] Schonhardt 2023
[31] The White House 2023
[32] The White House 2022a, b
[33] US Senate 2022
[34] Reuters 2023
[35] Reuters 2023
[36] IEA 2021

3 Geoeconomics, Economic Statecraft, and Institutional Design

In light of the changes we have seen in recent years in the global political economy, this volume focuses on the intersection of economic competition, economic statecraft, and institutional design. To this end, we discuss some key concepts here that underlie this work.

Geoeconomics has been used as a term for many years.[37] Consistent with James Lee's discussion,[38] we view geoeconomics and geopolitics as systemic concepts. Geoeconomics is distinctive in our view in that it goes beyond traditional power distribution analysis as developed by Kenneth Waltz,[39] to incorporate a focus on the elements of economic power competition and the critical nature of technology in the context of broader geopolitical competition.

Turning to economic statecraft, the focus of this book, we borrow from Aggarwal and Reddie's more expansive definition of this term or what they call "new economic statecraft," which builds on existing approaches.[40] This approach focuses on how government-firm relations affect geostrategic competition—rather than the literature's traditional focus on economic statecraft that emphasizes policies related to economic sanctions.[41]

Contemporary scholarship concerning economic statecraft examines the implications of economic development in a globalized economy, where security, technology, and innovation are highly interdependent.[42] Although the traditional economic statecraft literature focuses on linking economic tools like sanctions with security objectives, new research extends this concept to security externalities arising from an interconnected economy characterized by rapid technological development.[43] The theoretical foundations of "new economic statecraft" draw on the literature on the economics of innovation but expand its scope by discussing the security of the state through the framework of national innovation systems. Given the increasing importance of technology transfer, innovation networks, and associated spillover effects on economic foreign policies, we argue that it is necessary to have a broader

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37 Luttwak 1990, 19

38 For an excellent discussion of geoeconomics, economic statecraft, and the political economy of national security, see Lee (in press).

39 Waltz 1979

40 This discussion of new economic statecraft draws heavily on Aggarwal and Reddie 2020 and 2022. See also Norris 2016.

41 Baldwin 1985; Drezner 1999. Other work along these lines is discussed in Aggarwal and Reddie 2020.

42 Farrell and Newman 2019

43 Mowery 2008

reframing of economic statecraft beyond the use of economic policy to further military objectives.[44]

In terms of policies, the focus of new economic statecraft is on trade, investment, and industrial policy. More specifically, we distinguish policies in terms of measures that are taken behind the border, at the border, and beyond the border. We begin with the most traditional focus on trade and investment policies, namely, those at the border.

Trade at the border restricts goods and services. These can take a variety of forms including import-taxing tariffs which make domestic goods more competitive than their foreign counterparts. Governments might also tax exports if they want to keep specific types of goods inside the country. Quotas operate similarly in that they limit goods arriving in, or exported from, the country, usually in terms of monetary value, but sometimes in terms of quantity. Customs regulations represent an additional border measure that adds friction to the trade process.

The most obvious intervention at the border in investment is rules on foreign direct investment. Governments might limit shareholding of a publicly held firm at a specific percentage or review foreign acquisitions of domestic firms for antitrust reasons. More recently, based on national security considerations, many countries have begun to more aggressively police foreign direct investment. In the United States, the Foreign Investment Risk Review Modernization Act (FIRRMA) of 2018 expanded the jurisdiction of the Committee on Foreign Investment in the United States (CFIUS), which previously ruled against investment in very few cases, to address mandatory filing requirements for investments involving foreign governments or representing critical infrastructure.[45]

Turning to behind the border measures, there are a variety of trade measures that can affect imports. These can include various types of industrial policy that might employ a host of trade distorting measures. Often these are described as measures used to drive "backdoor protectionism."[46] The most obvious behind-the-border trade measure is a regulatory environment that can be manipulated to discriminate against a foreign good or service. Regulatory standards, whether binding or voluntary, clearly have an impact on market access. For example, product-content requirements (also known as localization rules) are often used to limit foreign-market access. Relatedly, the government is also a customer and can influence trade patterns through procurement rules. Finally, domestic-market trade subsidies are designed to make goods from the targeted industry cheaper than their foreign counterparts. This has the dual effect of making imports less attractive and goods for export cheaper.

[44] Technology transfer refers to a situation in which the products of research and development necessary for the development and fabrication of a product travel across a border. Innovation networks refer to the various institutions necessary to create new technologies that include universities, government labs, and private industry along with investment vehicles that fund research and development.

[45] Aggarwal and Reddie 2019

[46] Cimino-Isaacs and Zilinsky 2016; Aggarwal and Evenett 2017

Governments also influence direct and indirect investment behind the border. Traditionally, this type of state behavior has been captured in the context of industrial policy. In terms of direct investment, governments often involve themselves directly in specific sectors of the economy or create state-owned vehicles that operate on their behalf. As with trade rules designed to protect foreign firms, direct and indirect investments provide domestic firms with an advantage within the domestic market and in preparation of their goods and services for export. Governments may also identify specific firms in which to invest and regulate both within the home country and abroad. This practice is particularly common in the defense sector in the United States and Europe as firms are often limited in terms of the goods and services that they can provide abroad, narrowing their ability to achieve economies of scale. Governments also pursue indirect investment in strategic industries through human capital development programs. Indirect government interventions do not target a specific firm but rather identify a strategic need and subsidize the cost of creating knowledge networks necessary for the functioning of a particular industry.

Beyond-the-border measures in trade include efforts to promote a country's exports in some fashion. These can include subsidies that favor domestic firms as well as export promotion measures that lower the prices of goods. These export subsidies are increasingly regulated by the WTO, but countries can circumvent such measures through more hidden measures such as specific tax breaks or other non-transparent bounties. More benign from a WTO perspective are export promotion agencies to help firms identify foreign market opportunities. The negotiation of a variety of trade arrangements such as bilateral accords, minilateral groupings, or working through the WTO also fall under the category of beyond-the-border trade measures.

Lastly, with respect to beyond-the-border investment measures, countries can encourage outgoing FDI by negotiating agreements with other countries. These can include trade-focused accords (with one or more country) or more direct negotiation of bilateral investment treaties (BITs), which now number well over 2000 and include 180 countries.[47] Some benefits of BITs to multinational investors include clear rules and procedures for investment, a more level playing field, protection from expropriation, investor-state dispute resolution provisions, and facilitate profit repatriation. In addition, outgoing investment can be encouraged by financial investments through government lending agencies, information provision on foreign markets, and improving political relationships with other governments.

To analyze these economic statecraft measures, Aggarwal and Reddie develop a five-factor model.[48] This approach identifies key categories of variables that are likely to influence government policies: technology, market structure, domestic structure, international regimes, and the international structure. The technological characteristics vary in terms of being primarily civilian or military in nature,

[47] https://investmentpolicy.unctad.org/international-investment-agreements/countries/223/united-states

[48] Aggarwal and Reddie 2020. See this work for the detailed logic of the five factor model.

emergent externalities for other industries or society, and appropriability. With respect to the market, they consider the number of competitors in a given industry, supply resilience or security of supply, barriers to entry, and economies of scale. Domestic structure is critical in understanding a government's ability to resist *regulatory capture* by private firms, and an understanding of what elements allow states to do this is critical, which include the quality of the bureaucracy and government-business networks, among others.

At the international level, various kinds of international arrangements can influence statecraft, a topic we take up in more detail below. The final key element Aggarwal and Reddie identify is system polarity, which influences how states perceive threats and thus how they might be more or less willing to pursue economic statecraft.

We now turn to institutional design, another theme of this volume.[49] As countries pursue economic statecraft, we can ask if such statecraft might include the creation of new institutions or might be constrained by existing institutions. The analysis of international regimes is an important academic enterprise, with Keohane and Nye defining international regimes "as sets of governing arrangements that affect relationships of international interdependence as international regimes…" and "…networks of rules, norms, and procedures that regularize behavior and control its effects."[50] Aggarwal more precisely defined international regimes as "rules and procedures that regulate the negotiation of bilateral agreements and restrict the use of unilateral national controls."[51] This definition helps us to think of the creation of international regimes in terms of their supply and demand.[52]

With respect to their supply, regimes have long been seen as being supplied by a hegemon with the capacity to coordinate international policies.[53] On the demand side, political actors generally demand regimes for three reasons. First, regimes reduce transaction costs, particularly the costs of providing information to participants and of negotiating and implementing individual accords.[54] Second, actors may wish to control the behavior of other international—or domestic—actors through rule-based systems rather than through direct coercion.[55] In a domestic context, signing an international agreement may bolster politicians' ability to reject demands from interest groups. Third, decision-makers may try to bring lower-level (i.e., more specific) arrangements into conformity with broader institutions. This "institutional nesting" discourages actors from participating in arrangements that might undermine broader accords because of their more significant concerns with these higher-level institutions.[56]

[49] See Aggarwal 1998 for a detailed discussion of institutional design.

[50] Keohane and Nye 1977

[51] Aggarwal 1981, 1983

[52] Keohane 1982

[53] Olson 1971; Kindleberger 1973; Gilpin 1975; Krasner 1976

[54] Keohane 1984

[55] Aggarwal 1983

[56] Aggarwal 1985.

Our discussion of economic statecraft focusing on industrial policy, trade measures, and new FDI regulation raises the issue of how countries might cooperate on a multilateral basis to address the external impact of such policies.[57] Drawing on insights from international regime theory, we can consider the demand and supply for an international regime (or regimes) to cope with the impact of economic statecraft. Put succinctly, will we remain in a world of unilateral measures and bilateral accords or one in which actors push for the creation of one or more international regimes?

The first scenario is fairly simple. Economic statecraft can be handled as it is currently being addressed with unilateral industrial policy, trade restrictions, and the creation of domestic regulations on foreign investment—all in the name of national security.

Second, it could also be dealt with on a strictly bilateral basis in which agreements like the US-China Phase One agreements are *sui generis*—mirroring the strategic arms control agreements between the United States and Soviet Union in the Cold War in which additional parties were viewed as unnecessary. The rapid rise of bilateral FTAs and negotiation of Bilateral Investment Treaties are indicative of this trend. This approach could take place in the context of broader regimes, but it can also be seen as reflecting growing dissatisfaction with ineffective global institutions.

A third scenario reflects the potential for the development of one or more international regimes to address economic statecraft. On the demand side, existing bilateral and minilateral commitments to address issues of economic statecraft represent transaction costs—in terms of investor-state dispute settlement, for example—that a global regime might address. With respect to control, a multilateral accord could offer mechanisms for states party to the regime to control the behavior of international actors to their benefit. Washington, for example, might address forced technology transfer, while Beijing could safeguard a market for Huawei and ZTE. A regime may also better regulate the behavior of domestic firms that currently engage in technology transfer that governments often see as detrimental to their interests in return for market access.

In terms of the demand for consistency with higher-level regimes, under the current US administration, it would be an understatement to say that this pressure has dramatically fallen in significance. Currently the United States has blocked the appointment of judges to the Appellate body of the WTO, and several trade measures that it has used are clearly a violation of WTO norms, if not rules. The TRIMs and TRIPs agreements also have not been explicitly addressed in the US-China accord.

On the supply side, the situation looks more difficult. Unlike the post-WWII liberal economic order that was led primarily by the United States but with some support from the United Kingdom, the story of regime creation with China and the United States as two superpower rivals looks more likely to devolve into two spheres of influence with their own institutions as we saw with US-Soviet rivalry. But for now, the current context remains different in that the United States and China are highly economically interdependent—a marked difference from the Cold War. A

[57] See Aggarwal and Reddie 2021 from which this subsection draws on heavily.

key theme in this book is a focus on efforts to create new institutions in a changing geopolitical context.

A fourth scenario would be to significantly modify existing institutions. Is it possible to constrain the use of new economic statecraft into these regimes meant for the broader global economic regime? The institutional design of regimes can vary in terms of a variety of parameters including membership, strength, scope, and flexibility.[58] What are the alternatives for a "fit" with existing international regimes?[59] Here, we can consider two potential regime changes that might address issues of economic statecraft.

The first potential outcome is the modification of the existing WTO to incorporate new issues relating to economic statecraft. This would be akin to the expansion of the issue scope of the GATT to include services as part of the Uruguay Round negotiations that created the WTO. Indeed, we have already seen the introduction of investment and intellectual property issues into the WTO. Of these, the TRIMs agreement has been less impressive than the TRIPs agreement, with the latter having very significant impact on issues such as the regulation of access to pharmaceutical drugs.

Second, one could envisage the creation of sector-specific agreements in investment and intellectual property that would be broken out of the WTO. Optimism on this score might come from the successful negotiation of three open sectoral agreements: the Information Technology Agreement, the Financial Services Agreement, and the Basic Telecommunications Agreement.[60] As in the case of the STA/LTA and its successor, the MFA, this would be an example of nested institutions. In this case, we would see concerns over the need to globally manage "strategic industries" and "frontier technologies," but each with its individual characteristics. As a result, it is possible that regimes addressing digital technologies, telecommunications, and biotechnology, for example, might be created that are separated from oversight by the WTO. As an example, the ITA 2 and BTA, among others, could exist—independent of the procedures of the WTO rather than being embedded in them.

We next turn to an overview of the contributors to this volume.

4 Overview of the Empirical Chapters

How have states responded to US-China competition in international institutions? Part 2 of this volume explores this question in different contexts. Aggarwal systematically compares institutions created by the United States and China, amid great power competition. Next, Kenney describes how middle power states have expanded their influence via the creation of international institutions during this period. Finally, in her chapter, Su examines the problems the EU faces in institutional unity,

[58] Haas 1975; Aggarwal 1985; Rosendorff and Milner 2001

[59] Aggarwal 1998

[60] Aggarwal and Ravenhill 2001

making it difficult for the EU to play a key role in the emerging bipolar geoeconomic competition between the United States and China.

First, Aggarwal develops a typology for institutions to classify the Chinese Belt and Road Initiative (BRI) and the US Build Back Better World (B3W). These recently constructed institutions are emblematic of broader great power competition between the United States and China.

To fill this gap, Aggarwal argues that these institutions differ markedly from orthodox institutions and instead are composed of hub-and-spoke arrangements. A pseudo institution is defined by the author as lacking clear rules and procedures (regime), resulting in limited consensus decision-making. The hub tends to determine the regime, while the spokes, or the members of the institution, experience the effects within the institutional context. His analysis finds that both the BRI and the B3W are global liberalizing initiatives, and all countries are welcome to join, but their institutional strength is weak, and their partner size has been small. For sectoral coverage and aggregate monetary value, the Chinese initiative surpasses the US-centric one.

Aggarwal emphasizes the importance of understanding these institutions, given that they are a manifestation of US-China competition. Additionally, he argues that these institutions may offer insight into the nature of China's rise and the United States' hold on the status quo. At the same time, they acknowledge that it is possible that both states will learn and change the functioning of their institutions as they face challenges.

Focusing on the opposite set of actors, Kenney investigates middle power states' creation of international institutions, independent of great power states. While great power states had been the primary orchestrators of institutions since WWII, there has been a precipitous leveling off in great power IO membership since the 2000s. Domestic discontent for international institutions has plagued the United States, the United Kingdom, and China (among others) which may explain these states backing away from the creation of new organizations. At the same time, there has been an increase in institutions created by middle power states (independent of great power membership). In response to this empirical fact, Kenney investigates how middle powers design institutions using case studies of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Digital Economic Partnership Agreement (DEPA).

Kenney argues that middle powers have intentionally designed these institutions in anticipation of the future accession of great power states. While the economic benefits that great powers bring to organizations are large, there are fears that great powers will attempt to dominate decision-making, should they join the organization in the future.

Through a case study of the CPTPP and DEPA, Kenney provides an analysis of the attributes that are found in middle power-designed institutions. First, decisions are made by consensus, rather than unilateral directives. Centralization in the organization is also limited, with no secretariat. This allows middle powers to maintain their power in future decision-making processes. Additionally, there is significant flexibility for original members in the requirements of the institution, while applicants are held to strict standards. Membership is limited by institutional nesting, but open to all states that can meet PTA standards. There is significant divergence in the scope of the institution, demonstrating that middle powers can take on both niche and broad issues within the institutions that they create.

Finally, in Chap. 4, Su examines geoeconomic competition from another perspective: the European Union. As US-China competition has heightened, the European Union has shifted its diplomatic focus from its near neighbors into the East Asian region. The EU maintains a limited security presence in East Asia and instead has focused its efforts on economic agreements and climate policy improvement. Su argues that the EU can only be successful in this region if Europe acts as a unified force. The aforementioned policy areas are ones in which the EU does have a relatively straightforward and unified stance. Additionally, Su argues that these types of policies allow the EU to pursue its normative agenda in the Indo-Pacific.

Su contributes by providing a broad definition of geopolitical significance, highlighting the EU's power in the Indo-Pacific. Furthermore, she argues that the unique political structure of the EU has distinct impacts on the actions that the organization chooses to take on in the Indo-Pacific.

In an era of geopolitical competition, Aggarwal and Kenney offer a picture of how the structure of international politics affects institutions broadly, focusing on institutional design. For her part, Su looks at another significant actor, the EU, as it attempts to maneuver within the context of US-China geopolitical competition. The structure of global markets also both conditions and is affected by the structure of the international community.

Next, Part III consisting of Chaps. 5 and 6 addresses East Asian economic statecraft by major powers in two key issue areas, focusing on the Japan-China rivalry in infrastructure financing and Chinese strategy in the global shipping industry.

In Chap. 5, Katada examines infrastructure investment competition in the Global South between Japan and China. Katada outlines how the 2008 financial crisis pushed forward the financialization of investment projects in the Global South by both governments and private industry. Investments in infrastructure projects are often associated with significant risks, which governments have attempted to offset through public-private partnerships.

Katada explains that Japan's Blue Dot Network and China's Belt and Road Initiative allow for the comparison of quality versus quantity infrastructure investment. As China pursued massive infrastructure funding plans, Japan in response developed a "quality approach" that allows the country to differentiate itself from Chinese funding. To a lesser extent, the United States also implemented this differentiated policy, offering a separate path to countries seeking infrastructure investment. As infrastructure funding to the Global South has been dramatically increasing, Katada argues that understanding the type of investment is important in assessing their effects on the global economy.

Katada argues that Japan's quality approach is motivated by improving bankability or the inclusion of private investment in foreign infrastructure projects. By removing risks to private actors, the government incentivizes an increase in bankability by choosing projects that have a clear return on investment, state-firm cooperation, and compliance with laws and regulations. Therefore, she concludes that these strategies have deep roots and are not solely a consequence of geoeconomic competition.

Next, Lin and Kaplan consider the role of the shipping industry in geoeconomic competition in Chap. 6. The authors illustrate the rise of China's network centrality in this industry through the case of the China Ocean Shipping Group (COSCO). The industry has become increasingly consolidated in the last 10 years. Alliances in the industry have promoted cooperation and, subsequently, anti-competition. In general, Lin and Kaplan argue that China has been extremely successful and connected as a maritime commercial power in the twenty-first century. However, China took action to set up COSCO for success during this period of industry consolidation via regulatory action and asset restructuring. This action was not necessarily a part of a master plan to challenge the US or Western power but did result in an increase in Chinese market power in this industry.

Lin and Kaplan contribute to our analysis of geoeconomic competition between the United States and China. This case illustrates that scholars should not impute a rational grand plan by either great power when viewing their actions in retrospect. Additionally, the authors argue that China's power in the shipping industry should be factored into comparisons between US and Chinese market power to adequately capture the power differential. More broadly, the centrality of the "node" (whether it be China or the United States) in each industry is critical to making these comparisons.

In Part 4, we turn to case studies of middle powers' economic statecraft. In these chapters, the authors illustrate how Japan, South Korea, and Vietnam have pushed beyond their imagined limitations to expand their power in the international system. First, the authors explain how middle power's holistic strategies have changed among US-China competition. Next, the authors consider middle power leadership in unique contexts, such as digital trade rules and renewable energy, to demonstrate the distinct arenas in which middle powers have taken initiative.

In Chap. 7, Lee discusses South Korea's policy of strategic ambiguity to balance the interests of the United States and China. With the US-China focus on strengthening bilateral relationships in East Asia, Lee argues that South Korea has faced increasing pressure to choose one partner. However, South Korea has continued its policy of hedging and strategic ambiguity to avoid this path. At the same time, Lee illustrates that approval of China is relatively low among the public in South Korea, while they are largely favorable of the United States.

Therefore, Lee argues that South Korea has taken some actions to reduce its vulnerability to China. First, the country is restructuring supply chains through the "China+α" strategy. Rather than exiting China completely, this policy is designed to expand beyond China to bolster supply chains that showed vulnerability during the

COVID-19 pandemic. As a result, Lee argues that South Korea has turned to Southeast Asia to diversify its supply chains and relationships in the region.

Overall, Lee offers a clear description of the complicated and strategic landscape of South Korea's response to great power competition. He also provides two main policy recommendations. First, South Korea should take advantage of the Biden administration's regional strategy without damaging its relationship with China. Next, the Korean government should strengthen its relationship with ASEAN.

In Chap. 8, Bui addresses a similar question in the case of Vietnam. Bui argues that Vietnam's close geographic relationship with China has led to a storied past. Recently, Vietnam's relationship with China has been more positive with China assisting in increasing the state's infrastructure and FDI. The long-standing territorial disputes and ongoing conflict in the South China Sea have hindered the development of a close relationship.

As US-China competition has increased in recent years, Bui argues that Vietnam has developed a unique diplomatic stance to emerge as a regional middle power. "Bamboo diplomacy" is defined by Bui as Vietnam's "strong roots, continuous growth, and strength and resilience through flexible adaptation." This unique strategy has helped the middle power state to maximize its regional and international influence while facing powerful great power pressure. Bui's unique analysis offers a clear picture of how Vietnam will continue to operate in geoeconomics in the future.

Chapters 9 and 10 demonstrate how middle powers have expanded their leadership into industries that have been rapidly growing in the twenty-first century. First, in Chap. 9, Miura and Urata examine Japan's role in the creation of digital trade rules. Rather than passively accepting rules legislated by great powers, Japan has taken on a firm leadership rule in the Comprehensive and Progressive Agreement on Trans-Pacific Partnership (CPTPP) and the Digital Economy Partnership Agreement (DEPA) to promote a consensus on digital trade.

Miura and Urata argue that digital trade clauses have been increasingly included in free trade agreements in the twenty-first century. However, there are significant issues that have not been addressed in these forums. For example, data protectionism was not sufficiently discussed in FTAs. This topic is very important as China's distinct data policy measures are more restrictive than in many other countries, with significant data retention obligations. When the conversation moved into multilateral forums, Japan took the initiative to promote its concept of DFFT. This policy gained traction among many participants and illuminated Japan's potential to lead legislation on new and niche issues.

In Chap. 10, Koo analyses South Korea's leadership in renewable energy. Koo argues that South Korea has faced numerous obstacles to pursuing a carbon neutral energy policy—most notably, the extreme speed of the strategy and the politicization of the process. In particular, corruption scandals and accidents in the nuclear industry have caused significant setbacks.

At the same time, however, he argues that the policy will ultimately be helpful in improving clean energy access and climate action. Due to the East Asia region lacking non-renewable energy resources themselves, renewable energy is vital to avoid dependencies on other states and sustaining their production. The Moon administration's FIT plan and land reclamation project were the first steps of South Korea's Green New Deal to address these issues (despite potential WTO violations). Koo expresses hope for the future of South Korea's renewable energy sector based on the lessons learned in the last few years and the increase in transparency requirements.

5 Common Themes and Conclusions

Based on the empirical work of our contributors, we see several common themes emerging, both in the US-China-EU context and with respect to middle power strategies. We address each in turn.

With respect to major power competition, we see that while the United States, China, and the EU are interdependent, competition for economic dominance is an emerging theme in their relationship. This competition is reflected in trade negotiations, tariffs, and intellectual property disputes. A second theme is growing geopolitical rivalry. The United States and China increasingly see each other as geopolitical rivals, with each seeking to exert influence and dominance in the Asia-Pacific region and beyond. The EU, while not as directly involved in this rivalry, now expresses growing concern about China and talks about the need to "de-risk" the relationship.[61]

A third theme among major powers is technological innovation. The United States, China, and the EU are all leaders in high-tech innovation, and competition in areas such as artificial intelligence, 5G, and cybersecurity is likely to continue. Each has taken aggressive steps to either onshore or friend shore key technologies. The fourth is multilateralism. The United States, China, and the EU all participate in multilateral organizations and forums such as the World Trade Organization, the United Nations, and G20. However, they have diverging views on the role of these institutions and the extent to which they should be reformed. Indeed, the United States and China are trying to establish their own institutions to compete with these traditional institutions.

Turning to middle power strategies, there are significant opportunities for middle powers to maneuver within this major power context. The contributors focus on three key strategies that have proven to be effective: self-reliance strategies, hedging and alliances, and institutional design.

Self-reliance is a classical strategy in neorealist thinking. Unable to directly compete with major powers, middle powers can attempt to bolster their own economy and military capabilities. Domestically, as in the case of Vietnam, this may involve a strong state to provide direction to policy or, as in the case of South Korea, significant investment in high technology and nuclear energy, among other industries.

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[61] https://ec.europa.eu/commission/presscorner/detail/en/speech_23_2063

Most middle powers in East Asia face the dilemma of high dependence on the Chinese market but reliance in many cases on the United States for security. This difficult nexus forces countries to engage in various types of hedging behavior, attempting to steer clear of the US-China tensions, by cooperating with both superpowers in the region. Of course, in some cases, closer ties to one power or the other are unavoidable, even at the cost of upsetting the other power. South Korea's decision to allow the installation of THAAD missiles on its territory led to retaliation by China, but it was a price that the South Korean government at the time was willing to pay. In terms of less formal cooperation, short of alliances, South Korea's pursuit of cooperation with ASEAN countries provides an example of maneuvering between the United States and China.

Lastly, institutional strategies remain critical for middle powers. South Korea, Vietnam, and Japan, for example, are members of the Regional Comprehensive Economic Partnership that includes China among others. At the same time, these three also enthusiastically have supported the US-led Indo-Pacific Economic Framework (IPEF). In addition, Japan continued to press forward with the failed Trans-Pacific Partnership and managed to help create the Comprehensive and Progressive Agreement for Trans-Pacific Partnership in 2018 with all TPP members except the United States. More recently, it has been exploring an option to work with other countries to further develop the 2020 Digital Economy Partnership Agreement on digital economy issues initially developed by Singapore, Chile, and New Zealand.

With tensions growing in East Asia, middle powers can extract significant concessions and benefits from great powers as the United States and China jockey for influence in the region. Overall, the chapters in this volume emphasize that the current international structure still allows for significant room for middle powers to maneuver.

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Part II
U.S.-China Competition and International Institutions

Pseudo Institutions: A Comparative Analysis of China's BRI and the US-Led B3W

Vinod K. Aggarwal

1 Introduction

In 2013, China launched the Silk Road Economic Belt which later became known as One Belt, One Road and in the West, as simply the Belt and Road Initiative (BRI). This ambitious global infrastructure project includes both developing countries and advanced industrialized economies. It is arguably China's broadest geoeconomic effort to engage with the rest of the world. Eight years later, the Group of Seven (G7) leaders met in Cornwall, England, in June 2021, agreeing to create a grand new initiative to support global infrastructure investment, which was dubbed "Build Back Better World" (B3W). B3W focuses on four areas—"climate change, health and health security, digital technology, and gender equity and equality."

In the broad context of great power competition between the United States and China, both initiatives have captured increasing attention from academics, pundits, and practitioners, and many posit that the B3W is the G7's response to China's BRI. However, few works have compared the BRI and B3W systematically. Most of the scholarship examines the motivation for creating the BRI. For example, some argue that the BRI is an attempt by China to sustain its economic growth by exploring overseas markets. The vast under-invested regions in the Global South have thus become potential targets for China's exports and outbound investments.[1] Some scholars maintain that the BRI reflects China's ambition to step up Beijing's

[1] Huang 2016

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geoeconomic influence in the US-led international system, challenging US dominance.[2] Other scholars point out that the BRI seeks to advance China's high-tech development by building a collaborative innovation community and promoting close exchanges and communication with participating countries on science and technology innovation. From this perspective, this initiative could potentially contribute to China's cyber capabilities.[3]

With respect to the B3W, most discussion of its rationale has come from media reports and blog posts. Journalists from globally influential newspapers contend that the G7 countries created B3W to provide a "democratic" alternative to Chinese loans.[4] Experts from American think tanks share similar views, arguing that the B3W is Biden's counter to the BRI. They also point out that the BRI lacks transparency, leading to a wide variety of problems such as adverse environmental and social impacts.[5] Some argue that B3W seeks to address the unmet global demand for infrastructure financing. They note that lending under BRI's auspices has significantly diminished in recent years, underscoring Beijing's challenges in managing the endeavor. More cynically, in the words of one analyst, Biden is "doing what is best for the country at home, and he has gotten the rest of the world on board."[6]

A few analysts compare the B3W with the BRI solely based on funding, arguing that B3W is inadequately funded. Others point to the discouraging experience of the Blue Dot Network (BDN)[7] or cursory summaries of these lending initiatives without supporting evidence.[8]

Beyond such commentaries, in the last couple of years, an increasing number of scholars have started to examine the BRI and B3W through an institutional lens. Some contend that the BRI should be seen as an institution as it is backed by social ideas and concepts rather than a simple funding initiative.[9] Others view the BRI as a multilateral institutional alternative to the Bretton-Woods institutions or as a Chinese strategy to shape the economic landscape on the Eurasian continent.[10] Some argue that the BRI is a new force for institutional change. From this perspective, the BRI is a Chinese institutional arrangement to further globalization that leads to institutional change by being a result of the narrative of globalization.[11] Still, others suggest that BRI's problems have created institutional space for G7 countries to offer competing alternatives, but the US-led B3W's "institutional

[2] Cai 2018; Jain 2020

[3] Aggarwal and Reddie 2020

[4] Parker et al. 2021

[5] Goodman and Hillman 2021

[6] Bernard 2021

[7] Feffer 2021

[8] Crystal 2021

[9] Yang et al. 2022

[10] Schulhof et al. 2022; Holzer 2020; He 2021; Li et al. 2022

[11] Casas-Klett and Li 2022

architecture is not fit to deliver on development objectives at a global scale."[12] From my perspective, while the BRI and B3W are presented as multilateral institutions, they appear to function more like hub-and-spoke systems in relation to global infrastructure development.

My goal here is to systematically compare and contrast the BRI and B3W. I argue that both initiatives should be seen as pseudo institutions. The rest of the paper is organized as follows. Section 2 provides a typology of institutions and defines orthodox and pseudo institutions by drawing on both theoretical ideas and concrete examples. Sections 3 and 4 turn to an examination of the Chinese style and US-led hub-and-spoke systems in development finance, respectively. Section 5 compares BRI and B3W by analyzing their institutional strength, nature, actor scope, geography, partner size, sectoral coverage, and the aggregate monetary scale of infrastructure projects. Section 6 provides possible future pathways for the BRI and B3W and considers the implications for US-China relations. Section 7 concludes with directions for future research.

2 Institutions: Orthodox and Pseudo

Institutions can be seen as having both a meta-regime (principles and norms) and regime (rules and procedures).[13] I define an orthodox institution as a formal multilateral or minilateral arrangement with clear rules and procedures that are widely accepted by its members. On the other hand, a pseudo institution is not as well-established or transparent in terms of its decision-making processes. Typically, pseudo institutions lack a clear and precise "regime" or consensus among members on joint decision-making.

The World Trade Organization (WTO) provides an example of an orthodox institution. Some may posit that the United States controls the institution. Yet all WTO members have joined the system as a result of negotiations, and therefore membership comes with a balance of rights and obligations. Countries enjoy the privileges that other member countries grant them and the security that the trading rules provide. In return, they must make commitments to open their markets and abide by the rules.[14] The institution is highly legalized. Concerning the obligation dimension, the WTO's tightening of safeguards and the automatic adoption of Dispute Settlement Body panel reports result in stringent obligations, apart from WTO agreements being legally binding. Moreover, WTO rules and procedures are precise in that there are many prescribed and proscribed, as evidenced by the sheer volume of the Uruguay Round Agreement that created the WTO as a successor to the GATT.[15]

[12] Liao and Beal 2022

[13] See Aggarwal 1983; Krasner 1981; Aggarwal 1998.

[14] The World Trade Organization 1947

[15] Cohee 2008

Within the domain of cross-border infrastructure development, the World Bank is a prime example of an orthodox institution. World Bank rules and procedures, as outlined in the International Bank of Reconstruction and Development (IBRD) Articles of Agreement, are multilateral as they apply to all member states. For example, all members are obliged to subscribe to shares of the World Bank's capital stock, and all members are granted voting powers determined by the number of shares held.[16] The World Bank is legalistic in that it embodies the three critical components of legalization—obligation, precision, and delegation.[17] With respect to the obligation dimension, the World Bank's Operational Manual creates obligations for both the Bank itself and its borrowers in all stages of the project cycle—strategy development, project identification, preparation, appraisal, approval, implementation, completion, and evaluation.[18] For example, its "safeguard policies" define the Bank's and borrowers' responsibilities in assessing and mitigating the social and environmental impacts of their projects.[19] World Bank obligations are also precise in that, for example, Article II section 8 of the IBRD Articles of Agreement specifies the precise amounts and schedules of payments by member states.[20] Finally, the World Bank embodies the delegation of power by member states, and it plays a significant role in interpreting and implementing the IBRD Articles of Agreement. For example, it has developed specific rules on environmental impact assessment, treatment of indigenous populations, and the participation of non-governmental organizations in project planning—all of which are enforced by the World Bank's Inspection Panel.[21]

By contrast with orthodox institutions, a hub-and-spoke system that connects every location through a central "hub" might best be seen as a pseudo institution. After WWII, the United States established such a system with East Asian countries in security. The system's bilateral nature distinguishes it from orthodox institutions. Ever since John Foster Dulles, the US Secretary of State during the Dwight Eisenhower administration, referred to these military allies as "spokes on a wheel," the term hub-and-spokes has become a popular metaphor to describe the US-dominated alliance system.[22] In a hub-and-spoke system, there is often an imbalance of power between the hub and the spokes, which can give the hub state some influence in shaping the rules within the system. As a result, the rules and procedures in such a system may not always be clearly defined, and member states may not always have a say in decision-making processes.

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[16] The World Bank 2012; Blough 1968

[17] Abbott et al. 2000

[18] Bradlow and Fourie 2013

[19] Ibid.

[20] The World Bank 2012

[21] Goldstein et al. 2000

[22] Izumikawa 2020

3 Hub-and-Spoke System: BRI

China's BRI was unveiled in 2013, as an effort to promote the connectivity of the Asian, European, and African continents and global infrastructure development. Despite the discussion of BRI as a multilateral institution,[23] since its inception, the BRI has created an interconnected hub-and-spoke system vis-à-vis global infrastructure development.

At the time of this writing, the countries of the BRI are spread across all continents, including both developing and developed countries: 52 in Africa, 38 in Asia, 27 in Europe, 11 in Oceania, and 21 in North and Latin America.[24] With these participating countries, China typically discusses, negotiates, and then signs bilateral non-legally binding agreements. While some agreements are memorandums of understanding (MOUs), others are cooperation agreements. An MOU is the highest level of agreement for participants to the BRI, which not only promises cooperation within the framework of the BRI but also substantiates the legitimacy of the initiative. By March 2022, nearly 70% of BRI member countries had signed an MOU with the Chinese government.[25]

Over the last decade, China has provided significant funding to BRI member countries. While it has had limited success in attracting private funding to BRI investments, some large private firms such as Alibaba, Greenland, and Fosun have become involved. However, state-owned enterprises (SOEs) have soft budget constraints and can finance large capital expenditures in BRI countries. During 2013–2021, more than 60% of BRI investments came from Chinese SOEs.[26]

In addition to infrastructure investment, Chinese policy banks have provided lending to BRI member states. A significant portion of the lending comes from Chinese domestic savings. The lack of a comprehensive social safety net and limited investment channels have contributed to China's very high savings rate. China's high domestic savings has caused a savings glut, accounting for approximately 2% of GDP over the last two decades.[27] In an open economy, state banks transfer some of their excess savings to lend or invest in new markets in developing regions. It is certainly true that funding from China's domestic sources is far from sufficient. The other source of BRI's capital is China-led multinational banks such as the Asian Infrastructure Investment Bank (AIIB).[28] But the AIIB cannot be seen as an investment arm of China's BRI. It is a triple-A-rated multilateral institution that finances and invests in infrastructure. As Laurel Ostfield, the head of communications for the AIIB, notes: "If a project comes to you and it's One Belt, One Road are you going

[23] Schulhof et al. 2022; Holzer 2020; He 2021; Li and Taube 2018

[24] The Chinese Central Government 2022

[25] Ibid.

[26] American Enterprise Institute 2022

[27] Zhang 2018

[28] For the list of BRI funding institutions, see Ibold n.d.

to invest in it? Well, we could, but just because it's One Belt, One Road doesn't mean we will."[29]

The BRI initiative has created a hub-and-spoke system in global infrastructure development, with China emerging as the center of the network. BRI member countries have been working with China in order to receive economic resources, which has resulted in countries becoming spoke countries.

4 Hub-and-Spoke System: B3W

BRI's growing geoeconomic influence has generated an increasingly strong response from the United States and its partners. The B3W is a US-led infrastructure initiative launched by President Biden and leaders of other G7 countries in June 2021. However, despite claims of a break with the Trump administration, this initiative is best seen as an extension of the Blue Dot Network (BDN)—a US-led infrastructure hub-and-spoke system vying against China's BRI.[30]

The BDN is a legacy of the Trump era. It is a trilateral approach created by the United States and its two close allies in the Asia-Pacific—Japan and Australia—in November 2019. The BDN claims to promote quality infrastructure investment that is inclusive, transparent, environmentally sustainable, and compliant with international standards, laws, and regulations. It aims to bring together governments, the private sector, and civil society under shared standards for global infrastructure development. A main feature of the network is to certify infrastructure projects that demonstrate and uphold global infrastructure principles.[31] Although the founding members of the BDN underscore that the initiative is not an exclusive club and does not have a political agenda, the common perception is that the BDN is an effort to slow down the BRI. The choice of the word "blue" was considered by many as a direct response to China's "red."[32]

The BDN shares the same structure as the BRI: it is a hub-and-spoke system, with the United States, Australia, and Japan comprising the hub and the rest as spokes. In this US-led hub-and-spoke system, the United States International Development Finance Corporation (DFC) is the leading bankroller. Created in December 2019, it replaced the US Overseas Private Investment Corporation (OPIC) as the official development finance institution of the United States. Among

[29] Shepard 2017

[30] In this hub-and-spoke system, the United States, Australia, and Japan are the hub with the United States being the core of the hub. India, Taiwan, Georgia, Austria, Bulgaria, Estonia, Croatia, Lithuania, Latvia, Poland, Romania, Slovakia, Slovenia, the Czech Republic, and Hungary are the spokes.

[31] U.S. DFC 2019b

[32] Kuo 2020

other major changes, DFC has the ability to spend up to $60 billion, doubling the financial firepower of OPIC. Not only can it lend, but the agency can take equity positions in investments. Moreover, it has an expanded mission to support US foreign policy objectives.[33] In this regard, the new DFC looks more like the approach of Chinese policy banks such as the China Development Bank.

In 2020, India,[34] Georgia,[35] and 12 Three Seas countries[36] expressed support for the BDN, and the US government announced to commit a $1 billion investment in clean infrastructure in the Three Seas region between the Baltic, Adriatic, and Black seas.[37] For global infrastructure development, the Biden administration has not significantly distanced itself from the BDN. In practice, the B3W is old wine in new bottles. It is "new" in that it has brought together all the G7 countries and extended invitations to other democracies across the globe to join the system, including India, Australia, South Korea, and South Africa. Yet, the United States remains at its core with the hub now transforming into a larger democratic coalition.

On the ideological front, the B3W is a more salient response from the West to the Chinese BRI than the BDN. As UK's Prime Minister Johnson remarked at the Summit's first session, "We are building back better together. And building back greener. And building back fairer. And building back more equal."[38] The 25-page Summit Communique published on June 13, 2021, also highlights that "united as open societies and guided by the shared values of democracy, freedom, equality, the rule of law and respect for human rights, [the G7 countries] commit to building back better for all."[39]

5 Comparing the Two Hub-and-Spoke Systems

We next turn to a systematic comparison of the Chinese and US hub-and-spoke systems. To do so, we draw on concepts from the institutional design literature by examining characteristics including institutional strength, nature, actor scope, geography, partner size, sector coverage, and monetary value.[40]

[33] U.S. DFC 2019a

[34] Indian Ministry of External Affairs 2020

[35] US Department of State 2021a

[36] Axelrod 2021

[37] Ibid.

[38] Johnson 2021

[39] European Council 2021

[40] Most of these concepts are discussed at length in Aggarwal 1985; Aggarwal 1998; Aggarwal and Koo 2008.

Institutional Strength

BRI's institutional strength is weak. BRI's agreements are not legally binding. When China and participating countries decide to cooperate, their commitments are voluntary. For example, the MOU between China and Italy stipulates that "the Memorandum of Understanding does not constitute an international agreement which may lead to rights and obligations under international law. No provision of this Memorandum is to be understood and performed as a legal or financial obligation or commitment of the Parties."[41] Moreover, BRI agreements do not delegate third-party legal authorities to interpret, apply, and enforce rules as per established law doctrines. In practice, the Chinese central government and the BRI client government jointly implement and monitor the progress of BRI projects. For any disputes, the signing parties will settle amicable differences through diplomatic channels, in particular through direct consultations.[42]

Although trade and investment disputes are expected to be resolved under the auspices of the World Trade Organization and through the investor-state dispute settlement mechanism under international investment agreements, BRI's dispute settlement mechanism is not "formalistic" or "legalistic." In 2018 the Chinese government established the China International Commercial Court (CICC), which is a permanent adjudication organ to resolve disputes under the BRI. While the CICC suggests China is experimenting with a more legalized approach to international dispute resolution, some key features of the CICC (e.g., the CICC is not a fully independent court of the Chinese Supreme Court) reveal that the BRI's stance on legal matters may be somewhat unclear.[43]

The G7 claims that the B3W will adopt good governance and strong standards. As the White House writes:

> High standards have become ever more important at a time when governments are grappling with complex decisions on how to tackle climate change, build back local economies, direct scarce financing, and boost employment in an inclusive way. We are committed to providing citizens of recipient communities with the long-run benefits they expect and deserve from infrastructure projects. Our efforts will be guided by high standards and principles, such as those promoted by the updated Blue Dot Network, relating to the environment and climate, labor and social safeguards, transparency, financing, construction, anti-corruption, and other areas.[44]

However, the high standards and principles that the G7 outlines refer to only the meta-regime[45] instead of specific rules and procedures. The language the United

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[41] The Italian and Chinese Governments 2019

[42] See, for example, MOU signed by the Government of The Philippines and Government of China 2018.

[43] Chinese Supreme Court 2018a; Chinese Supreme Court 2018b

[44] The White House 2021

[45] For the definition of meta-regime, see Aggarwal 1985.

States and its partners are using does not clearly signify acceptance of norms by other countries.

Some note that the US DFC has audits on its global development projects. Indeed, according to DFC's Office of Inspector General,

> The BUILD Act requires DFC to create a performance measurement system to evaluate and monitor projects and to guide plans for future projects. DFC has begun addressing this requirement with the creation of the Impact Quotient (performance measurement tool) and the Roadmap for Impact. DFC has also deployed a new system to track the receipt, review, and certification of all project deliverables within their Insight System and is currently working to improve monitoring projects and reporting borrower evaluations.[46]

Nevertheless, the audits and measurements only "ensure the U.S. government achieves economic growth, promotes U.S. national security interests, and maximizes return on investments."[47]

So far, the agreements between the G7 countries and B3W recipient countries have also suffered from weak obligations. For instance, the MOU signed between Canada's Providence Therapeutics and Colombian firm VaxThera[48] is a commercial deal and is understood as a non-legal obligation or commitment of the parties. Moreover, such MOUs and other forms of B3W agreements (e.g., DFC's loans and equity investments in developing countries)[49] do not have the characteristics of legal delegation, lacking third-party legal authority to apply rules and settle disputes or implement the sound principles the G7 proclaims.

Nature

Nature refers to the goals promoted by the institutional arrangement.[50] The nature of China's BRI is liberal. As BRI agreements show, China and BRI member states will strengthen cooperation and promote regional connectivity within an "open and inclusive framework." "Unimpeded trade and investment" are an essential feature of BRI agreements. For example, under Paragraph II of BRI MOUs, China and the participating countries reaffirm their shared commitment to free trade and investment, which advance North-South and South-South cooperation.[51] A liberal arrangement suits China, as it can export its domestic over-capacity and excess savings, ultimately benefiting the Chinese economy. Therefore, the BRI has and will continue welcoming new members by embracing free and open trade and investment cooperation.

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[46] DFC's Office of Inspector General 2021

[47] Ibid.

[48] Providence Therapeutics 2021

[49] See, for example, U.S. Embassy in Senegal 2021.

[50] Aggarwal 1985

[51] See, for example, The Italian and Chinese Governments 2019.

B3W is liberal in orientation. The United States and its G7 partners have long supported a liberal international order in the past half century which benefited them tremendously on the economic front.[52] In a contemporary context where these countries focus on the preservation of democratic values in the free world order to compete with the growing authoritarian regimes, making the B3W liberal is inevitable.

Actor Scope and Geography

The BRI is a global initiative. The agreements between China and BRI members fall into the categories of geographically concentrated bilateral sub-regionalism and geographically dispersed bilateral trans-regionalism.[53] The MOUs and cooperation agreements between China and its neighboring countries in East and Southeast Asia have strengthened the traditional historical and cultural affinity and pushed the region into China's economic and political orbit. The agreements signed with participants in other parts of the world have also increased China's gravitational pull to retain BRI members in its global sphere of influence. For example, at the Asia and Pacific High-level Conference on Belt and Road Cooperation last year, political leaders from a large number of countries discussed the progress in international cooperation under the BRI.[54] The participants reached a consensus to further step up the Belt and Road cooperation for sustainable economic recovery, accelerate the implementation of the United Nations Sustainable Development Goal for 2030, and promote resilient and inclusive post-COVID economic growth.[55]

Although important international players like Iran and Russia did not participate in this conference, their bilateral relations with China remain strong. Even before the G7 meeting, Iran struck a deal with China in March 2021, joining the BRI and exchanging lower Iranian petroleum export prices for massive Chinese investment in key infrastructure programs such as airports, high-speed railways, and power plants. As the Iranian government notes, Iran-China cooperation is "strategic and long term."[56] In a similar fashion, Russia has expanded its economic—and security—relationship with China at both government and firm levels. President Putin hopes to benefit from the BRI by serving as a land bridge between Asia and Europe.

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[52] Eichengreen 2019

[53] For the concepts of geographically concentrated bilateral sub-regionalism and geographically dispersed bilateral trans-regionalism, see Aggarwal 2001. Aggarwal and Koo 2008 and Aggarwal and Lee 2011 look at these concepts in the Asian context.

[54] Afghanistan, Bangladesh, Brunei, Cambodia, Chile, Colombia, Fiji, Indonesia, Kazakhstan, Kyrgyzstan, Laos, Malaysia, Maldives, Mongolia, Myanmar, Nepal, Pakistan, Philippines, Saudi Arabia, Singapore, Solomon Islands, Sri Lanka, Tajikistan, Thailand, Turkmenistan, United Arab Emirates, Uzbekistan, and Vietnam

[55] Kobierski 2021

[56] Sohu News 2021

Many Russians also hold a positive attitude toward the BRI,[57] which can drive Russia's economic development and serve as an effective instrument to balance against US global power.

B3W agreements fall into the same categories as the BRI, both geographically concentrated bilateral sub-regionalism[58] and geographically dispersed bilateral trans-regionalism. So far, US officials have chosen some countries in Latin America and Africa for listening tours, dedicated to potential infrastructure development and negotiations with local officials. For instance, a US delegation traveled to Senegal to understand the infrastructure needs of the West African region and discuss ways in which countries can secure infrastructure projects under the B3W initiative. Furthermore, the US government promised to work with the Government of Senegal to contribute $600 million to help secure reliable power through transformative infrastructure and reform investments in the country's electricity sector.[59] The B3W is expected to be a global initiative with particular attention to low- and middle-income countries.

Partner Size

China's BRI was unilaterally launched by the Chinese government. Although China has signed a large number of agreements with member states and international organizations, there is no official partner associated with the initiative.

The B3W was unilaterally launched by the United States. In contrast to the BRI, the US-led initiative has six partners—Canada, France, Germany, Italy, the United Kingdom, and Japan. If we look at partner size, the B3W appears to be stronger than the BRI. The world's advanced industrialized countries appear to be forming an alliance balancing against China. So far, both the United States and China have strong economic relations with G7 members. While the United States has relatively more robust trade with Canada, the United Kingdom, Italy, and France, Japan's and Germany's total aggregated exports and imports with China are no less than that of the United States.[60]

G7 countries with stronger economic interdependence with the United States tend to be closer to the United States. Canada, as the United States' nearest ally geographically, is deeply integrated with the United States on issues ranging from culture and climate change to defense and intelligence. In the Roadmap for a Renewed US-Canada Partnership, Canadian Prime Minister Trudeau affirmed Canada's shared commitment to addressing global challenges and reiterated its firm commitment to the United Nations, G7, and G20 as well as NATO, the WTO, and

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[57] Feng et al. 2019; Xinhua News 2021a

[58] In this paper, we consider that North America and Latin America are sub-regions of America.

[59] US Embassy in Senegal 2021

[60] The World Bank 2021b; The World Bank 2021a

the Five Eyes community.[61] After the G7 meeting, Italy—a G7 member that has relatively higher trade volumes with the United States than China—proclaimed that Washington is a much more important ally for Rome than Beijing by saying that "Italy is a strong commercial partner with China, we have had historical relations, but they absolutely do not compare with and do not interfere with our alliance of values with the United States…"[62] Yet, given the giant Chinese market, G7 members expressed eagerness to continue their lucrative trade opportunities with China. A former senior diplomat in the EU notes that European allies cannot afford to be confrontational against China. Indeed, EU Council President Charles Michel said clearly in October 2022 that the EU will avoid "systematic confrontation with China."[63]

Additionally, China has sometimes discussed multiple issues at once during negotiations with European countries, potentially allowing it to wield greater bargaining power and possibly creating divisions among G7 members. After the G7 countries launched the B3W, Chinese State Councilor Wang Yi met with Josep Borrell Fontelles, the High Representative of the European Union, and stressed that "I do not think the EU is so narrow-minded. China holds that various connectivity initiatives can be linked up and coordinated to form synergy,"[64] implying that countering China's BRI may jeopardize China-EU cooperation on other global issues. Fontelles seems to receive and correctly understand Wang's signal by responding that the EU believes that China should be respected, and the EU does not want to confront China. As he further said, "We are willing to strengthen coordination with China to align the EU's connectivity initiative with the BRI. We are also willing to enhance cooperation with China in addressing climate change."[65] Thus, even if the United States has partners in the B3W and its G7 partners publicly endorsed the US-led initiative, it is facile to assume that all G7 countries have an identical policy with respect to China and would therefore react similarly to China's BRI.

Sector Coverage

With respect to the issue scope of infrastructure development, China's BRI concentrates on strategic sectors, such as energy, transport, metals, real estate, and technology, helping to boost oil and gas production and build roads, railways, and power plants that enhance productivity and economic growth in areas where many poor reside (Fig. 1).[66]

[61] US Department of State 2021b
[62] South China Morning Post 2021
[63] Aljazeera News 2022
[64] Xinhua News 2021b
[65] Ibid.
[66] Rodrik 2018; American Enterprise Institute 2022

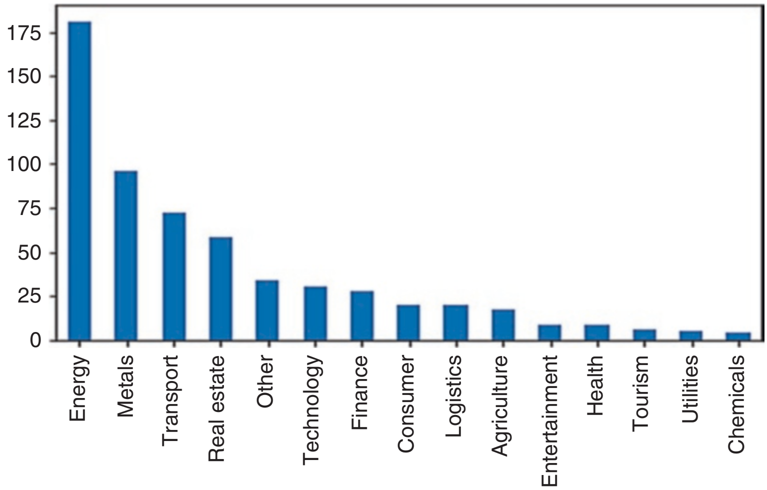

Fig. 1 BRI's sectoral coverage (2013–2022 1H). (Source: Authors' analysis based on AEI's database. Note: The vertical axis shows the frequency of BRI investments between 2013 and the first half of 2022)

The B3W is narrower than the BRI. The US-led initiative aims at projects related to climate change, health and health security, digital technology, and gender equality. During the first half of this year, the DFC approved about 20 projects that attempt to advance the B3W initiative. As shown in the table below, 55% and 40% of these projects are related to women's equality and climate change. Digital technology and health-related infrastructure projects account for 20% and 15%, respectively (Table 1).

Aggregate Monetary Value

China's state-owned banks and SOEs have provided massive funding and investments to BRI member states. Between 2013 and 2019, Chinese overseas greenfield and non-greenfield investments in BRI countries surpassed $292 billion. The aggregate sum of infrastructure projects that the BRI involved reached $723 billion. Since 2020, BRI investments have slowed owing to the negative effects of the COVID-19 pandemic on both the Chinese economy and external demand for Chinese outbound investments, especially in the energy sector. Still, BRI finance and investments in 2020 and 2021 totaled $120 billion.[67]

Compared to China's public-dominated infrastructure finance and investment, G7 countries' public capital offered to foreign infrastructure projects is

[67] Wang 2022

Table 1 B3W projects and sectoral coverage (2022 1H)

Time	Region/country	Project	Coverage
Q1 2022	Africa	Improving business management practices	Women's equality
Q1 2022	Indonesia	Climate-smart land management and emissions reduction	Climate change and women's equality
Q1 2022	Southeast Asia	Advancing the digitalization	Climate change, digital technology
Q1 2022	Africa and the Middle East	Expanding climate-resilient infrastructure	Climate change
Q1 2022	Lower-middle-income countries	Promoting natural climate solutions	Climate change
Q1 2022	India	Expanding women's access to affordable housing in India	Women's equality
Q1 2022	Brazil	Advancing gender equity in health systems	Health, women's equality
Q1 2022	Egypt	Supporting renewable energy	Climate change
Q1 2022	Mexico	Boosting entrepreneurship	Digital technology
Q1 2022	Mexico	Boosting entrepreneurship	Digital technology
Q1 2022	Nigeria	Increasing financing to enterprises empowering women	Women's equality
Q2 2022	Africa, Latin America, and Asia	Growing agricultural resilience	Climate change
Q2 2022	Sri Lanka	Increasing access to capital	Women equality
Q2 2022	Vietnam	Broadening impactful credit access	Women equality
Q2 2022	Nigeria	Narrowing the finance gap	Women equality
Q2 2022	Africa	Supporting innovative entrepreneurship	Health, digital technology
Q2 2022	Indonesia	Integrating critical supply chains	Women equality
Q2 2022	India	Supporting agritech and climate solutions	Climate change
Q2 2022	India	Supporting women's economic empowerment	Women equality
Q2 2022	Global	Scaling the outcomes market to achieve the SDGs	Health, climate change, women equality

Source: Author's analysis based on DFC's data substantially lower. During 2013–2019, official development assistance and other official flows to overseas infrastructure were approximately $273.2 billion. Even adding Australia, a long-standing member of the US-led democratic coalition, the total amount was still less than $285 billion.[68]

Despite the G7 leaders' announcement to mobilize private capital to support global infrastructure development and institutional investors who have been seeking international investment opportunities, there is an increasing consensus among scholars and policy analysts that significant barriers exist. Under a business-as-usual scenario, infrastructure projects usually require heavy upfront capital expenditures (Capex), but positive net cash flow might not materialize until many years later. In some cases, the project operations may fail, and the upfront Capex will become huge sunk costs. Thus, private sector investors are usually reluctant to put massive capital toward long-term infrastructure projects, especially in developing countries that have significant potential economic or political risks. Since 2013, private investors in G7 countries have only committed to several-dozen-billion dollars in infrastructure projects in developing countries.[69] Even worse, private investment among G7 countries in infrastructure projects has trended down over the last 5 years in African countries.[70] The US government has vowed to "support and catalyze a significant increase in private capital to address infrastructure needs [in low- and middle-income countries]." Yet, there is no concrete plan for the G7 countries on how to achieve their goal. In an interview with the Brookings Institute, Columbia University's Howard W. French put it bluntly:

> I worry that at some point not too far down the road it becomes more or less known as vaporware, basically—that the G-7 has a long history of talking up all sorts of good notions of initiatives that they are going to take and signing up pledges for funding this or that that don't ever really materialize or don't quite materialize.[71]

In a nutshell, both the BRI and the B3W can best be seen as pseudo institutions. Although their nature and geography are the same as those of the World Bank's global infrastructure development, the actor scope, partner size, and institutional strength are much less relative to the World Bank. To graphically illustrate the differences, Fig. 2 provides a longitudinal chart of the BRI based on the dimensions that we have discussed, and Fig. 3 provides a spider graph comparing the BRI and B3W with the World Bank as our benchmark.

[68] OECD Database n.d.

[69] World Bank Database n.d.

[70] Rautmann 2021

[71] French and Dollar 2021

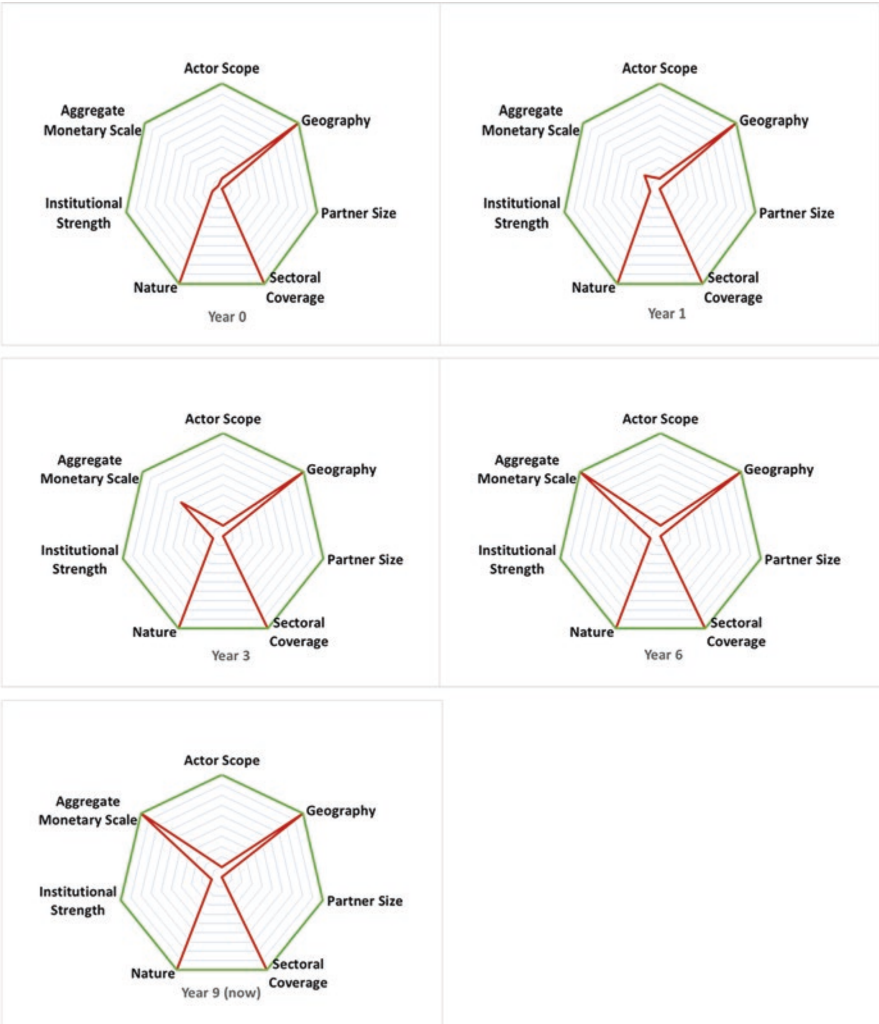

Fig. 2 Changes in institutional characteristics of the BRI (2013–present). (Source: Author's own analysis. Note: (1) Actor scope of BRI over time has been bilateral. (2) Aggregate scale of BRI finance and investment has increased substantially over the last 9 years. (3) The BRI, since its inception in 2013, has covered 13 sectors, while the B3W focuses on 4 areas. (4) The BRI has no partner)

6 Prospects for the BRI and B3W and Implications

From a more dynamic perspective, institutions can undergo changes over time. In recent years, China has made efforts to enhance the design and implementation of its BRI projects. With more businesses with BRI countries, China continues to secure feedback—both positive and negative—from local communities, through

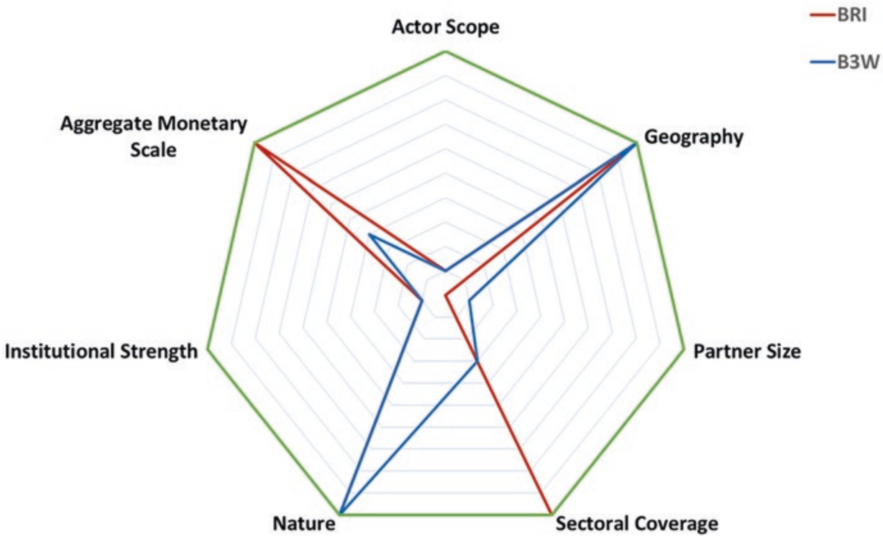

Fig. 3 Institutional characteristics of the BRI and B3W. (Source: Author's own analysis. Note: (1) Actor scope of both BRI and B3W is bilateral. The medium-level actor scope is minilateral, and the highest level is multilateral. (2) Aggregate scale of BRI finance and investment based on the data of 2013–2019 was on par with the World Bank. However, the aggregated finance and investment from the G7 countries during the same period were only about 40% of the BRI's. (3) The BRI covers 13 sectors, while the B3W focuses on 4 areas. (4) The BRI has no partner. The B3W's partner size is also small)

which China adds new information to prior knowledge and beliefs to revise their behavior accordingly. Although the learning process is dominated by an "availability heuristic" that is impossible for the Chinese government and companies to retrieve all the information and therefore limit their decision-making to only those available to them, China has been actively adapting and assimilating norms and best practices of orthodox institutions. In Latin America and the Caribbean region, for instance, Chinese actors have significantly improved their understanding and business conduct to deal with local rules, bureaucratic procedures, and public concerns around land rights, social development, and environmental degradation.[72]

International critiques of the BRI are expected to prompt China to make institutional changes in response. This might create great incentives for the country to further improve its conduct and avoid the risk of losing international support. Between 2014 and 2020, China either shelved, mothballed, or canceled more than $65 billion of Chinese-backed coal-fired power plants.[73] In the first half of 2021, China did not finance any coal projects through its BRI for the first time since its

[72] Abdenur et al. 2021.

[73] Wang 2021.

inception.[74] In July 2021, at the Chinese Communist Party and World Political Parties Summit and the APEC Informal Economic Leaders' Retreat, President Xi Jinping stressed China's willingness to work with the international community to promote high-quality projects of the BRI. He said, "We will…advance high-quality Belt and Road Cooperation. We hope to work with countries in the Asia-Pacific and beyond to achieve higher-standard mutual benefits and win-win cooperation."[75]

After Xi entered his third term as China's paramount leader in October 2022, he reiterated China's commitment to "promote high-quality Belt and Road cooperation."[76] While it is too early to tell if the BRI can become an orthodox institution in the near future, China will likely continue to learn and adapt its practices.

Similarly, the B3W may change over time in terms of its institutional characteristics, especially its aggregate monetary scale. In June 2022, the United States and other G7 countries officially launched the Partnership for Global Infrastructure and Investment. The United States has vowed to mobilize "$200 billion in public and private capital over the next five years." In total, the G7 countries combined are expected to mobilize approximately $600 billion by 2027.[77] If the United States and other G7 countries can achieve their commitment, the cumulative scale of B3W finance and investment will be on par with the BRI and the World Bank by the end of this decade.

The development of the BRI and B3W has profound implications for the US-China relationship and international geoeconomic landscape. On the one hand, the United States has called for more "like-minded" countries to join the B3W as potential partners, and the B3W's slogans such as "values-driven," "high-standard," and "transparent" seem appealing to pro-democracy countries. On the other hand, amid the trade and high-tech conflicts with the United States, China is improving its conduct and proactively pursuing economic policies to respond to the US strategic moves[78] and retain international support. During the China International Import Expo in November 2022, one of the Chinese Politburo Standing Committee members Li Qiang stressed that China would further open its market to promote the BRI.[79] Many countries, regardless of their political systems, have become increasingly dependent on the Chinese market and funding, leading to their deep involvement in the BRI. This trend may aggravate the strategic rivalry between the United States and China, alter the policies of countries that hope not to deviate away from either great power, or possibly form two competing coalitions under each of the superpowers.

74 Bloomberg News 2021.

75 People's Daily 2021.

76 Ministry of Foreign Affairs of China 2022.

77 The White House 2022.

78 Despite the fact that during the US-China trade and high-tech conflicts, China's proactive pursuit of economic policies might not be an optimal strategy for China. See, for instance, Zhang and Chang 2021.

79 Xinhua News 2022

7 Conclusion

This chapter has analyzed the BRI and B3W using a typology of institutions. I define an orthodox institution as a body of multilateral or minilateral arrangements with binding rules and procedures, whereas a pseudo institution is either not multilateral or minilateral, not formalized, or both. Based on this definition, I argue that the BRI has established a hub-and-spoke system in the domain of global infrastructure development, with China at the center through its provision of massive funding and bilateral agreements with BRI member states. BRI's expanding influence has invited an increasingly aggressive response from the United States and its partners. Similarly, in my view, the B3W is an extension of the BDN, a US-led infrastructure hub-and-spoke system that competes with the BRI. The hub in the B3W's structure is now transforming into a larger democratic coalition, and the United States remains the center.

I also suggest that comparing the two infrastructure initiatives should be broadened from a traditional lens that focuses on political motivations and financing to a different perspective that looks at seven variables—actor scope, geography, partner size, sectoral coverage, nature, institutional strength, and aggregate monetary value of the infrastructure projects. This analysis shows that both the BRI and the B3W are global liberalizing initiatives, and all countries are welcome to participate. Thus far, the partner size of both initiatives has been small—B3W's is six, while China has not had any partner engaged in the BRI. For scope and aggregate monetary scale, we also find that the BRI surpasses the B3W. Finally, the institutional strength of the BRI and the B3W is low as their agreements are not legally binding and have not stipulated specific, clear rules or delegated third-party legal authorities for project implementation, monitoring, and dispute settlement.

This research systematically analyzes and compares the BRI and the B3W. There are three areas that merit greater academic and policy attention. First, scholars might consider how China's BRI and the US-led B3W play a role in long-term global infrastructure development compared to orthodox institutions like the World Bank.

Second, from a dynamic perspective, institutions can evolve over time, and it is important to monitor any changes that occur within the BRI and the B3W. China has been engaging more with BRI countries, which has provided valuable feedback, both positive and negative, from local communities. This feedback helps to inform China's decision-making and allows for the assimilation of new information and best practices. While there may be limitations to this learning process, it is very likely that China will continue to adopt norms and best practices from orthodox institutions in the future. Similarly, the B3W may change in terms of its institutional characteristics, increasing the monetary scale of financing and becoming more formalistic and legalistic.

Third and relatedly, an important question to consider is how the development of the BRI and the B3W will affect the US-China relationship and the international geopolitical and economic landscape. The United States has invited like-minded countries to join the B3W and has emphasized the importance of high standards and transparency. However, China remains committed to the BRI and continues to improve its conduct to retain international support. Many countries are dependent on China's market and funding, making it challenging for them to disengage from the BRI. It is possible that this could lead to increased competition between the United States and China, which warrants further investigation.

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Middle Powers and Institutional Design: A Case Study of the CPTPP and DEPA

Margaret A. T. Kenney

1 Introduction

Great power states have historically been involved in a large number of international organizations. After World War II, the United States was particularly instrumental in the creation of the Bretton Woods institutions and promoting international cooperation. There was significant concern about the creation of organizations to simply bolster powerful states' goals given their monopoly over international design in this period. Therefore, in the international cooperation literature, there has been a strong strand of research which argues that institutions are epiphenomenal and merely reflect great power interests. Mearsheimer (1994) contends that institutions are only important on the margins and have little independent effect on state behavior. Moreover, he argues that power is the main determinant of international behavior and institutions are unable to change this predisposition in the international community. In addition, international institutions have been described as explicitly detrimental to less powerful states, as great powers design the organizations to uphold their own power and interests.[1] However, as can be seen in Fig. 1, after the dramatic surge following WWII, the involvement of great powers in international organizations has leveled off as a percentage and even declined, since the beginning of the 2000s.

[1] Steinberg 2002

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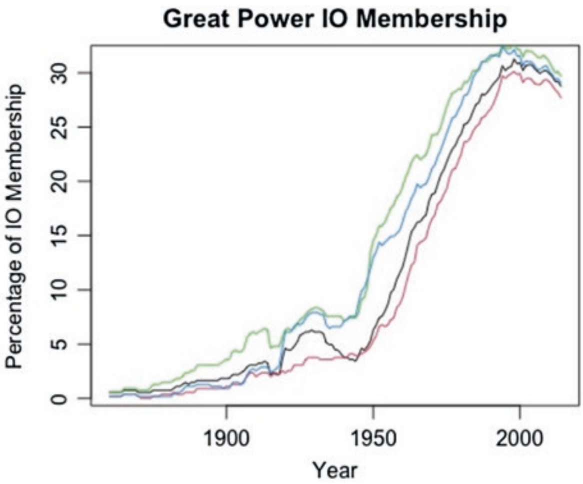

Fig. 1 Using the International Organizations v.3 dataset from the Correlates of War project (Pevehouse et al. 2020), this graphic illustrates the percentage of existing organizations that great power states are involved in. The United States is represented in black, the United Kingdom in red, China in green, and Russia in blue

One potential mechanism for this decline has been the increase in populism and protectionism among the domestic publics of developed economies. The effects of globalization have left citizens feeling "left behind" as "the forces of globalization have left them rudderless, closing industries, leading people to abandon their homes, and harming them economically."[2] As a result, criticism of international organizations has been at all time high, with skepticism about their effectiveness and the benefits that citizens accrue from their country's membership. In the United

States, there has been a steady increase since 2002 in the opinion that the United States should "mind its own business internationally" (see Fig. 2).[3] These concerns manifested in the election of President Donald Trump in 2016, which only exacerbated tensions between the United States and existing international organizations. Trump's administration is marked by its dramatic exit from the Paris Climate Agreement, Trans-Pacific Partnership, and World Health Organization alongside explicit criticisms of the North Atlantic Trade Organization and the United Nations.

At the same time, the United Kingdom's referendum to exit the European Union reflects similar feelings among its citizens. Their refrains echoed that of feeling left behind; "the connection between space, place, and class inequality is central in understanding the anger, the hurt, and the seemingly casual way that working- class people all over the UK appeared to vote against their interests."[4] Although the European Development Fund had provided significant aid to struggling ex-mining

[2] Pew Research Center 2020

[3] Ibid.

[4] McKenzie 2017

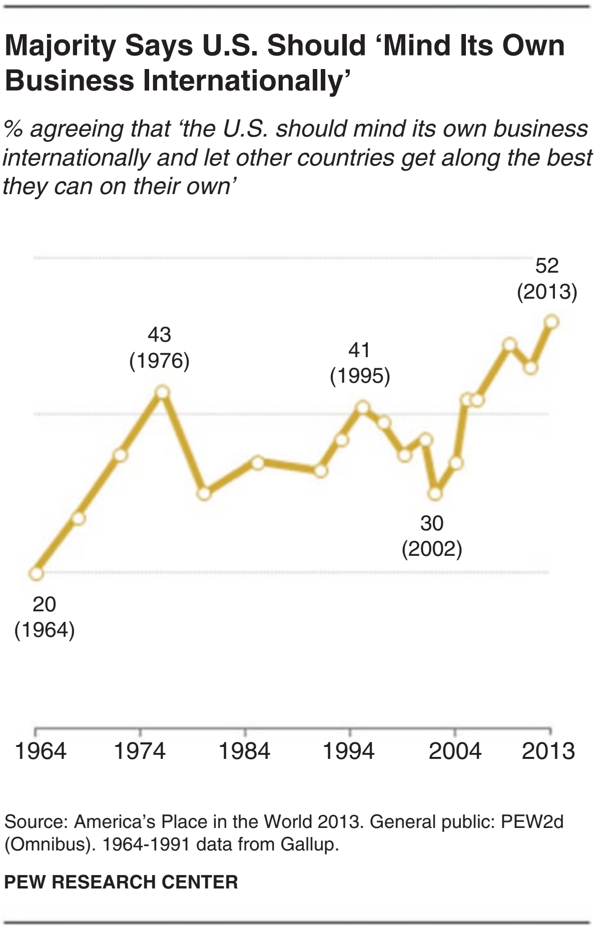

Fig. 2 Majority says U.S. should 'mind its own business internationally' (Source: Pew Research Center)

towns in the United Kingdom, among others, these were the very people who were vehemently against the organization in the run up to the referendum.[5]

China has also expressed discontent with existing international organizations for the lack of design adjustments that reflect its growing economic and international power.[6] Therefore, they have placed a focus on independent state initiatives, rather than operating solely through the World Trade Organization, International Monetary Fund, and United Nations. Additionally, China has created its own international institutions that better reflect their goals and preferences, such as the Asian Infrastructure Investment Bank.

[5] McKenzie 2017

[6] Rapp-Hooper 2019

One of the actors filling this leadership vacuum is middle power states, who have increasingly leveraged their burgeoning economies to bolster their international status. In recent years, middle powers have created institutions without the immediate accession of great power states. These institutions are not necessarily subversive to the international system but offer middle power states the opportunity to prioritize their goals and design preferences. Few institutions are more emblematic of this trend than the Comprehensive and Progressive Agreement for Trans-Pacific Partnership. While this trade agreement began as the TPP with the involvement of the United States, former US President Trump withdrew from the agreement at the start of his tenure in 2017. In response, the remaining participants—consisting of Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Peru, New Zealand, Singapore, and Vietnam—organized to form the CPTPP. However, these organizations do not explicitly limit participation to regional actors or middle powers. In the case of the CPTPP, both China and the United Kingdom have expressed strong interest in joining the trade agreement. Their potential accession has provoked substantial debate both internally in the organization and among the international community at large. Additionally, the Digital Economic Partnership Agreement was signed by New Zealand, Chile, and Singapore on June 12, 2020. This agreement, similarly created by middle powers, aims to "establish new rules and practices for digital trade, and promote ongoing discussion on issues like digital inclusion, inclusive trade, and support for small and medium enterprises (SMEs) in the digital economy," with both South Korea and China signaling their intention to apply.[7]

The way in which middle power states may design their institutions differently has not been widely discussed in the literature. Instead, the focus has been on great power and non-state actors' influence on design. As middle power designed institutions continue to grow in number and in their power in the international community, it will be important to understand how they are unique and what this tells us about the effectiveness of institutions. Additionally, because great powers are attempting to join middle power-designed international organizations, like the CPTPP, it is necessary to discern whether these institutions will evolve to be based largely on power relations or if middle powers have designed adequate safeguards to avoid being overpowered by large states.

Therefore, I will address the following questions in this paper. First, how do middle powers design institutions? By utilizing frameworks created by Koremenos et al. (2001) and Aggarwal (1998), I will analyze how the membership, scope, centralization, control, and flexibility differ in organizations created by middle powers. Second, how do these institutions respond to the application of great power states, and do they create plans to preserve their independence? These questions will be answered with a case study comparison of the CPTPP and DEPA to better understand the institutional design preferences of middle powers.

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[7] Lester 2021

2 The Influence of Middle Powers

Middle powers are defined as countries "which make no claim to the title of great power, but have been shown to be capable of exerting a degree of strength and influence not found in the small powers."[8] As a result, middle powers have distinct interests and behavior in the international system, due to their unique status. Their goals are broadly focused on "multilateralism, niche diplomacy, and soft power."[9] However, the growth of international organizations led by middle powers challenges these theoretical expectations and raises important questions about the evolution of middle power behavior.

In international organizations, middle powers often choose to focus their efforts on very specific issues that they believe they will be able to change effectively. Termed "niche diplomacy" by Cooper (1997), middle powers make use of their technical expertise and fundamental experiences to have an impact on a select set of issues. For example, Maitre (2017) concludes that Japan has championed nuclear deterrence as an issue because of the attacks on Hiroshima and Nagasaki, which allow it to claim this topic as intrinsically important to their state interests. Middle powers may also be able to command issues or initiatives that would be controversial if pursued by great powers.[10] This is because they appear to be less threatening than great powers in the international community[11] and thus have more latitude or discretion before they receive targeted scrutiny.

Second, middle powers place significant value on their definition as a middle power in the international system. This elevation above the status of a weaker power provides them with a platform to project regional influence and, potentially, international influence. Patience (2014) notes that "status anxieties loom large over middle powers" (p. 211). Therefore, middle powers will continually strive to maintain this status and to expand their power so that they maintain regard in the international system. Because this title is socially constructed, states have chosen to embrace it differently based on the leader in power.[12] However, whether or not states embrace this title does not have a substantive impact on their behavior.[13] In the aggregate, middle powers will attempt to cement their status in the international community by acting as "'status quo' powers when it comes to preserving the rules and institutions of the international system, but 'revisionist' powers when it comes to undue great power influence."[14]

8 Glazebrook 1947

9 Teo 2022

10 Ravenhill and Ravenhill 2001

11 Emmers 2018

12 Cooper and Dal 2016

13 O'Neil and Gilley 2014

14 Ibid.

Third, previous literature emphasizes middle powers' desire to work through multilateral organizations to achieve their international goals.[15] Middle powers have regional authority and power, but this often does not always extend to the international community. Therefore, in order to achieve broader goals, they utilize international organizations and work in collaboration with great powers. Most often, this is manifested in the promotion of international norms to bolster their interests.[16] More specifically, "their objective is to shape a rules-based order and establish good governance in international affairs through multilateralism."[17] If successful, this behavior results in an international system that is more predictable for middle powers. In other words, the international system becomes easier to navigate, as middle powers can worry less about the coercive or aggressive actions of great power states once these norms have been set in place. Additionally, Turnbull (2022) views these actions through realm of possibility for middle powers. Coercion is a task that can only be accomplished by great powers who have more leverage, while middle powers merely "avoid suffering at the hands of the strong" through rule-setting in multilateral organizations.[18] Without coercive capabilities, other scholars see middle powers' main role in international organizations as "mediating disputes and building bridges" among great powers to maintain international stability.[19] Again, this creates a more amenable landscape for middle powers as they can fend off aggressive actions and worldwide conflict in this manner.

Why are middle powers choosing this moment to create international organizations? Systemic shocks may have a substantial impact on middle powers. Middle powers have been able to expand their influence in the modern era after the global financial crisis and the elevation of the G20.[20] Cooper and Dal (2016) highlight that with middle powers such as South Korea, Canada, Mexico, Turkey, and Australia serving as hosts for the G20 meetings, they have been able to highlight issues that are most important to them. By creating a focal point around middle powers due to the geographic location of G20 conferences, middle powers have received heightened international recognition and influence. Additionally, the growth of China's economic and political influence has increased attention on middle powers, particularly those in Asia. Because of their geographic proximity and contrasting interests, middle powers in Asia have been placed in a situation that demands their action in balancing against China's rise.[21] Therefore, the threat of great power states increasing their influence in the international system may empower middle powers toward action.

It is clear that not all of these theoretical expectations are fully applicable today, as middle powers are increasing their influence through the creation of new international organizations rather than simply acting through existing IOs. Additionally,

[15] Cooper and Dal 2016

[16] Emmers 2018

[17] Emmers 2018

[18] Turnbull 2022

[19] O'Neil and Gilley 2014

[20] Cooper and Dal 2016

[21] O'Neil and Gilley 2014

the scope of middle powers' influence has broadened beyond rule-setting to trade agreements that will bolster the economic power of middle powers in the international system. Middle powers' economies have grown to a point where they may be much more effective at impacting international outcomes based on the inclusion or exclusion of members from their organizations. Thus, coercion may not be as far out of reach as Turnbull (2022) expects. It is important to extend this analysis to understand how they have learned from their experiences in large multilateral organizations and which characteristics they bring to organizations that they design themselves.

3 Institutional Design

Previous work on international organizations and their design has focused on how power is manifested. Mearsheimer (1994) argues that institutions are largely epiphenomenal, having only a minimal effect on state behavior at the margins. This realist critique is often presented to dissuade from the study of organizations because they are merely another form of state power projection. Next, Abbott and Snidal (1998) and Steinberg (2002) also argue that powerful states design institutions to magnify their interests. Abbott and Snidal (1998) posit that "powerful states structure such organizations to further their own interests but must do so in a way that induces weaker states to participate" (p. 8). Steinberg (2002) offers an example of this type of behavior through the WTO's consensus-based decision-making rules. Despite its purported aim to treat every state's voice equally in the decision-making process, the design of the organization is largely useless because powerful states magnify their influence behind the scenes. Law-based bargaining occurs during the early stages to determine the reservation points of developing states. Then, the EC and the United States create agreements that push developing states as far as possible to their reservation points, while the powerful get their preferred deal. This strand of literature poses a serious obstacle to the study of institutions and their design, because it implies that power is the primary determinant and thus institutions are not worthy of study. However, although institutions designed by middle powers may reflect some power considerations, the above explanations cannot apply as directly because great powers are not involved in their initial design stages. Therefore, the structure and outcomes of these organizations may differ markedly from what is hypothesized in the case of international organizations that are dominated by great powers.

This literature has begun to expand beyond a focus solely on institutions created by powerful states. First, institutions are no longer designed entirely by powerful states. Johnson (2013) illustrates that 2/3 of intergovernmental organizations (IGO) were not made by states alone, but alongside international bureaucrats. As bureaucrats become more proactive in designing IGOs, they work against the interests of powerful states to insulate the IGO from state control mechanisms.[22] Explicitly, these design choices reduce the strength of all states from intervening in the organization's activities. This runs directly counter to Abbott and Snidal (1998)'s assertion that powerful states would never join organizations that they cannot influence. This study illustrates the impact of actors other than great power states and how they can reclaim the systems of power in the international system. Therefore, Johnson (2013) suggests that international organizations are beginning to explicitly restrict the influence of great power states, with the international bureaucrats taking away some of their discretion.

Additionally, scholars have begun to analyze how states in the Global South choose to engage in international cooperation. Beall (2023) explains that regional organizations have played an important role in "weak, dependent, and subordinate states" being able to avoid the imposition of external authority. Instead of relying on global international institutions, these states have instead transferred sovereignty to regional organizations over which they have more control. Additionally, others explain that regional international organizations (RIOs) are increasingly dominated by authoritarian states that aim to delay democratization efforts in the region.[23] Therefore, RIOs may have differential impacts on peacekeeping, election monitoring, and development aid as compared to other international organizations. This research demonstrates that states utilize existing institutions to further their interests and goals. However, this research is still mainly focused on the effects of great powers in these organizations, specifically China and Russia, and how their influence might counter that of the United States. Additionally, regional organizations in the Global South may not necessarily have the same goals or face the same challenges as those created by middle powers. This is because there is significant path dependency in the states who are involved in these regional organizations, and it is unlikely after years of regional independence that great power states would attempt to apply to accession or intervene significantly in their activities. As a result, their design may differ quite prominently from those of middle powers.

In this paper, I utilize Koremenos et al. (2001) and Aggarwal (1998) frameworks to understand the design of institutions created by middle powers. This framework posits that "states use international institutions to further their own goals, and they design institutions accordingly" (p. 762). Institutional design is important to states, and they will spend considerable amounts of time and effort to create the system that they want because "design... affects outcomes."[24]

Therefore, the institutions that middle powers create will be explicitly designed to maximize their preferences in the international system. I hypothesize that, first and foremost, middle powers utilize these organizations to project power globally and escape their role as a purely regional organization. In terms of membership, middle powers will allow applications from great power states because of the

[22] Johnson 2013

[23] Cottiero and Haggard 2021

[24] Koremenos et al. 2001

economic and power gains that their membership can bring. However, they will utilize institutionalized safeguards, like PTA standards and nesting, to avoid complete takeover by great powers. Control will be diffused among member states, with decision by consensus. This structure reflects how middle powers want to be viewed in the international system: with equality in collective decisions. At the same time, states will use public statements and direct appeals to make clear their position on certain issues and distinguish themselves from other members. Between organizations, the breadth and depth of scope differ substantially. What is made clear, however, is that middle powers are no longer bound to niche diplomacy and have the opportunity to pursue broad agendas if they choose. Next, flexibility is provided for the original members of the organization, while strict standards are set for applicants to membership. Finally, as a reflection of concerns about politicization in the organization, international institutions designed by middle powers have limited centralization with no overarching secretariat or independent body. In sum, middle powers will utilize international organizations to expand their global influence, which requires cooperation with great powers. However, they will create systems in which great powers are relatively disadvantaged, learning from their experience in other international organizations.

Both the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Digital Economy Partnership Agreement (DEPA) are international institutions formed by middle powers. There are important similarities in their membership, control, flexibility, and centralization. These institutional safeguards allow middle powers to protect against great power influence as they open up membership beyond the original members. However, they differ substantially in the scope of their work. This distinction demonstrates that middle powers are capable of leading via "niche diplomacy" (discussed above) and broader substantive territory (Fig. 3).

	Membership	**Control**	**Scope**	**Flexibility**	**Centralization**
CPTPP	Limited by nesting, but open to all states that can meet PTA standards.	Decision by consensus; use public statements and direct appeals for unilateral control.	Expansive in breadth and depth.	Flexibility for original members; strict standards for applicants.	Limited: no secretariat or independent body.
DEPA	Limited by nesting, but open to all states that can meet PTA standards.	Decision by consensus.	Limited in breadth, expansive in depth.	Flexibility for original members; strict standards for applicants.	Limited: no secretariat, independent body, or dispute settlement body.

Fig. 3 Source: Author

4 Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)

Membership

The CPTPP currently consists of ten member states—Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Peru, New Zealand, Singapore, and Vietnam. The geographical distance between member states indicates that this is not purely a regional organization. Due to the economic benefits, the CPTPP is open to membership from great power states, rather than restricting its membership. For example, the CPTPP suspended the clauses that the United States had required for accession into the TPP. This action leaves the door open for the United States to rejoin, as CPTPP members would merely have to re-enact the measures, rather than completely amend the agreement. More specifically, the CPTPP suspended provisions on illegal wildlife trade, intellectual property rights, government procurement, investments, and bilateral labor plans.[25] In sum, because of the economic benefits of great powers' involvement in the agreement, middle powers do not explicitly bar them from inclusion and, what is more, they provide clear avenues to accession. At the same time, the control that middle powers are exerting gives them substantial leverage to dictate the future of the international order. With the almost simultaneous applications of Taiwan, China, and the United Kingdom, the choices that CPTPP members make will have ripple effects, and the inclusion of one may preclude the inclusion of others.

Second, the CPTPP is nested in the APEC framework, which allows the states to provide clear standards for membership and commit to their values. For example, Chinese Taipei was a member of APEC, which makes it "procedurally possible for Taiwan to apply for CPTPP membership."[26] By constraining itself through nesting in other previously created institutions, CPTPP members have leverage to advocate for their positions by appealing to precedent in their nested institutions. Aggarwal (1998) establishes the term "nested institutions" and explains that in the context of the Long-Term Arrangement on Cotton Textiles, nested within the GATT/WTO, actors were able to reconcile competing interests and utilize the existing framework of principles and norms. In a similar way, CPTPP's creation as a nested institution is a strategic maneuver to constrain membership. As a result, middle powers will be able to maintain their influence over the organization and avoid the incursion of members that could threaten their objectives. Additionally, the organization can credibly commit to maintaining APEC's core principles and norms, most notably the Bogor Goals which focus on the importance of free trade and investment among member states.[27]

[25] Congressional Research Service 2022

[26] Kawashima 2021

[27] APEC 2021

Third, allowing additional states, including great powers, to join the multilateral agreement lets middle powers avoid overt coercion and economic pressure to undertake bilateral trade agreements. This attitude was expressed as "Former Japanese trade negotiator Kazuhito Yamashita even suggested that 'if the US demands a US-Japan FTA, Japan should say that the US should just join the CPTPP as Japan has switched to multilateral FTAs.'"[28] Similar to the above, these provisions will allow the middle powers to solidify their power in the international system, despite potential barriers that they might face.

Control

To make collective decisions, CPTPP operates on unanimous consent. This decision-making structure reflects the perspective of middle power states, as they have created safeguards that give each state equal power over the choices that are made. As Steinberg (2002) notes above, consensus by decision-making cannot ensure equality among member states; however, an important aspect of the CPTPP process is that consensus is needed at every stage in the process.[29] Therefore, there are fewer opportunities for powerful states to push forward their agenda without consulting the entirety of the organization. Fig. 4[30] illustrates the complex sequence of steps that are required to add an additional member to the trade agreement. In sum, requiring unanimous consent at all stages is reflective of middle powers' interests to protect their influence and sovereignty in the multilateral organization. Additionally, this process dilutes great powers' influence if they were to join the organization.

However, individual states still have opportunities to express their unilateral perspective through assistance to applicants and public statements. Applicants have appealed directly to specific CPTPP members in order to bolster their application. For example, in the United Kingdom's bid for accession, the UK created connections with some existing states so that their application was received more positively. Japan and Vietnam were particularly receptive to the UK's application, with Vietnam "ready to share information and accession experience with the U.K., if the country wishes to know."[31] These types of conversations take some power away from the official process, as the informal talks have allowed the United Kingdom to move through the accession process at a faster pace. Similarly, China has appealed directly to Vietnam and Singapore's leaders to gain support for their application.[32]

[28] Kim 2019

[29] Schott 2021b

[30] Schott 2021b

[31] Hoang 2021

[32] Hadano and Hoyama 2021

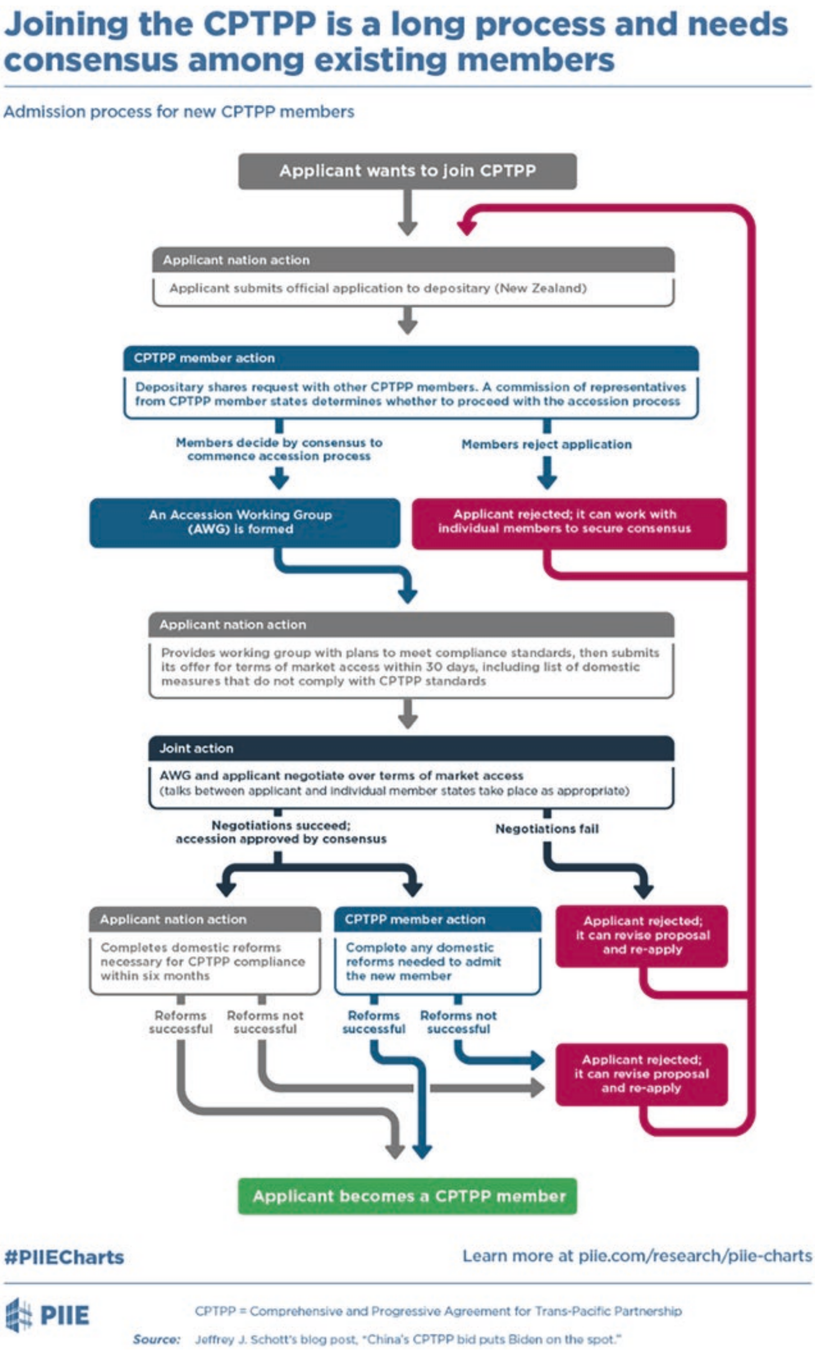

Fig. 4 Joining the CPTPP is a long process and needs consensus among existing members (Source: Peterson Institute for International Economics).

CPTPP members have also utilized public statements to make their positions clear, outside the context of the official decision-making process. These actions allow for middle powers to expand their influence on the international stage and differentiate themselves from the unanimous decisions that are reached inside the CPTPP commission. For example, following Taiwan's application, Australia expressed its support, as "the Joint Standing Committee on Foreign Affairs, Defense, and Trade said the Australian government, along with other CPTPP members, should facilitate Taiwan's accession."[33] In addition, this statement was augmented by discussions about a bilateral trade agreement between Taiwan and Australia.[34] Vietnam and Singapore utilized public statements to express their support for China's accession.[35] This is another informal channel by which states can influence the decision-making process; however, signaling their commitment to a trade deal cannot replace the arduous process that states must go through to formally accede. Therefore, the process of collective decision-making provides opportunities for states to set themselves apart while creating strong protections against any one state taking over the process unilaterally.

Scope

The scope and magnitude chosen by CPTPP members at the outset of the agreement matter, especially in its effects on applicants. The CPTPP covers "virtually all aspects of trade and investment."[36] Broadly, CPTPP includes issues such as trade in goods and services, rules of origin, customs facilitation, regulatory cooperation, government procurement, investment, intellectual property, labor, and the environment.[37] This differs sharply from arguments in the literature about middle powers only succeeding at pursuing niche international goals. Instead, the breadth of the agreement is expected to have significant effects on member states' economies, as "86 percent of CPTPP parties' tariff lines will be duty-free for originating goods. This amount will reach 99 percent within 15 years through the gradual phase-out of remaining duties, subject to each party's specific commitments."[38] Additionally, the breadth covered by the agreement will make accession a more lengthy process as the necessary reforms will be more extensive. For example, in order for China to accede, they have to abide by the standing rules in the original agreement. These standards are extremely high, even after removing some of the most selective clauses that were favored by the United States in the TPP. To indicate a willingness

[33] Chiou and Yeh 2022

[34] Ibid.

[35] Hadano and Hoyoma 2021

[36] Government of Canada 2015

[37] Ibid.

[38] Ibid.

to reform, China has begun to trial CPTPP rules in “some of China’s pilot free trade zones.”[39] However, because of the wide scope of the agreement, the reforms needed for accession are extensive. Some of the most worrying provisions for China’s accession include those on market access, labor rights, and government procurement.[40] The breadth of the CPTPP’s scope will make it more challenging for all member states to accede. However, the reforms required to join reflect middle powers’ interests and influence over the international community. In the case of the CPTPP, the promotion of liberal economic standards could have far-reaching effects as states start the accession and reform process.

Flexibility

Flexibility was extended in the CPTPP to original members; however, the agreement maintains strict standards for applicants. In initial negotiations, CPTPP members created exceptions to particular clauses in the trade agreement. For example, Vietnam and Malaysia were exempted from multiple pieces of the e-commerce clause. The agreement freed the two states from Article 14.4 (Non-Discriminatory Treatment of Digital Products) and Article 14.11 (Cross-Border Transfer of Information by Electronic Means) for 5 years after the agreement commenced. These exceptions allowed the states to convince their domestic public that the necessary reforms were feasible after accession. This is important, as Vietnam is utilizing its CPTPP membership to “induce further domestic reforms by aligning external pressure over domestic vested interests.”[41] Therefore, moderating the extent of reforms in Vietnam was necessary to induce these broad economic changes. However, the organization is selective about how they apply these exceptions and has made clear publicly that they are unwilling to do so for great power states (i.e., China).[42] Beyond these verbal commitments, experts posit that exempting China would be “implausible given China’s size alone.”[43] However, it is possible that without the inclusion of the United States in the agreement, member states may have an incentive to welcome China into the CPTPP to take advantage of its large market and economic force. Because the TPP was originally created as a counterweight to China’s growing economic power, member states may leverage the opportunity to push China toward liberal economic reform. This situation exhibits an opportunity for middle powers to coerce a relatively large state and affect the international economic order broadly.

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[39] Ibid.

[40] Solis 2021

[41] Doung 2022

[42] Solis 2021

[43] Schott 2021a

Centralization

Centralization is limited in the CPTPP, as there is no secretariat or independent body that is tasked with managing the trade agreement.[44] Instead, "New Zealand serves as the official repository country for ... the CPTPP."[45] Therefore, applications to the agreement and other official documents are housed there. To balance the responsibilities among member states, another official post in the organization is the role of Commission Chair. This position rotates annually and "is dictated by the order in which members joined the agreement."[46] The lack of centralization in the organization will extend the time that it will take for new members to accede.[47] However, what centralization lacks in efficiency it makes up for in equality among member states. This model does not allow the body to privilege certain members or for the organization to become completely politicized. CPTPP provides an internal dispute settlement mechanism for members and investors. This portion of the PTA "promotes investor confidence and can protect against sovereign or political risk."[48] The mechanism cannot infringe on state's sovereignty by negating its domestic laws and regulations.[49] The disputant can decide on the forum in which it would like to pursue adjudication. For example, if there is an issue that could be managed by the WTO or CPTPP, the member state would have discretion between the two dispute settlement bodies. Therefore, this centralized component allows multiple forums for disputants to pursue their claims, in the arena that they believe will be the most fair or impartial.

5 Digital Economy Partnership Agreement (DEPA)

Membership

DEPA currently has three members—Chile, New Zealand, and Singapore. Similar to the CPTPP, DEPA is not a geographically regional organization and thus provides avenues for new members from around the world to accede to the trade agreement. However, because of the recency of the agreement, there are currently not clear standards on how states can accede. Rather, the agreement states that the standards must be agreed upon by all member states. DEPA's signing text highlights that the agreement contains "high quality standards" that may be difficult for applicants to

[44] Elms 2021c

[45] Elms 2021b

[46] Elms 2021b

[47] Elms 2021b

[48] Australian Government 2019

[49] Australian Government 2019

achieve. South Korea and China have requested to join the agreement in September 2021 and October 2021, respectively. Since their applications, DEPA has established a working group to define these expectations more clearly.[50] Additionally, these working groups include "participation of technical teams from the four countries, which will review and evaluate Chinese standards and regulations, conducting a series of questions and answers to determine compliance with the norms and standards already negotiated in the agreement."[51]

DEPA is also nested within the Asia-Pacific Economic Cooperation (APEC), which, similar to CPTPP, gives it the advantage of deferring to the APEC standards when facing a potential challenge. Additionally, APEC's main tenets are reflected in the agreement's focus on improving economic integration and creating shared regulatory standards. As stated above, the nested nature of DEPA provides significant leverage to middle power countries to credibly commit to standards as great powers apply and accede to the agreement.

Scope

The scope of DEPA is limited specifically to the digital economy, making it significantly less ambitious than the multitude of issues covered by CPTPP. The topics addressed in the agreement include "electronic payments, personal data protection, digital identities, online consumer protection, fintech, and open government data."[52] Interestingly, the agreement is framed explicitly around how cooperation under these auspices can benefit smaller economies, relative to great powers.[53] Increasing the comparative advantage of smaller states in the digital economy marketplace could have profound effects on their growing economies. More specifically, DEPA established these standards to encourage multinational corporations to invest and establish their businesses in these locations.[54] Additionally, the scope of the agreement has significant implications for membership. Because of its limits, "a sectoral deal on digital issues would not require formal approval from the U.S. Congress, since the United States would be making no new market-access concessions."[55] Therefore, the scope creates opportunities for cooperation beyond its original creators by limiting domestic hurdles. This procedural difference could allow great power states to join DEPA more easily and bolster the agreement's legitimacy.

The depth of the cooperation within the limited scope of issues will provide significant benefits to member states. DEPA is the first agreement of its kind with an

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[50] Kurohi 2021

[51] Chilean Ministry of Foreign Affairs 2021

[52] Elms 2021a

[53] Chilean Ministry of Foreign Affairs 2021

[54] Ibid.

[55] Goodman 2021

explicit focus on the digital economy.[56] The conversations around digital economy in DEPA progressed past what was accomplished in the e-commerce clause in the CPTPP.[57] Therefore, it reiterates one of the many issues that were discussed in previous negotiations and finds opportunities for more intense cooperation. The impacts of this agreement will expand far beyond the middle powers that designed it, because of the ingenuity of this type of cooperation. Aiming for depth in a cooperative agreement on a new issue provides a framework for future institutions and clauses.[58] The first mover advantage of DEPA will magnify its impact in the international community and reflects the previous literature that indicates middle powers' particular influence in niche issues. There are many digital economy negotiations underway, most notably in the WTO. It is possible that DEPA's framework will be carried over into these expansive multilateral agreements.

Control

Decision-making is conducted by consensus in DEPA. Additionally, changing decision-making rules requires consensus among member states. Although the decision-making is not codified as clearly as in CPTPP, there is constant reference throughout the body of the agreement that states must be in "mutual agreement" to move forward. For example, in the case of disputes between two states, parties are required to work together to locate agreed upon locations, mediators, arbitrators, and mutually satisfactory resolutions. Therefore, both the disputant and defendant have equal standing to influence the initial stages of this process, rather than creating a standing body that could be politicized or influenced by their self-interest. This has been voiced as a concern at the WTO, as Brutger and Morse (2015) demonstrate. Because of the design of the WTO dispute settlement bodies, there exist "a set of incentives that encourage panelists to moderate rulings against the most powerful WTO members."[59] Middle powers have incentives to limit politicization at all costs, as it has often disadvantaged them in other international organizations.

However, recognizing that this process of agreement may be difficult in tense disputes, DEPA suggests that the parties solicit the WTO Secretary General, among others, for assistance if necessary. Nesting is at work again in this case, as the body defers to the WTO as the final arbitrator in case of difficulties in reaching mutual agreement. As stated above, by nesting, actors are able to resolve their competing interests and defer to the overarching institution. In this case, DEPA is compatible with the meta regime, or the principles and norms, of the WTO. Therefore, nesting provides an additional safeguard against overt coercion by great powers in a dispute,

[56] Chilean Ministry of Foreign Affairs 2021

[57] Ibid.

[58] Ramasubramanian 2020

[59] Brutger and Morse 2015

if they were to join DEPA in the future. This reflects middle powers' concern for their autonomy and sovereignty in the institution, and the overall framework of control in DEPA highlights the importance of equality and mutual decision-making.

Flexibility

In contrast to CPTPP, DEPA is not legally binding, and there is not an associated dispute settlement body ingrained in the institution.[60] This provides a significant amount of flexibility for member states, with a greater focus on the establishment of norms and collaboration. The nonbinding nature of the agreement may provoke concerns about whether it will create any change in the international community. However, this approach "has proved effective in an Asian context, as evidenced by the useful work in the Asia-Pacific Economic Cooperation (APEC) forum."[61] Additionally, the agreement is divided into 12 distinct modules that provide guidance on digital policy.[62] The modular format allows for states to implement portions of the agreement, while excluding others.

The treaty also allows New Zealand to have significant flexibility to fulfill its obligations under the Treaty of Waitangi. This treaty requires New Zealand to provide favorable treatment to the Maori people. This treaty is no longer part of New Zealand's domestic law explicitly, but its historical importance and recent activism have called attention to its continued importance. Similar clauses exist in other free trade agreements that New Zealand has signed.

However, this flexibility does not appear to extend to accession into DEPA. Instead, states are required to meet the "high standards" outlined above. The process for accession is not codified. However, as DEPA members have been considering China, Canada, and South Korea's interest in joining, important factors under examination include states' regulatory regimes and data transparency.[63] Statements from member state officials imply that similar to CPTPP, the organization will require reforms if states are not already in line with their expectations on the digital economy.

Centralization

DEPA is extremely decentralized, again reflecting its non-binding status. Rather than establishing a central dispute settlement body, the agreement encourages each member state to create independent tribunals to resolve disagreements.[64] Additionally, if mediation is necessary, disputant states must find an agreed upon

[60] Chilean Ministry of Foreign Affairs 2021
[61] Goodman 2021
[62] Ramasubramanian 2020
[63] Tan 2021
[64] DEPA Signing Text 2020

mediator to help them resolve the dispute.[65] Therefore, the procedural elements are documented in the agreement, but are not accompanied by strong internal and centralized bodies to draw upon for assistance.[66] As mentioned above, this decentralization places disputants on equal playing fields as they must agree upon the venue and source of mediation rather than allowing for a centralized body that could become politicized by great powers who join the agreement.

Additionally, the parties are obligated under DEPA to meet once a year. However, they did not establish an independent secretariat. Therefore, power is concentrated among the member states themselves, rather than transferred to any independent agents in the organization. As mentioned in the case of the CPTPP, the decentralization of the organization complicates the accession of new member states and creates inefficiencies. However, under the framework of middle power interests, it is clear that the protection of individual state sovereignty outweighs these externalities.

6 Conclusion

In recent years, middle powers have created and designed international organizations, with emblematic examples found in DEPA and CPTPP. These organizations are characterized by open membership, decision by consensus, discretionary flexibility, and limited centralization. However, the scope of the organizations varies widely which reflects that middle powers can be successful championing either depth or breadth.

This paper provides a first cut at analyzing how middle powers design international institutions. Therefore, it makes several contributions to the current literature on middle powers and institutional design. First, it documents the mechanisms with which middle powers exert influence, in a way that is different from the narrative in the current literature. Most importantly, they are creating and designing international institutions with wide-ranging goals. However, at the same time, middle powers are leveraging their historical advantage in furthering niche issues and working through multilateral institutions. Additionally, this article builds upon Koremenos et al. (2001) and Aggarwal (1998) to illustrate how middle powers are pursuing their self-interest as they design institutions, which results in unique institutional design. There are significant benefits to derive from great powers' participation, so international organizations are designed to allow for their accession. However, learning from their experience in other international organizations, middle powers have created safeguards to avoid institutions that are largely run by politicization and power calculations. Finally, this paper provides an in-depth analysis of the design of the CPTPP and DEPA. As states continue to apply to these preferential trade agreements, it is probable that their influence on the international system will only

[65] Ibid.

[66] Ibid.

increase. Therefore, understanding how they are structured at their outset will allow us to better understand their benefits and consequences in the future. Additionally, in the context of the US-China trade war, these organizations created in the Indo-Pacific by middle powers will have significant effects on future systemic power calculations.

In sum, this paper documents a growing phenomenon, namely, the design of institutions by middle powers. Future research should provide further analysis of the institutions in which middle powers have an unprecedented role. The CPTPP and DEPA were constructed by similar actors, and their memberships are concentrated in the Indo-Pacific. Therefore, this comparison may not be highly generalizable to all middle power activities in institutional design. While this paper identifies a growing phenomenon, utilizing quantitative methods to parse the major differences in middle power design could aid in developing more comprehensive and overarching theory in the future. Additionally, these types of agreements could be placed in conversation with regional trade agreements to understand how they might differ. For example, regional trade agreements may not expect the accession or application by states outside of their geographic region. Therefore, the safeguards that exist in these agreements may be limited, and other design characteristics may differ.

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EU's Geo-economic Strategy in the Indo-Pacific

Cho-Hsin Su

1 Introduction

As a gradually integrated supranational actor on world stage, the European Union (EU) has been developing slowly its common position toward international affairs. Geopolitically speaking, the EU's main focus on external relations lies in its neighborhood, namely, Russia, Eastern Europe, and the Mediterranean region, in addition to maintaining its strategic relationship with the United States (US). It is another story from the geo-economic point of view since first of all, as the world's biggest common market with full competence on its economic policy, the EU has a much stronger say in its external relations regarding economics. Secondly, with the globalization and the development of global production networks, the EU has found its most suited economic partners outside of its neighborhood, most importantly in Asia since the twenty-first century.[1] However, East Asia is a region that embodies the upfront US-China competition global structure. Traditionally, it is an area where the US and China enjoy a preeminence position for historic reasons. The new power dynamic of US-China competition, however, makes the region at the heart of geo-economic tensions and gives the EU a more relevant role in the midst of this new geo-economic competition.

[1] For example, ASEAN is currently the third largest trading partner of the EU, after China and the US, and vice versa. And the EU is the largest investor in ASEAN countries. See the European Commission official website, https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/association-south-east-asian-nations-asean_en

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That said, for the EU to play a significant role in the region, it needs first and foremost to act as one unified power and establish its international actorness on the world stage. This aspiration has been called out again and again by prominent political figures in Europe since the second half of the 2010s. From Angela Merkel's proclamation that "Europe must take fate into its own hands" to Emmanuel Macron's "European sovereignty" speech at the Sorbonne,[2] and more recently to Olaf Scholtz's endorsement to the "European Sovereignty" concept at Charles University in Prague, the prospects of one unified European power keeps piling up until Ursula von der Leyen officially declared that the European Commission under her helm since 2019 will be a geopolitical one. With the same confident tone, the EU High Representative, Josep Borrell, unequivocally called for "strategic autonomy" as the new EU strategy amid US-Sino competition in his 2020 article so that the EU would not have to "choose between being a Chinese colony or an American colony."[3] In 2021, the EU came up with its first "Indo-Pacific Strategy," which picked up the term "Indo-Pacific" upheld by the US, but with content that centers around incorporating China into regional strategy.

The inquiry of this research starts here – whether there is an EU's geo-economic strategy in Indo-Pacific and, if so, how it is carried out in the region. As Schunz denotes in his studies, "a strategy is about systematicity and creativity with regard to both content and process (ways) for effectively using resources (means) to attain objectives (ends)."[4] He also distinguishes planning from strategy and argues that "sound planning needs to be based on an overall structure and the necessary guidance for a foreign policy actor."[5] As mentioned earlier, the EU's end goals in the region could be identified as becoming a relevant power and finding its strategic autonomy amid the US-China competition. To understand how EU's geo-economic strategy in the Indo-Pacific is established, this paper begins with examining the ways of this strategy, reflected in the EU's current external policies in Indo-Pacific. Then it focuses on the three primary policy fields where the EU is most visible in the region and recalibrates the latest development of EU's multilevel governance system in these policy fields. This paper argues that the unique way of common policy-making of the EU affects its international actorness and how the EU's multilevel governance works in different policy areas will hinder or support the strategic autonomy of the EU. Finally, it depicts how the EU navigates the geo-economic tensions in the Indo-Pacific by using this strategy, following the new principled pragmatism directory.

[2] The "European sovereignty" proposed by President Macron in his Speech at the Sorbonne in 2017 embodies a transformation of the concept of sovereignty, which goes beyond the traditional configuration of nation-state. It does not imply, therefore, that the EU is moving away from a supranational organization to a state.

[3] Borrell 2020

[4] Schunz 2018, pp. 341–342

[5] Schunz 2018, pp. 341–342

2 EU's Policies in the Indo-Pacific

As a unified actor on the world stage, EU's geopolitical actorness is less evident in the Indo-Pacific than the US and China. Its security presence is much less significant than the other two powers, and its common foreign policy on political issues also lacks weight.[6] On the other hand, the EU enjoys much greater visibility in trade, development, and environmental policies in the Indo-Pacific. Trade policy as a discipline has gradually "become more of a means of economic statecraft" in the latest development.[7] The concentration of power gives the EU more capacity to scheme out its long-range trade policy in the world. Since the launch of the 2006 "Global Europe: Competing in the World" strategy,[8] the EU has made clear its ambition to become a world leading economy with the highest level of trade standards. It had right away turned to Asia to find its partners to sign this new series of trade agreements. The region was chosen not only because East Asia is the fastest-growing market in the world but also due to the fact that Europe and East Asia are two regions with complementary trade structure and have great potential in creating closer economic ties. By 2018, two-thirds of EU's top trading partners fell within the Asia-Pacific region.[9] South Korea became the first partner that EU signed a seminal FTA with in the Indo-Pacific region. The EU-Korea FTA was signed in 2010 and took effect 1 year later. After that, the EU started negotiations with almost all Asian partners. Some negotiations got stalled, others moved forward, and a few of them went into force, namely, the economic agreements with Japan, Singapore, and Vietnam. This policy direction has remained largely unchanged for the past two decades. That said, the recent developments – namely, the economic rise of China, former President Trump's resultant response with protectionism, and the economic damage to the European economies brought by the COVID-19 pandemic – have substantially changed the international trade environment and sharpened the geopolitical and geo-economic tensions, which triggered the EU to "launch a public consultation process for a review of its trade policy." The European Parliament, Member States, as well as civil society and business groups were therefore all involved in this review process to provide feedback, which resulted in the 2020 "A Renewed Trade Policy for a Stronger Europe: Consultation Note" and the 2021 "Trade Policy Review – An Open, Sustainable and Assertive Trade Policy."[10]

According to the Commission, the "Open Strategic Autonomy" indicates that the EU wants "to continue reaping the benefits of international rules-based trade and exerting leadership in the international sphere, while having the right tools in place to protect ourselves from unfair practices."[11] Moreover, the EU vows to promote this

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6 Su 2022

7 Adriaensen and Postnikov 2022, p. 470

8 European Commission 2016

9 Eurostat 2018

10 Schmucker and Mildner 2020

11 European Commission 2020

idea notably by "increasing the EU's capacity to pursue its interests and enforce its rights."[12] In the words of Charles Michel, the President of European Council, himself, "we will reduce dependencies and achieve resilience in areas such as energy, digital, cyber security, semiconductors, industrial policy, trade and reinforcing the single market."[13] The key objective for the EU is then to diversify trade relationships while stabilizing its strategic engagement with key trading partners.[14] Under this new "open strategic autonomy" policy, global trade is considered as the engine for economic growth and will be fundamentally important for Europe's recovery. Regarding the existing policy of FTA signing in Asia, the EU is likely to give an extra push for concluding more FTAs with ASEAN countries. Moreover, the COVID-19 pandemic also revealed the strategic importance of medical supplies. As "six of the world's top ten exporters of medical and pharmaceutical products are from the EU market," an FTA that fosters liberal trade undoubtedly would enhance ASEAN governments' control over the pandemic crisis[15] and, thus, provide more incentives to the ASEAN authorities to conclude the FTA negotiations.

While the EU continues this bilateral FTA signing policy in Asia, it has also begun to propose more ambitious, region-wide, economic foreign policy in the region in the past 2 years, namely, the "Global Gateway." It was introduced as a new vision and a concrete implementation plan to build "smart, clean and secure links in digital, energy and transport sectors and to strengthen health, education, and research systems" around the world.[16] It would be a comprehensive development program that covers both hard and soft infrastructure to create connectivity, with green and digital transitions and with guiding European value-based norms. The Global Gateway program authorizes the deployment of 300 billion euros for projects spanning from 2021 to 2027. In the communication, four concepts are highlighted: high standards, good governance, transparency, and sustainability. For now, the employment of the infrastructure projects seems most promising in the neighborhood of the EU and in countries with which the Member States have long historical connections.[17] At the EU-African Union Summit held in February 2022, the first Global Gateway regional investment plan was announced, with 150 billion euros in financing over 7 years for the investment package. The five priority areas would be "accelerating the green transition, accelerating the digital transition, accelerating sustainable growth and decent job creation, strengthening health systems, and improving education and training."[18] Concrete plans in other regions, however, are still in discussion. In June 2022, the European Commission held a global forum on development cooperation – the European Development Days – focusing on the

[12] European Commission 2021a

[13] European Council 2021

[14] Lutz et al. 2021, pp. 41–42

[15] Hsieh 2022, pp. 135–136

[16] European Commission 2021b

[17] Karjalainen 2022

[18] European Commission 2022a

Global Gateway. In the session of "The Global Gateway in the Indo-Pacific," panelists from Europe and Asia joined together to discuss a feasible plan for Global Gateway in the region. One general agreement among the panelists was that the Indo-Pacific is a vast region with actors of great diversity. The EU should therefore avoid the "one size fits all" approach and try to make tailored investment plans that correspond to each partner's needs.[19] Before the arrival of an official Global Gateway in Indo-Pacific package, some smaller in scale development projects are already in place. Okano-Heijmans and Vosse, for example, argue the importance of continued digital development cooperation between two sides, not only because the EU has role to play amid the US-China competition in the region and presents an alternative to what the great powers are offering but also because "digital development cooperation is important for both developmental and normative reasons – to set against a context of rising digital authoritarianism and to spread liberal norms like openness, transparency and privacy in the digital domain."[20] Grzegorzewski also makes an elaborate study on the EU's actions supporting Asia-Pacific countries in combating the pandemic, which comprises not only vaccine provision but also numerous development programs to help the countries in the region build long-term resilience to epidemic crisis.[21]

Because of the series of impressive climate policy achievements, the EU has gradually become the global leader in the field, which gives this internal policy an external dimension especially in its relations to its Indo-Pacific partners. In Asia, environmental policy has raised more and more attention, especially when it is linked with development issues. In 1997, the Asian Development Bank (ADB) noted that "the root cause of the poor state of the environment in the region was a failure of policy and institutions, and that the ecological degradation is becoming more and more a constraint on future economic development."[22] The EU thus comes into the picture as the most suitable partner. It integrates the environmental policy with its foreign policy in the region by investing a large sum of financial resources in helping the most vulnerable countries adapt to the rapidly changing environment and build resilience to climate change. In terms of the modalities, besides direct grant funding to the most climate vulnerable countries, the EU also uses grants to leverage private investment by combining grants with other financial resources from both public and private sectors. For example, the Global Climate Change Alliance Plus, the EU flagship initiative focusing on highly climate vulnerable developing states launched in 2007, has already contributed US$19.47 million to Nepal Climate Change Support Programme from 2013 to 2015.[23]

In the same vein, in recent years, the EU and China have increasingly recognized the importance of working together on global climate issues. Gurol and Starkmann

[19] European Commission 2022b

[20] Okano-Heijmans and Vosse 2021

[21] Grzegorzewski 2022

[22] ADB, 199

[23] Mahat et al. 2019, p. 5

note in their research that despite some political challenges, there have been several critical moments that have led to improved cooperation between the two parties.

One such moment was the 2009 Conference of the Parties, which encouraged the EU to adopt a more collaborative approach to climate governance. The Paris Agreement of 2015 was another turning point, as China shifted its role from policy-taker to active participant in the fight against climate change. Finally, the US's exit from the Paris Agreement in 2017 "created a leadership vacuum, opening a window of opportunity for the EU and China to readjust their positions in the international climate governance system and fostered EU–China cooperation."[24]

Gradually, the EU and China developed a joint vision about the importance of reducing pollution in general and a common interest when it comes to enhancing their energy security, which makes bilateral cooperation per se, as evidenced by the China-EU Partnership on Climate Change, much more probable. Besides, the endeavors to fight climate change also present economic opportunities, especially for low-carbon technology sectors. This could be of great interests to China and to some key EU Member States, namely, Germany and France.[25] This EU-China climate cooperation has been disrupted by the outbreak of the global pandemic, but it is argued that the pandemic impact would be temporary.[26]

3 EU's Multilevel Governance in External Actions

In summary, the EU's actions in the Indo-Pacific are much more significant via trade, development, and environmental policies than through security policy. This observation hence brings focus to the very unique governance system of the EU. As a *sui generis* political construct, since the beginning of the regional integration development in the 1950s, the European community has created an innovative public governance system that transcends national boundaries. It began with functional integration in certain policy fields and then gradually spilled over to other fields of public policy.[27] Throughout this process, a distinct governance system is built to facilitate the public affairs that associate supranational, national, and subnational levels. The academic literature on the multilevel governance of the EU is now an extensive body of work.[28] Generally speaking, the multilevel governance indicates the shifts in power and authority relations within the political structure in Europe. The formulation of the concept began in the early 1990s, which went hand in hand with the European integration process and its ever-evolving governance structure. The fundamental notion is "decision making in a pluralistic and highly dispersed

24 Gurol and Starkmann 2021, p. 530

25 Belis et al. 2018, p. 96

26 Zhang and Gong 2020, p. 87

27 Haas 1968

28 Enderlein et al. 2011; Hooghe and Marks 2001; Rosenau et al. 1992

policymaking milieu where multiple actors participate at various political levels."[29] Overall, it means the reduction of state sovereignty through competence sharing between European, national, and subnational levels and through joining of international coordination mechanisms.[30]

Through this complex web of governance, the EU's external policy is like no other. Different from nation state's political system, the EU's external policy includes not solely its Common Foreign and Security Policy (CFSP). In fact, in this multilevel governance political system, each policy holds a different level of integration among Member States and, subsequently, provides varied international actorness for the EU when it engages in external relations. Overall, to have one common foreign policy facing the world is not an easy task for the European bloc. Since the very beginning of the regional integration development, the idea of a common defense community was proposed that went as far as creating a common armed force and common budget for a European Defense Community. The plan did not come through, but the idea subsisted and had been repackaged several times in the following decades. In 1992, the CFSP was formally introduced as the second pillar of the European Union with the Maastricht Treaty, and a more security-focused European Security and Defense Policy was launched in 1999, which was later relabeled as Common Security and Defense Policy (CSDP) in 2007 with the Lisbon Treaty. To gain more actorness in IR and further disentangle from the traditional Atlantic Alliance, the strategic autonomy concept was built up with more substantial content since 2016 with the EU Global Strategy,[31] namely, the Permanent Structured Cooperation (PESCO), an enhanced defense cooperation framework in 2017, and the Strategic Compass in 2022, which actually granted the EU a rapid deployment capacity of up to 5000 troops.

As foreign and security policy is core to any state's sovereignty, the CFSP and CSDP have remained intergovernmental in nature with Member States retaining most control. That said, with treaty reforms, new mechanisms setup, and everyday practice of the multilevel governance system, the EU has progressively developed a working mode of forging a common stand on managing its external relations. Coordination between the EU's foreign policy structures and the national diplomacies of its Member States is essential for the EU to form coherent and effective global action in the changing world order. As Balfour, Carta, and Raik note, the national diplomatic structures and working processes of the Member States "are being shaped by the new EU foreign policy system that entails increased interaction and interpenetration between the EU and national levels."[32] They summarize the scholarly work on the issue and identify three modes of complex interactions between national and EU foreign policies, including "downloading," "uploading," and "cross loading," which together form the socialization between the European

[29] Stephenson 2013; Ishtiaque 2021, pp. 172–173

[30] Piattoni 2009; Di Gregorio 2019, p. 65

[31] European Commission 2016

[32] Balfour et al. 2015, p. 1

elites at supranational and national levels which contribute to policy convergence. They also note that it is empirically difficult to draw neat distinctions between the three modes.[33] Overall, while there certainly is socialization among agents at different levels, the legal base for CFSP and CSDP remains in the shared competence category with the Member States retaining largely the power.

While the autonomous geopolitical actor is still in the making, as a traditionally strong trade actor in the world, Brussels is much more unified on trade policy. This is because the common market and trade policy has been the heart and showpiece of the integration process since the very beginning. "Together with agriculture and competition policy, it was one of the few policy domains that were transferred immediately to the supranational level by the Rome Treaties launching European integration."[34] Scholars have noted that even with some changes in priorities over time, the EU's trade policy shows an astonishing continuity, mostly because of the continuous centralization of EU trade policy since the Treaty of Nice.[35] While the conferral of power still follows the principles specified in the Treaty on European Union (TEU),[36] through treaty revisions and rulings by the Court of Justice of the European Union (CJEU),[37] the authority at the European level incrementally extended to the point where the Member States basically handed all their say on trade over to the supranational level of governance. While various agents, including the European Commission, European Parliament, and the Member States, as well as civil society organizations, industrial associations, etc. are all engaged in the policy formulation,[38] trade policy falls in the category in which "the EU has exclusive competence." This means that the EU institution, namely, the European Commission, is granted expansive powers to coordinate between Member States on their trade policy positions and to negotiate on behalf of the Union with third countries. The Directorate General for Trade in the Commission and its officials are the primary actors responsible for concrete policy formulation.[39] With the Lisbon Treaty in 2007, EU's trade policy competence was indeed expanded to "services, intellectual property rights, and investment," which then considered "complete," with the ordinary legislative procedure. In the ruling on the EU-Singapore Agreement, the CJEU decided in its opinion 2/15 that "the EU is now fully competent for concluding a comprehensive 'twenty-first century trade agreement', except for the provisions on non-direct investment and for investor-state dispute settlement (ISDS)."[40] While the

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[33] Balfour et al. 2015, p. 6

[34] De Ville 2020, p. 278

[35] Lutz et al. 2021, p. 38

[36] The Article 5 of TEU specifies the limits of the EU competences as they are governed by the principles of subsidiarity and proportionality.

[37] Such CJEU rulings include "Case 22/70 Commission v. Council (AETR) [1971] ECR 263, 275"; Opinion 1/78 re International Agreement on Natural Rubber [1979] ECR 2871; Opinion 1/94 re WTO Agreement [1994] ECR 1–5267, etc.

[38] Park 2017, p. 836

[39] Lutz et al. 2021, p. 32

[40] De Ville 2020, p. 280

Member States have lost its say in the decision-making process, new actors are playing bigger roles and seeking influence in the process, such as business associations, trade unions, and nongovernmental organizations.[41]

Highly related to trade, another important external action of the EU is its development cooperation. Article 208(1) of the Treaty of the Functioning of the European Union (TFEU) specifies that "Union policy in the field of development cooperation shall be conducted within the framework of the principles and objectives of the Union's external action" and that it "shall have as its primary objective the reduction and, in the long term, the eradication of poverty." According to the latest data of the Organization for Economic Co-operation and Development (OECD), the EU and its Member States remain the largest donors of Official Development Assistance (ODA) in the world.[42] Because of this position as donors, the EU has been granted a certain capacity to influence its partners, wherefore development cooperation becomes a crucial part of its external relations. The legal basis of EU's competence in this policy area lies in Article 4(4) TFEU, where it puts development cooperation in the shared competence category and determines that "in the areas of development cooperation and humanitarian aid, the Union shall have competence to carry out activities and conduct a common policy; however, the exercise of that competence shall not result in Member States being prevented from exercising theirs." On the one hand, the article provides the EU with a prevailing stance in forging common policy in development cooperation. On the other hand, co-existence of development policies between the EU and Member States requires the European Commission to coordinate policies at different levels to ensure coherence and consistency in the EU's development cooperation with third parties. In addition to implementing its own development programs, the European Commission must work to coordinate policies between the EU and its member states. This coordination is crucial to ensuring that the EU's development policies are aligned and work together effectively.

Another area where the EU has built up its international actorness lies in its sustainable development efforts. Internally, the Single European Act of 1987 had established a sound legal basis for the EU's environmental policy. The Act basically exhibited a general opinion among the European citizens that the EU is the apt level to adopt rules to protect the environment, which could minimize the risk of competition distortions within the EU's domestic market. According to this legal framework, the Council, which represents "the Member States, could co-decide with the European Parliament upon environmental regulations" with qualified majority vote. This mechanism provides the Member States with ample engagement in the decision-making process and yet leaves Brussels with enough authority to generate common policy and goals. Member states are given the task to set for "binding targets and to put in place concrete policies to meet them." After more than three decades of operation, now we could find in the EU legislation a complete set of

[41] Lutz et al. 2021, p. 33

[42] OECD 2022

regulations addressing environmental protection of air quality, water, and biodiversity.[43] The EU also implements various sector-specific measures at a union-wide level to help countries achieve their targets.[44] With the example of EU ETS,[45] it operates in all EU member states, as well as Iceland, Liechtenstein, and Norway, covering approximately 40% of European total emissions. To be more specific, the European Commission and the EU member states collaborate closely in the operation of the Union Registry. Under this system, each member state is responsible for administering accounts and, when necessary, providing "services in national languages." This may include offering helpdesk support to users of the system. Other players, such as market intermediaries (banks, brokers) and individuals, can also become account holders in this system.[46] And the EU continues to champion in its environmental regulations. Its objective to cut its net emissions by 55% from 1990 levels by 2030 has been embodied in a package of energy and climate laws, named "Fit for 55." In the Council's conclusions ahead of the UN Climate Summit 2022, the COP27 in Sharm El-Sheikh, Egypt, recalls the "Fit for 55" package and emphasized the level of ambitions the EU is ready to commit on climate actions.[47]

In sum, the EU's common foreign policy, in the strict sense of the term, remains intergovernmental in nature with Member States playing the dominant role, whereas the EU struggles to forge common position in face of the rapidly changing international environment. Despite its limitations in certain areas, the EU has been able to establish itself as an international actor through other policy fields where it has either exclusive competence or shares competence with its Member States but is given a leading role in developing a European agenda. For varied reasons that will be discussed in the following section, trade, development, and environmental policies have become EU's strongest tools in achieving its foreign policy objectives and have helped the EU establish substantial connections with the world. Sometimes, the EU would even combine the three policies to form robust common strategies, such as the European Green Deal, the flagship project launched by the Von der Leyen Commission which tactfully formulated a major development strategy that boldly based the economic recovery plan on more progressive environmental regulations.

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[43] Delbeke and Vis 2015, pp. 11–12

[44] Delbeke and Klaasen 2015, p. 93.

[45] The EU has "developed novel ways to share the effort required to reduce emissions between its MS and across different economic sectors, namely the EU Emissions Trading System (ETS). It is "the world's first multi-country cap-and-trade scheme for greenhouse gases," and it has been emulated elsewhere.

[46] Meadows et al. 2015, p. 45.

[47] Council of the European Union 2022.

4 EU's Geo-Economic Strategy and the Principled Pragmatism Maneuver in the Indo-Pacific

With these continued engagement policies in the Indo-Pacific, the EU has progressively built up its geo-economic strategy in the region, by virtue of its multiple external policy instruments. Regarding the means, distinct from other powers in the region, the resources of this approach are neither of military nor of economic nature. Instead, the persistent normative direction, its accumulated expertise, an ever more comprehensive regulatory framework, and its multiple policy instruments permit the EU of its leading role in engaging in trade, development, and environmental issues in the Indo-Pacific. This normative policy via trade, development, and environmental cooperation corresponds to the "normative power Europe" (NPE) concept, which was first shown in Ian Manners' seminal article published in 2002.[48] And since then, the concept has been unremittingly enriched by both academia and EU elites, which now creates an expansive literature on the NPE studies[49] and by simply putting it into practice. Nonetheless, the NPE identity building does not go without a hitch. In fact, it has been confronted with numerous challenges and setbacks in the past decade. In the aftermath of the Arab Spring, the Crimean crisis, and the migrant crisis that followed starting from 2015, the EU was forced to face the reality that even if the NPE image was successfully built, it does not necessarily imply that the European norms can be internalized by its partners and that the security situation is worsening in its close neighborhoods. Throughout the expansion of NPE, EU's close neighbors actually turned into chaos and created genuine threats to Europe's stability. In response, Natalie Tocci, who served as an advisor to the High Representative Federica Mogherini from 2014 to 2019, proposed an important reform of the NPE concept, named "principled pragmatism." The new concept was well elaborated in her book *Framing the EU Global Strategy*, in which she states that when facing all the new challenges in its close neighborhood, the EU should adopt a "pragmatic philosophy that looks at the world as it is and not as it would like to see it."[50] This reformed idea of NPE gives the EU more flexibility in its external policies in the Indo-Pacific, where its geo-economic strategy is applied with more resilience.

Taking a closer look at the trade agreement negotiations with Asian partners, the EU has indeed inserted its normative program into discussion with no exception.[51] In each of the FTAs signed with its Asian partners, there is a "sustainable development" chapter that covers issues ranging from labor rights protection to environmental regulations, which is something that was previously not on the agenda of any trade agreement talk of the Asian countries. Besides the great consumer market size that creates attractiveness for Asian economies, Bradford (2020) also notes other

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[48] Manners 2002

[49] Björkdahl et al. 2015; Laïdi 2008; Su 2019; Whitman 2011

[50] Tocci 2017

[51] Su 2019

sources of power that the EU acquires for partners to voluntarily insert EU norms into their own legal system, including the regulatory capacity as well as the political will to generate stringent rules. When it comes to FTA signing, economic interests and commercial goals are naturally at the heart of the negotiation. And yet, these goals do not necessarily go along with EU's geo-economic strategy in Indo-Pacific, which is to create strategic autonomy and to pursue normative objectives. The geo-strategic alignment and regulatory differences tend to complicate the negotiation process. As the Commission holds the exclusive competence in negotiating these trade agreements and in pursuing coherence between different policy goals, the principled pragmatism becomes useful as it allows the EU to have more space of maneuver. The Commission could, to a great extent, make its own judgment while moving on the spectrum, from principled to pragmatic and vice versa, according to the scenario given at the time. One important variable in the Indo-Pacific is of course the changing power dynamics and the tension rise between the US and China. This ever-changing power structure is increasingly influencing the decision made by both the EU and its trading partners in the region. Thus, they are compelled to seek out FTAs as a means of achieving strategic advantage. An instance of this is the EU-Japan Economic Partnership Agreement, which was finalized in 2017. Osborne (2017) notes that the Trade Commissioner at the time, Cecilia Malmström, expressed her will "to make the EU the global leader in free trade" and her belief that "a deal with Japan would issue a defiant counter-blast against Trump's protectionist agenda." That said, scholars have also noted that the final results demonstrated in the agreements usually reflect the prevalence of commercial interests.[52] This also relates to the EU's multilevel governance system where, in trade policy, it is in Brussels where the lobbying activities happen, instead of in the Member States. Scholars have notified that the EU industrial associations and civil society organizations have intensified their lobbying activities toward the European Commission and the European Parliament.[53] Kang especially identified the European Automobile Manufacturers' Association (ACEA) as being "frequently involved from the initial phase of development of the EU's new trade policy agenda, thereby being in a position to redirect EU trade policy toward their interests."[54] The "open strategic autonomy" principle affirms the EU's approach to geo-economic strategy in trade, emphasizing a pragmatic and principled approach. With regard to competition between the US and China in the Indo-Pacific region, the EU's strategic autonomy signifies its intent to diversify its trade partners and avoid aligning with any specific bloc. Meanwhile, the "open" aspect highlights the EU's commitment to rules-based trade and fair competition. This pragmatic approach enables the EU to have greater flexibility in selecting trading partners, without necessarily aligning with its traditional Atlantic partner. The principled stance of the EU on trade regulations and fair competition is particularly relevant in its relationship with China, with whom it has had trade disputes at the WTO for several years.

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[52] Adriaensen and Postnikov 2022, p. 469; Su 2019

[53] Kang 2015; Lee-Makiyama and Velschelde 2014; Park 2017, p. 836–837

[54] Kang 2015

Concerning EU's development policy in the Indo-Pacific, the EU tries to push forward a normative agenda that distinguishes itself from the US and China. Through initiatives like digital development cooperation and the flagship program Global Gateway, the EU aims to offer an alternative that prioritizes openness, transparency, and privacy in digital connectivity while emphasizing high standards, good governance, transparency, and sustainability in infrastructure development and loans.[55] This approach is implicitly contrasted with China's Belt and Road Initiative (BRI) launched in 2013.[56] However, there are challenges to this strategy. Geopolitically, the Indo-Pacific is far from Europe, and the region's constantly changing context makes it difficult to predict the effectiveness of the EU's normative power. Additionally, the EU's multilevel governance system can create obstacles, as Member States have differing views on China and the BRI. The 14 + 1 cooperation framework[57] and the division between Member States who have endorsed the BRI (18 out of the 27 Member States) and those who have not evidently create fault lines within the Union. Karjalainen (2022) notes that the good China relations that some EU countries depend on are making EU's joint critique toward China more difficult to happen, which potentially runs the risk that the Union's policy-making could be influenced by China. The Global Gateway aims to overcome these challenges by fostering coordination between the Commission, the EEAS, and Member States, thus bridging the gap between the CFSP and economic and development policy sides of the EU.

Regarding its environmental foreign policy, having "the most comprehensive regional environmental protection regime in the world,"[58] the EU has externalized its environmental policy and has been playing a leading role in environmental issues on world stage. It has taken unilateral, bilateral, or multilateral action with partners around the world, and it has also integrated its internal environmental objectives into its external actions. Perhaps more importantly, the EU has served as the multilateral diplomat for environmental protection in the world. This also gives the EU a vantage point in global-level negotiations on environmental policy. Scholars have argued that the EU has adopted a "leadership-by-example approach" and persistently pressed for "targets and timetables" to drive action, "including that average global temperature rise should not exceed 2°C above pre-industrial levels and that global greenhouse gas emissions should be halved from 1990 levels by 2050."[59] However, this "leadership-by-example" or "one-size-fits-all" approach exercised by the EU had not added up to a strategy but remained at a level of planning before

[55] Okano-Heijmans and Vosse 2021

[56] Karjalainen 2022

[57] The cooperation was originally established in 2012, with 16 countries from Central and Eastern Europe plus the People's Republic of China. The framework became 17 + 1 in 2019 with the joining of Greece. It then turned into 16 + 1 with Lithuania dropping out in 2021 and became 14 + 1 since August 2022 with Estonia and Latvia stepping out.

[58] Axelrod and Schreurs 2014, p. 168

[59] Rayner and Jordan 2016, pp. 1–2

2016, where its approach relied heavily on persuasion of its partners to take on EU's model without analyzing the strategic context. Following the 2016 Global Europe strategy and the advent of the principled pragmatism concept, there begins to have signs of changing within the EU, where a more joined-up global actor aspiration and a pragmatic approach in foreign policy are highlighted.[60] The pragmatic turn of EU's external policy helps facilitate EU's geo-economic engagement in Asia, which complemented its normative agenda with greater *à la carte* components in recognition of partner countries' differences and EU's own (limited) leverage over them. This allowed the Union to adopt an approach that was less centered on exporting its own model.[61] In environmental cooperation, EU's approach is no longer just about technology transfer but also about building a "thorough evaluation of EU environmental policies in order to choose policies and technologies which offer the most efficient solutions."[62] Schunz also notes that this strategic adjustment of the EU was "well informed by geopolitical considerations, an understanding of power relations, the interests and beliefs of other parties, and a more realistic assessment of the Union's own place in this complex context."[63] The same argument that the EU has developed into a much more pragmatic climate diplomat could be found in other studies as well.[64]

The environmental cooperation reflected another important asset of EU's geo-economic strategy in the region, which is the flexibility provided by its multilevel governance structure. In some cases, the multilevel governance system and the lack of one single voice on the international front could be perceived as the Achilles' heel of the EU. The "effectiveness deficit," "the internal divisions such as an incoherence between Member States,"[65] remains an issue for the multilevel governance system. But scholars also argue that it could be a plus for EU's international actorness. According to Rayner and Jordan, the EU's multilevel governance system benefits its environmental stance due to strong public support for environmental policy. This has led to increased attention and legal authority being granted to the supranational level through changes to EU treaties. At the same time, the multilevel governance system allows the Member States' governments to still maintain a certain level of autonomy, especially regarding policies related to energy, taxation, and land-use planning,[66] which makes Member States less antagonistic to a European common environmental policy. In any case, as the states are gradually less effective in coping with global challenges, such as the climate issues, the EU also gradually shifted its climate diplomacy from the hands of environment ministries to greater ownership for foreign ministries. Moreover,

[60] European Commission 2016

[61] Belis et al. 2018, p. 95

[62] Schepelmann 2006, p. 194

[63] Schunz 2018, p. 353

[64] Belis et al. 2018, p. 91

[65] Delreux 2014, p. 1017

[66] Rayner and Jordan 2016, p. 4

the global affairs are becoming more and more intertwined. Climate change issues can hardly be separated from energy issues, and environmental issues are almost always linked with trade issues. Orsini and Cobut thus point out that "the EU is increasingly aware of this institutional entanglement and tries to adopt a division of labor strategy among its different units to ensure coherence and consistency across sectors and levels."[67] The flexibility that comes from its multilevel governance system makes the EU an adaptive player in a complex power dynamic at an international level, such as the Indo-Pacific region.

To summarize, the EU's geo-economics strategy has been well established in the Indo-Pacific through trade, development, and environmental policies. From the examination of the programs and actions that the EU has delivered in the region, it is observed that this strategy is not only sustained by the distinct resources that the EU acquires – namely, the persistent normative direction, accumulated expertise, an ever more comprehensive regulatory framework, and its multiple policy instruments – but also by the transformed idea of NPE and its unique political system. The principled pragmatism and multilevel governance system provide greater flexibility and maneuverability for the EU's strategy. This is demonstrated through recent policies such as the "open strategic autonomy" in trade and the "Global Gateway" in development and climate actions, which highlight the unique and strong aspects of the EU's geo-economic strategy in the Indo-Pacific.

5 Conclusion

The EU's limited military presence in the region may pose a challenge for it to play a significant geopolitical role in the Indo-Pacific. However, from a geo-economic perspective, the EU now demonstrates both the capacity and the willingness to engage more in the region. In a region that embodies the upfront US-China competition global structure, the EU, as one of the biggest trade partners and investors in the Indo-Pacific, has come up with its geo-economic strategy amid this new power dynamic. Without substantial geopolitical significance in Indo-Pacific, the EU develops a geo-economic strategy by virtue of a series of normative policies built upon its distinct resources. This paper starts with an examination of EU's actions in the Indo-Pacific. It then proceeds by examining recent changes in the EU's multilevel governance in its external actions, particularly in the areas of trade, development, and environmental policies. It then presents an evaluation of the EU's geo-economic strategy, identifies its unique resources as a normative power in the Indo-Pacific, and explores how the principled pragmatism is being implemented in this context.

The EU has strategically focused on promoting its normative power while navigating the US-China competition in the Indo-Pacific region. It has taken a

[67] Orsini and Cobut 2020, p. 135

systematic and creative approach to cooperation on trade, development, and environment and has leveraged its unique political structure, the multilevel governance system. On the one hand, it hinders the EU's geopolitical actorness in the Indo-Pacific, as CFSP and CSDP remain intergovernmental in nature with Member States retaining mostly the control. On the other hand, it provides the EU with advantages in ensuring its normative actorness in trade, development, and environmental actions in the region since Brussels either enjoys exclusive competence or acquires stronger public support in these policy fields. The evolution that EU's trade, development, and environmental policies all reflect an external dimension and even become the main element of EU's engagement policy in the Indo-Pacific manifests EU's normative international actorness in the region, although it could generate tensions between the pragmatic commercial aims and broader foreign policy objectives at times.[68] The paper highlights the EU's resources for its normative approach, including its clear direction, expertise, regulatory framework, and policy instruments. These resources enable the EU to take a leading role in addressing trade, development, and environmental challenges in the Indo-Pacific and set it apart from other regional powers. Furthermore, the reformed version of NPE, the principled pragmatism concept since 2016, gives the EU more flexibility in its external policies in the Indo-Pacific, where its geo-economic strategy is applied with more resilience. The multilevel governance also brings out a certain level of flexibility in EU's normative policy, which corresponds to its pragmatic turn and copes more easily with its common policies and strategies.

After examining EU's geo-economic strategy in the Indo-Pacific, new questions arise, principally whether this strategy has been effective in using its resources and in attaining its objectives in finding a strategic autonomy position. For now, there are scholars who already argue that "the EU's action in the Indo-Pacific is still catching up with its rhetoric."[69] Grzegorzewski also mentions the battle of narratives with other powers in the Asia-Pacific that hinders the public perception of EU's normative actorness.[70] In the panel discussion on "The Global Gateway in the Indo-Pacific" last year in June, Xanana Gusmão, the former President of East Timor, also firmly argued that the EU should recognize more the regional reality of a vast and diverse Indo-Pacific where each actor needs more tailored cooperation plan.[71] The principled pragmatism, the reformed idea of NPE, definitely gives the EU more flexibility in its normative policies application. However, it also makes people question about EU's normative actorness and wonder how principled and how pragmatic the EU intends to be. The ongoing Russia-Ukraine War might be another great examination of EU's principled pragmatism maneuver. Nonetheless, from the Asian countries' perspectives, it might also signal the EU's shift of attention back to the

[68] Woolcock 2020, p. 219

[69] Okano-Heijmans and Vosse 2021

[70] Grzegorzewski 2022

[71] European Commission 2022b

Heartland.[72] When the willingness and the resources that the EU acquires to engage in Indo-Pacific are put into question, the normative power might appear even less attractive for its Asian partners.

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[72] Halford John Mackinder's classic work "The Geographical Pivot of History" posits that the "Heartland" refers to Eastern Europe and is a pivotal area in world politics. According to Mackinder (1904), "whoever rules the Heartland commands the world."

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Part III
East Asian Economic Statecraft

Between Big Push (Quantity) and Bankability (Quality): Geoeconomics of Infrastructure Financing in the Indo-Pacific

Saori N. Katada

1 Introduction

In the contentious world economy of the 2020s, one thing that the global leaders seem to agree on is the importance of infrastructure investment around the world. Not only does China continue its multi-trillion dollar Belt-and-Road Initiative (BRI) of infrastructure push, but Western governments are also quite keen on introducing various initiatives to invigorate global infrastructure investment ranging from Build-Back-Better World (B3W) and Global Gateway Initiative to Partnership for Quality Infrastructure (PQI).[1] In 2022, G7 leaders launched Partnership for Global Infrastructure and Investment (PGII) at its summit where they committed to

[1] B3W is based on US President Biden's original domestic initiative of 'Build Back Better' economic recovery plan arising from his presidential campaign promise. The US advocated B3W at the 2021 G7 Summit in the United Kingdom. FACT SHEET: President Biden and G7 Leaders Launch Build Back Better World (B3W) Partnership, June 12, 2021 (available: https://www.whitehouse.gov/briefing-room/statements-releases/2021/06/12/fact-sheet-president-biden-and-g7-leaders-launch-build-back-better-world-b3w-partnership/). Global Gateway is the European Union (EU) project revealed on December 1, 2021, which promises €300 billion ($340 billion) in infrastructure investments between 2021 and 2027. The EU plans to leverage resources from European financial institutions, development banks, and member states. Prior to these initiatives, the Japanese government promoted its PQI from 2015 under Prime Minister Abe to beef up investment in 'quality' infrastructure through partnership with the private sector (discussed below).

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mobilizing $600 billion in the next 5 years.[2] While some may expect the ongoing war in Ukraine to divert the G7 members' attention toward security and away from infrastructure, it was clear that the war has not quelled their interest in the topic. In the post-COVID world, this is one way to kick-start the global economy suffering from massive economic dislocation from supply chain disruptions to export contraction. It is important, nonetheless, to acknowledge that this new wave of interest on the part of capital-rich world in infrastructure development has dated back, at least, to the global recession of the late 2000s, where the previous model of investments into financial instruments such as mortgage-backed securities and collateralized debt obligations collapsed.[3]

Of course, on the side of China, President Xi Jinping has been very active in utilizing infrastructure investment and exports as the country's national geoeconomic strategy. As the Chinese authority launched the BRI in 2013, they also established two new regional multilateral development banks, Asian Infrastructure Investment Bank (AIIB) and New Development Bank (NDB) in the first half of the 2010s. As discussed below, a part of the motivation behind this initiative was to manage China's excess capacity problem, particularly in the aftermath of the massive economic stimulus during the global financial crisis a few years earlier. With an already estimated $1 trillion funding for physical infrastructure invested in regions from Asia to the Middle East and Eurasia to Africa, China's infrastructure power and presence in this issue area have vastly expanded.

In contrast, Japan's "quality infrastructure" aims at building infrastructure "that might look expensive in the onset, but it is easy to use, durable, environmentally sustainable, resilient against disasters, and will end up being economical in the long run."[4] Of course, such emphasis is a way for Japan to intentionally contrast with China's vast infrastructure investment at a cheaper cost, which can often be of low quality with little social and environmental consideration. In the background, nonetheless, the interest on the part of capital-rich countries (other than China) in infrastructure investment actually has a similar recent history of "savings-," "banking-," or "portfolio-glut" emerging in the twenty-first century that became exacerbated in the aftermath of the global financial crisis.[5] There were already efforts to connect the financialization of domestic economies with infrastructure investment as early as the immediate aftermath of the global financial crisis. In the early 2010s, even prior to the BRI announcements, the United National Development Program (UNDP) was exploring "de-risking" of renewable energy investment. Private

[2] On PGII, see FACT SHEET: President Biden and G7 Leaders Formally Launch the Partnership for Global Infrastructure and Investment, June 26, 2022. (https://www.whitehouse.gov/briefing-room/statements-releases/2022/06/26/fact-sheet-president-biden-and-g7-leaders-formally-launch-the-partnership-for-global-infrastructure-and-investment/)

[3] For good discussion of the financial foundation of the global financial crisis, see Wolf 2014 or Roubini and Mihm 2010.

[4] Kanda 2015, p. 11. Translation by the author.

[5] Shin 2012; Arezki et al. 2017.

financiers also began to focus on infrastructure as an asset class to invest in.[6] For example, Deutsche Bank Asset Management already identified a good match between the type of available funding and infrastructure investment. Its report stated that "the cash flows of infrastructure assets with inherently long lives and strong intrinsic value, can provide a good match for the long-term liabilities of certain investors, such as pension funds for example."[7]

The infrastructure "competition" in the Global South that takes place between China's BRI and OECD financials occurs within a broader global financial context. In Asia, scholars have analyzed these dynamics in terms of China's geopolitical ambition and the China-Japan rivalry to cultivate regional leadership.[8] In existent work, the issue of "quality infrastructure" is a way for Japan (or the United States) to differentiate itself from China's geoeconomic strategy. It is vital to note, however, that this contrasting approach to infrastructure has another important dimension, which is the financial foundation that can advantage or constrain governments' geoeconomic strategy. The competition between the big push (quantity) strategy of China and the quality strategy of Japan and the United States (plus Australia) on infrastructure investment constitutes a fundamental geoeconomic race in the Indo-Pacific. As I argue below, "quality" is fundamentally important for Japan to raise private funds and to compete against China, based on distinct funding structures and mechanisms of infrastructure investments and loans between these two camps.

Following this introduction, the second section of this chapter outlines the rise of development financing of infrastructure investment in the context of the post-2008 challenge. The role of capitalist governments in such context was to de-risk vast infrastructure investments and to make these infrastructure projects "investable" or "bankable." The third section contrasts infrastructure investment dynamics especially between China and Japan in the twenty-first century. The fourth section focuses on the financing side of infrastructure exports and examines how and why the competition between the "big push" by China and bankability by the OECD nations is rooted in the political economy of financing these infrastructure investments between the two camps. In the conclusion, the chapter suggests the implications of the financial foundation of big push versus bankability in infrastructure investment on China, Japan, and the countries receiving such investment.

2 Infrastructure Investment, Development Finance, and De-Risking

Physical infrastructure covering areas from transportation, energy, and communication to water supply has been of vital necessity for economic development and industrialization. Economists have long advocated for infrastructure investment,

[6] For discussion on the recent "infrastructure as an asset class" movement, see Inderset (2010) and Andonov et al. (2018).

[7] Deutsche Bank Asset Management 2017

[8] Beeson 2018; Wang 2016; Ye 2019; Zhao 2015

especially in the process of late industrializers' catch-up drive.[9] Infrastructure would allow developing countries to leap-frog into high growth equilibrium,[10] and such investments could reduce input costs and increase the productivity of private capital.[11] Particularly for the capital-scarce developing economies with limited domestic savings, access to foreign capital to support such investment has been crucial.[12] Nonetheless, infrastructure projects such as constructing ports and high-speed rails are risky business. Not only do these projects have a long gestation period spanning decades of planning and funding, but they also come with multitudes of potential challenges ranging from detrimental social and environmental impacts to cost overruns, corruption, mismanagement, as well as financial sustainability.[13] Experiences from the 1980s of sovereign debt crises have made investors weary of weak fiscal and governance capacity of recipient states.[14]

The international development community's response to infrastructure needs in the emerging and developing world through development financing came in the ebbs and flows.[15] Since the global financial crisis of the late 2000s, however, infrastructure investment has become one of the priorities of development so much so that the issue is now included prominent in the United Nations Sustainable Development Goals (2015–2030).[16] The significant needs and demands of infrastructure investment around the world in the next few decades have been highlighted. According to some estimates, \$94 trillion globally and \$26 trillion in Asia alone are needed for infrastructure in the next few decades.[17]

Scholars analyze this shift in the aftermath of the global financial crisis has emerged as a result of the multiple critical structural challenges of global finance. The first aspect of the challenge is the continuing financialization in the capital-rich economies where "a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production."[18] With the end of the housing boom and the souring of mortgage-backed securities in the late 2000s, the wealth-seeking energy of "share-holder" and "rentier" economy under "secular stagnation"[19] has been in search of profitable investment in development. This condition has created what Gabor calls the "Wall Street Consensus" where the institutional mechanisms of the state are reoriented toward protecting the

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9 Rosenstein-Rodan 1943, Hirschman 1958, Gerschenkron 1962

10 Agénor 2010

11 Hirschman 1958

12 The famous "two-gap" model of economic development. Cheney and Strout 1966, for example

13 For the variety of risks in infrastructure investment, see OECD (2015).

14 Reinhart et al. 2016

15 For example, Wood 1986; Humphrey 2015

16 Mawdsley et al. 2014

17 \$94 trillion between 2017 and 2040. Source: Global Infrastructure Outlook, Global Infrastructure Hub (https://outlook.gihub.org/). \$26 trillion over 2016–2030. Source, ADB. Asian Development Bank, "Meeting Asia's Infrastructure Needs," ADB Manila, Philippines, 2017

18 Krippner 2005, 174

19 Summers 2016

political order of financial capitalism.[20] With this supply condition, the above-mentioned high demand for infrastructure development has led to the "financialization of development" where development projects are turned into assets to invest, and investment into such assets is considered "development finance" consisting not only of governments' funding but also private capital.[21]

The second and related challenge comes in the form of "de-risking" such investment in the financialization-development nexus, as more than half of the projects in the developing world are not investable from the institutional investors' perspective.[22] The role of the state becomes critical in this de-risking process. For the states and international entities such as multilateral development banks (MDBs), the question of "how to construct investible development assets" has become imperative.[23] There are multiple types of risks involved in infrastructure projects ranging from physical and financial risks to political risks.[24] With the aim to assemble successful public-private partnerships (PPPs) for those projects, the state (the government and state entities) plays an active role in reducing these risks both in real terms and perceived. One way to do so is to provide insurance and guarantee, while another way is to be involved through either concessional or non-concessional and create "blended" financial arrangements.[25]

The third and final challenge of the changing development financing especially of large physical infrastructure projects in developing countries is how to balance strong interests among all the investing partners and host governments regarding quality and debt sustainability of these projects. As the supply of such finance leads to investor competition along with the host government's eagerness to pursue such projects, an "easy money" conundrum could lead to low quality, assessment short-cuts, and cost overrun.[26] In most cases, host government guarantees of repayments are no solution to the challenge, which could end up in severe debt sustainability problem.[27]

Facing a dire need for infrastructure investment in the Global South, on the one hand, and increasing financialization of development, on the other hand, a vital part of infrastructure competition between China and the traditional Western donors including Japan takes the form of quantity versus quality or bankability. For Japan, the PQI consists of four pillars. The first is to expand and speed up the amount of Japanese infrastructure investment by mobilizing Japan's economic cooperation tools. The second pillar is to collaborate closely with the Asian Development Bank.

[20] Gabor 2021, 431

[21] Mawdsley 2018a

[22] Gabor 2021, 435 and Inderset 2018

[23] Gabor 2021, 431

[24] There are many more types of risks including legal risk, construction risk, design risk, environmental risk, and contractual risk. For more discussion, see Inderset (2010).

[25] Mawdsley 2018a, 269, and Attridge and Engen 2019

[26] Liao and Katada 2021

[27] Oh 2018

The third focuses on increasing the supply of funding that the Japan Bank for International Cooperation (JBIC) can provide and increase Japanese business involvement in overseas infrastructure projects. The last pillar is to diffuse the quality infrastructure as the global standard so that there will be demand from developing countries to such projects.[28] In relation to infrastructure investments, there are five benchmarks of quality: "openness, transparency, economic viability, debt sustainability, and compliance with laws and regulations."[29] Meanwhile, in the last 10 years, China has implemented a vast amount of infrastructure investment where, as discussed below, all of these five values of quality are challenged. Therefore, Japan began to engage in the quality push in the face of BRI.

3 Infrastructure Investment by Japan and China: A Road to BRI and PQI in the Indo-Pacific

Infrastructure investment has been an important priority for economic development. Governments of post-war Japan and South Korea, as well as China later, all mobilized funds for domestic infrastructure investments that helped contribute to their impressive growth.[30] Along with export promotion, their respective governments channeled the countries' robust domestic savings into infrastructure investment. For both Japan and China, their economic maturity, accumulating foreign reserves, and the saturation of domestic investment, along with search for natural resource access, became the impetus for expanding their respective overseas infrastructure investments.

Japan launched its overseas infrastructure investment as soon as the Japanese government began its foreign aid program in the form of war reparations to Southeast Asia in the mid-1950s.[31] Japan's foreign investment and loans including ones for infrastructure began expanding rapidly as Japan became a surplus country in the 1970s, particularly in the search for access to energy and natural resources. Japan

[28] Kanda 2015, p. 13

[29] The JBIC highlighted these five issues in the Memorandum of Understanding signed with the Chinese Development bank in October 2018 (https://www.jbic.go.jp/en/information/press/press-2018/1026-011525.html). Also this point is raised in my interview with a JBIC official on April 12, 2022.

[30] Perkins 2013. In general, the amount and the pace of infrastructure investment tend to slow down after a country reaches certain level of developments. For example, most of the Organisation for Economic Co-operation and Development (OECD) countries, whose ratio of public investment to GDP was 4–5 percent in the early 1970s, saw this ratio significantly decline to around 2 percent in the 1990s. Both Japan and China, however, have maintained relatively high infrastructure spending in their policy planning (Mody 1997), where Japan's ratio stayed above 5 percent in the 2000s (Kohsaka 2007) and China on average invested 8 percent of its GDP into infrastructure into the early 2000s (Thanh and Dapice 2007).

[31] The first project was Balu Chaung Hydro Power Plant constructed in Burma that was completed in 1960 (Fujikawa and Nakayama 2016, 43).

became the largest infrastructure investor in East Asia in the 1980s and became the world's largest foreign aid donor in 1989.[32] One of the major characteristics of Japan's development financing during this period was its heavy focus on "economic infrastructure,"[33] based on the "trinity approach" to development capitalizing on the synergy among trade, investment, and foreign aid.[34] During this period, Japan's de-risking strategy was to use public funding and collaborate closely with the Japanese private firms along with the recipient governments based on their repayment guarantees. This was an extension of the public works model that Japan used to conduct domestically that reduced the risk to the private sector.[35]

By the 1990s, however, the Japanese government's support for infrastructure investment through foreign aid weakened due to a strong push to eliminate tied aid, which partly targeted Japan as the actor distorting healthy competition in overseas infrastructure investments. Budget pressure arising from Japan's worsening national fiscal position further contributed to this decline. Throughout the 2000s, the Ministry of International Trade and Industry (until 2001 and later the Ministry of Economy, Trade, and Industry) promoted cost and risk sharing between the public and private sectors in infrastructure building to little avail.[36] Despite increased demands for infrastructure investment, globally and especially in Asia, overseas infrastructure exports by Japanese firms stagnated in the 2000s at around $20 billion annually from 2005 into 2011. It also faced harsher business competition from rising Asian economies, as infrastructure exports from South Korea increased by three times (from $20 billion to $60 billion) and China's increased even more dramatically with 700% growth (from less than $20 billion to $140 billion) during this same timeframe.[37] As discussed below, the Japanese government launched a new round of infrastructure export strategy utilizing ODA along with private investment as a part of the economic recovery strategy in the aftermath of the global financial crisis in the late 2000s.[38]

China clearly took the lead in the recent round of infrastructure investment boom in the twenty-first century. In 2013, China's newly inaugurated leader Xi Jinping launched the BRI, whose infrastructure projects are designed to deepen economic connectivity between China and regions to its west through land and maritime channels. Heavy infrastructure investment has also catered to China's domestic imperatives of managing excess capacity and vested economic interests of state-owned

[32] Solis 2004; Arase 1995

[33] In comparison to other aid donors, the Japanese aid in the 1980s was highly concentrated in economic infrastructure at the rate of 40 percent, while the average among the DAC donors was 15.7 percent (Watanabe and Miura 2003, 39–40).

[34] Fukuda-Parr and Shiga 2016

[35] Interview with a JBIC official, April 12, 2022

[36] Report from the Study Group on Asian PPP (METI 2006, 17). Translation by the author

[37] Cited in Ezaki (2016, 22). Data by the Japan Machine Center for Trade and Investment, which take semi-annual survey of over 100 companies (reports can be accessed at http://www.jmcti.org/planthomepage/)

[38] Yamamoto 2015

enterprises (SOEs).[39] In addition, 6 years since its official establishment of January 2016, the AIIB has emerged as a solid multilateral development bank with 191 infrastructure investment projects approved (as of October 27, 2022) and a triple-A credit rating given by the big-three Western credit rating agencies. The AIIB has attracted the participation of 105 countries as of October 2022, although Japan and the United States have not joined.

China's economic strategy offers a seemingly viable alternative to revitalizing economies of the least developed countries through infrastructure development[40] and challenges the influence of economic neoliberalism. China's "big push" approach, which gives China an economic edge through the promotion of investment and economic connectivity around the region, nonetheless, presents host countries a mixed blessing. On the one hand, it has given recipient countries easier access to infrastructure financing as in the cases of high-speed rail sales competition in Southeast Asia. On the other hand, problems such as poor assessment and planning, durability, and debt sustainability raise concerns.[41] Furthermore, some countries have begun facing mounting debts to China's infrastructure loans, leading many to blame China's "debt trap diplomacy."[42]

China's massive infrastructure push energized Japan's infrastructure export promotion that had already taken place quietly along with the global trend of financialization-development nexus and as a part of the country's growth strategy in the twenty-first century. In 2015, Prime Minister Abe officially announced a plan to meet the huge demand for such investment in Asia through PQI. The Japanese government and the Asian Development Bank pledged $110 billion in infrastructure support for Asia over 5 years through this imitative. In 2016, the Japanese government also announced the "Expanded Partnership for Quality Infrastructure" at the Ise-Shima G7 summit promising to expand the investment to $200 billion. Finally, and as discussed above, at the G20 Summit in Osaka in June 2019, Japan advocated the "G20 Principles for Quality Infrastructure Investment" and received support from all participating leaders. Japan has called for high-quality infrastructure support to be disbursed through its high technical ability and quality as well as infrastructure expertise. Furthermore, the Japanese government collaborated with India to launch the Asia Africa Growth Corridor Initiative to strengthen economic partnerships with the Middle East and Africa and to limit China's advance into the Indian Ocean.[43]

Following Japan, the US government began to beef up its efforts in the Indo-Pacific infrastructure investment as a pillar of the US's FOIP strategy after President

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[39] Liao and Katada 2022; Ye 2019

[40] Terada 2018

[41] Jiang 2019; Liao and Katada 2021

[42] The reality of China intentionally trapping these countries into debt is also widely questioned. Singh (2021) evaluated that China's debt trap diplomacy is the narrative led largely by the United States to discredit China and that there is no evidence of China's predatory behavior in Africa or Latin America. Brautigam (2020) and her team have also argued that "debt trap" by China is a myth.

[43] Blah 2018; Ito 2018

Trump's speech at the 2017 APEC Summit in Vietnam. Since then, the US Congress passed the "Better Utilization of Investments Leading to Development (BUILD)" Act in 2018, which converted the outdated Overseas Private Investment Corporation (OPIC) into a newly established US International Development Finance Corporation (DFC). The new corporation is modelled after JBIC where it can now extend funding to middle- to high-income countries with some level of political risk, as long as the funding is in line with the US foreign policy and security objectives and supports private sector funding.[44] A total of $60 billion DFC infrastructure investment fund was twice the limit of the OPIC years. Furthermore, in support of quality infrastructure and in the effort to channel private funding to these investment needs, the US State Department led the negotiation to establish Blue Dot Network in November 2019 in the context of the FOIP. Quoted as "a multi-stakeholder initiative to bring together governments, the private sector and civil society to promote high-quality, trusted standards for global infrastructure development," this network provides its "seal of approval" to certify infrastructure that meets its quality, sustainability, and "bankability" standards.[45] Following these initiatives, the G7 Cornwall summit in 2021 emphasized the importance of quality infrastructure investment. In order to realize the Blue Dot Network's mission, the OECD is now involved in setting up a global certification framework for quality infrastructure.[46]

Geoeconomic competition in the Indo-Pacific over infrastructure investment has thus far taken the form of China's "big push" investment strategy versus Japan-US response highlighting quality infrastructure. Bankability associated with the quality of infrastructure constitutes a focal point for the FOIP countries due to the different financing structures of infrastructure investment from China. The contrasting financing features and risk consideration of infrastructure investment between these rivals dictate the type of geoeconomic instruments these major powers can use in this competition.

4 Economics and Politics of Infrastructure Funding

Quality standard to make projects bankable is a crucial part of de-risking infrastructure investment for traditional creditor/donor governments that seek to involve the private sector and private finance. Private investors are averse to investing in infrastructure projects when facing a region whose governments, in their views, continue to have "weak legal and regulatory frameworks" and "poorly structured and prepared projects."[47] The repercussion of political opportunism is, as history shows,

[44] Interview with a JBIC official on April 11, 2022

[45] Rajah 2020

[46] OECD, "OECD and the Blue Dot Network," 21 March, 2022. https://www.oecd.org/corporate/oecd-and-the-blue-dot-network.htm

[47] PricewaterhouseCoopers. Developing Infrastructure in Asia Pacific: Outlook, Challenges and Solutions, May 2014, p. 11–15. http://www.pwc.com/sg/en/capital-projects-infrastructure/assets/cpi-develop-infrastructure-in-ap-201405.pdf. See also Lessambo (2022)'s chapter on bankability.

that this state-backed capital is misspent, if not altogether embezzled.[48] Some practitioners even argue, "the issue is not a shortage of funding, but rather how these countries produce only a limited number of bankable projects that banks are willing to finance." Essentially, western governments of free-market economies cannot even imagine competing effectively in expanding the amount of infrastructure projects when developing regions "produce so few bankable projects that U.S. [and other western] banks are willing to finance."[49]

Funding China's BRI

How is China different? China's "big push" infrastructure funding skyrocketed in the first two decades of the twenty-first century. By 2019, prior to the onset of the COVID-19 pandemics, Chinese financial institutions, China Development Bank (CDB) and Export-Import Bank of China (ChEXIM), the main vehicles of overseas infrastructure investments, have provided more financing to emerging and developing countries than all the MDBs combined.[50] As of 2018, the total assets of CDB stood at 16.2 trillion RMB (US$2.5 trillion) and ChEXIM Bank 4.2 trillion RMB (US$610 billion), which eclipse any policy banks from the OECD countries (KfW from Germany, JBIC from Japan, Export-Import Bank or DFC from the United States) whose assets are in the range of hundreds of billions of dollars.[51] Beyond the sheer size, many critics argue that Chinese infrastructure financing has adopted lax rules—slack due diligence, flexible socio-environmental standards, and no political or fiscal conditions—to make its programs more accessible to borrowing countries.[52] Granted that it is the case, Chinese finance covers infrastructure projects that most other creditors, both the public and private, stay away from due to concerns of high risk. In such sense, the emergence of China as a creditor has facilitated South-South development.[53]

There are several mechanisms that make China's two large policy banks the key to China's infrastructure investment expansion around the world particularly in the least developed regions where no other donors/creditors would (or could). First, although these banks are self-funded, they raise their funds from the market through issuing bonds that are purchased by China's state-owned commercial banks. These banks are owned and controlled by the Chinese state (i.e., SOEs) and receive budgetary transfers from China's Ministry of Finance in exchange for providing

[48] Moser 2016

[49] Cochrane 2016

[50] Chin and Gallagher 2019, 246

[51] Chen 2021, Figure 2

[52] Woods 2008

[53] Mawdsley 2018b; Lin and Wang 2016. In general and by contributing infrastructure funding to regions such as Africa, China's expanding finance works to fill the investment gap rather than undermining the effectiveness of Western assistance (Dreher et al. 2021).

financial support for firms and projects that advance China's national policy objectives.[54] For example, CDB and ChEXIM Bank received $93 billion worth of cash injection in 2015.[55] Hence, although these banks care about their commercial bottom line, they can take higher risks on their loans to foreign entities.

Second, these banks can provide loans directly to developing country governments and local governments, which are most often the owners of projects, so that these hard-currency strapped governments can pay for projects leading to Chinese construction companies winning their bids.[56] Meanwhile, these banks can also choose to transfer no money to recipient governments by disbursing loans directly to Chinese contractor firms that implement the projects.[57] Vendor financing (or supplier credit) in support of Chinese companies exporting items to the recipient countries is common in China's funding.

Third, these banks tend to charge high interest rates to make projects commercially viable. Unlike foreign aid (ODA) by traditional donors, majority of whose funding comes from government sources, the majority of funds of these two Chinese banks are raised via sovereign-guaranteed bond issuance. The interest rates on CDB and ChEXIM lending average are based on London Interbank Offer Rate (LIBOR) which fluctuates, and then these banks add 1 to 4 percent depending on the level of risk.[58]

Finally, these policy banks implement various ways to guarantee repayments. Firms can choose to use China's state-owned insurance agency, Sinosure (China Export & Credit Insurance Corporation), to cover the losses or use their own assets as guarantees to acquire bank loans. In addition, investments require project owners to guarantee repayment based on their future revenues. Particularly in relations to loans to resource-rich regions of Africa and Latin America, it is common for these banks to extend "commodity-backed" or "resource-secured" finance to secure repayments.[59] This last method allows the host government to use its natural resources as collateral and commit foreign exchange income from their future exports as a source of the government's repayments.[60]

So far, the Chinese authority has been able to increase the risk tolerance of the infrastructure investment due to these financial characteristics. China's methods of securing funding for these overseas investments are being tested, however, as many borrowers face economic contraction. Geoeconomic competition in infrastructure investment has already caused an overextension of public sector indebtedness within the emerging and developing countries, and the Chinese authority is

[54] Reilly 2021, 43; Hopewell 2020, 143.

[55] Kong and Gallagher 2017

[56] Chen 2021

[57] Horn et al. 2019, 9

[58] For Details, see Gelpern et al. 2021.

[59] Estimated 50% of China's infrastructure loans to these regions are covered by this arrangement (Brautigam and Gallagher 2014).

[60] Chen 2021; Brautigam and Gallagher 2014

reforming their lending practices in response to global pressure. As emerging and developing Asia faces COVID-19 economic slowdown, infrastructure developments have become the immediate liability in the form of debt exposure. Given the opaque nature of China's financing, there is a continued debate over the massive debt masked by China. Some argue that Chinese lending comes with senior debtor demands and control over the loan terms to influence the borrower's actions,[61] while others point to China's willingness to reschedule and refinance (but not cancel) its loans.[62] Nonetheless, since the onset of pandemic-induced debt crisis, China has responded to the calls for debt relief by participating in the G20-led Debt Service Suspension Initiative (DSSI) to temporary suspend debt-repayment from 77 low-income countries.[63] The Chinese government, though not a member of the Paris Club of official creditor governments, signed onto the G20 Ministers and Governors' "Common Framework for Debt Treatment beyond DSSI" toward debt relief in November 2020.[64] With these challenges, the funding advantage on the part of China might be at a cross-road.

Transformation of Japan's Infrastructure Financing

With these financing methods, Chinese infrastructure funding expanded into high-risk regions and funding projects with low commercial viability. This approach was actually modeled after the public financing structure of Japan's developmentalist past. Seventy years ago, Japan's domestic political and institutional context heavily shaped the government's infrastructure investment strategy. Japan's postwar public financing started with the Japan Export-Import Bank (JEXIM Bank) established in 1950[65] for largely implementing export credit scheme. The Overseas Economic Cooperation Fund (OECF) was established in 1960 to manage Japan's war reparation payments and later the concessional yen loans.[66] During the earlier years, JEXIM Bank implemented OECF loans, and the blending of and overlapping between the two institutions and the use of concessional loans in support of Japanese firms' exports, overseas expansion, and infrastructure financing represented Japan's

[61] Gerlpern et al. 2021

[62] Acker et al. 2020, and updates by Horn et al. 2022

[63] The original term of the debt suspension was from May through December of 2020, which has since then extended till the end of 2021.

[64] Chad, Ethiopia, and Zambia formally requested debt relief under this Common Framework (Rieffel 2021). China also agreed to provide a 2-year debt moratorium to Sri Lank in January 2023.

[65] Japan Export-Import Bank originally started with the name "Japan Export Bank" in 1950, and "import" bank function, and hence the title, was added in 1952.

[66] Lancaster 2007, 113–114. Meanwhile, Overseas Technical Cooperation Agency (later renamed to Japan International Cooperation Agency, JICA) was established in 1961 to implement grant aid as well as technical training and assistance.

mercantilist "catch-up" strategy in support of Japanese businesses.[67] This blending was a particularly important innovation for Japan where "neither domestic corporations nor commercial banks had the capital to finance riskier investment projects abroad."[68] Later, these two institutions were temporarily merged in 1999 into the Japan Bank for International Cooperation (JBIC) in the context of Japan's administrative reform with clear demarcation between the two functions. Then finally the Japanese government officially separated these two functions as the concessional loan function was transferred from the JBIC to New JICA in 2008.[69]

Japanese public financing policies have transformed from its original developmentalist model of government's support to one based on market discipline through the 1990s. The first reason comes from Japan's membership in the OECD, which pressured Japan to respond to the organization's evolving norms. Over the course of 20 years from the late 1970s through the 1990s, the Arrangement on Officially Supported Export Credits at the OECD, which governs standards and rules on tied aid as well as the terms of export financing, developed such norms. The current arrangement mandates the members on minimum interest rates, minimum premium rate to cover credit risk, loan payment period, and a grace period to 85% maximum support for export contracts.[70] Furthermore, the OECD/DAC has instituted the 1991 Helsinki discipline that restricts tied aid practices for commercially viable projects.[71] These rules and peer pressure from the Western donors have influenced Japanese infrastructure lending practices, and in response, Japan's tied aid, which used to be up to 40% of Japan's foreign aid (and this amount gets higher if we include partial tied and developing country tied), declined significantly to virtually zero by the first half of the 1990s (Fig. 1).

Second, along with declining tied aid and government support to infrastructure exports, the Japanese firms began losing their competitiveness. A part of the loss came from Japan's high cost. In most instances, Japanese businesses are outbid by firms from emerging economies, and Japan has not yet managed to utilize non-Japanese and/or local firms as partners to reduce costs.[72] An additional factor is a lack of management capacity to oversee the entirety of large infrastructure projects in a one-stop shop fashion due to a fragmentation of operations among many Japanese entities, particularly in mega-projects involving the public sector. The

67 Solis 2004; Chen 2021

68 Solis 2004, 84

69 Tsunekawa 2014

70 Hopewell 2020 and Hopewell 2021

71 Hall 2011

72 That is the case for Japanese companies' competitiveness in bidding to win projects funded by the Asian Development Bank. Japan's procurement rate of the ADB-funded projects has hovered around 0.5 percent in the mid-2010s compared to 50 percent by the companies from China and India combined.

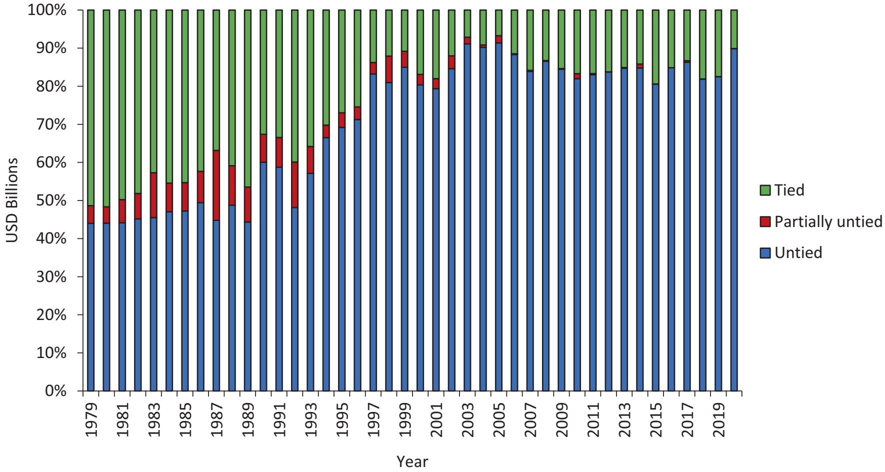

Fig. 1 Proportional change of Japan's tied aid from 1979 to 2020. (Source: OECD, "Aid (ODA) Tying Status." https://stats.oecd.org/viewhtml.aspx?datasetcode=TABLE7B&lang=en#)

Japanese firms were also concerned about the obvious lack of contractual and legal structure in most developing countries where they operate.[73]

Most prominently, Japanese businesses' high sensitivity to financial risks associated with infrastructure projects has stunted expansion of Japan's infrastructure investments. Japanese firms have robust expertise in the "Engineering, Procurement, Construction (EPC)" scheme, for which they have established well-identified parameters and limited operational and financial responsibility to effectively reduce uncertainty and risk in investment. The support of both the host and Japanese governments has also been an indispensable part of reducing the risk of large and long-term projects. In recent years, nonetheless, emerging and developing governments themselves have started to count on private markets to raise investment and operate their infrastructure projects with limited reliance on government guarantees. Many infrastructure projects in emerging Asian economies come in the form of "concessions," where private firms take responsibility not only for the operation and maintenance of the invested assets but also for financing and managing of all required investments. These firms hence take risks for the condition of the assets and for investment.[74] Japanese businesses, however, are not used to such a scheme and consider this scheme's associated risks to be too high.[75]

[73] For more analysis with the case of electronic sector, see Ezaki (2013). These three points are raised by Hideo Naito, the Director of Infrastructure and Environment Finance Department of the JBIC (https://www.jbic.go.jp/ja/about/surrounding/infra)

[74] Note explaining the concept on the World Bank website on "Public-Private Partnership in Infrastructure Resource Center" (https://ppp.worldbank.org/public-private-partnership/agreements/concessions-bots-dbos)

[75] Ezaki 2016, 23

The Japanese government, in its strategy to revive Japan's standing in infrastructure exports and use it for the country's growth strategy, began to formulate modalities to tackle these challenges. But simply reviving Japan's old infrastructure investment practice of the 1970s–1980s was not an option for the Japanese government given the country's economic maturity and transformation since then.[76] On the one hand, Japanese businesses have become more powerful and financially resourceful. The case in point, in 2019, 78% of gross financial flows to developing regions from Japan is from private sources, while the remaining comes from the public sources.[77] On the other hand, through the lost decades since the early 1990s, the Japanese government's fiscal position has drastically deteriorated, which makes infrastructure subsidization much more difficult. Furthermore, the Fiscal Investment and Loan Program (FILP) reform in the late 1990s led a large bulk of capital for concessional and non-concessional yen loans to be exposed to more stringent market discipline.[78] Rapidly changing norms of export credit and public funding under China's aggressive infrastructure investment in the twenty-first century[79] have triggered the Japanese government to take several measures balancing its use of government tools with its reliance on private sector and its financial resources. In such a process, nonetheless, market discipline and risk calculations became paramount considerations.[80]

First, METI began to proactively adopt its own version of PPP modality to Asia's infrastructure development in the aftermath of the Asian Financial Crisis (1997–1998).[81] With the 1999 Act on Promotion of Private Finance Initiatives (PFI), the Japanese government began to promote a "Japan package" modality where the Japanese government would engage in planning with aid recipient governments to provide a package-type aid (with increased tied aid). The package includes everything from identifying possible infrastructure projects and public and private financing to construction and maintenance. After the global financial crisis (2008–2009), the Japanese government began to further emphasize infrastructure investment as a part of Japan's economic growth strategy and installed "Ministers' Conference related to Package-type Infrastructure Overseas Operation" in December 2010 under the Democratic Party of Japan government. The Act on Promotion of PFI was

[76] Katada 2020

[77] Ministry of Finance. "2019 nen ni okeru Nihon no Kaihatsu tojokoku ni taisuru shikin no nagare." https://www.mof.go.jp/international_policy/reference/financial_flows_to_developing_countries/2019.html

[78] Zenkoku Ginko Kyokai 'Zaisei seiyaku kano kouteki kinyu minkan kinyu no yakurawi buntan to shakai shihon seibi no okeru minkan shikin tou no katsuyou' February 13, 2013. (https://www.zenginkyo.or.jp/news/2013/n3263/)

[79] Hopewell 2020

[80] These risks include future income uncertainty, financial and currency mismatch, as well as political and financial risks (Nishizawa 2018).

[81] METI defines PPP as "the division of labor between the public and private in infrastructure building and administrative services, as the two entities share adequate cost and risk."

amended in 2011 to increase the coverage of PFI projects and financial use of private capital to improve public infrastructure.

Second, from the public funding side, two institutions, JBIC and JICA, have continued to play important funding roles, and their frequent restructuring demonstrates the Japanese government's efforts to achieve a right balance between the state-led efforts and market imperative of infrastructure investment. The JICA's foreign aid modality shifted as the practice of tied aid was (re)introduced under the New Miyazawa Initiative in 1998 in response to the Asian financial crisis, and the modality was renewed in the form of the Special Terms for Economic Partnership (STEP) in 2002. This was aimed at allowing Japanese businesses to enhance procurement in specific areas of infrastructure building.[82]

JBIC also became the principal institution for the infrastructure export push starting with the expansion of its investment finance accessible to Japanese firms' projects in developing countries in December 2010.[83] In 2011 at the time of dramatic yen appreciation, the Japanese government channeled the US dollars from the country's foreign exchange reserves to support Japanese businesses to conduct M&A and invest in energy resources. In addition, JBIC provides stepped-up financing (two-step loans) to Japanese private banks so that they can extend loans to Japanese businesses operating abroad. In April 2012, JBIC became independent from the Japan Finance Cooperation as a special company under 100% government funding.

Finally, during Prime Minister Abe's second term (December 2012–September 2020), as discussed above, infrastructure exports, particularly in the context of the FOIP, became a major pillar of Japan's growth strategy. In the context of PQI in 2015–2016, the new JBIC law (passed on May 11, 2016) has enhanced the bank's risk tolerance by allowing multi-project assessment (rather than single-project), setting up ¥200 billion (US$2 billion) special account in support of Japan's infrastructure investment, expanding JBIC's repayment terms, allowing a local government (sub-sovereign) to be the owners of projects as well as allowing loans in the local currency.[84] Although the amount is still small, JBIC can also participate in equity for projects, as well as provide JBIC guarantees. Meanwhile, JBIC untied loans to support overseas projects, in general, contracted significantly during this period (Fig. 2). Furthermore, JICA has further expanded its ODA channels for funding Japanese businesses abroad. New facilities to encourage Japanese firms' participation in

[82] METI 2006

[83] The legal change in March 2010 allowed the JBIC to fund environmental projects. In 2021, the JBIC announced its Environmental, Social, and Governance (ESG) funding strategy (https://www.jbic.go.jp/ja/information/press/press-2021/1028-015365.htm)

[84] "Risuku toshiwaku ni 2000 okuen" Nihon Keizai shimbun, May 11, 2016. Also interviews with JBIC officials on April 11 and May 10, 2022.

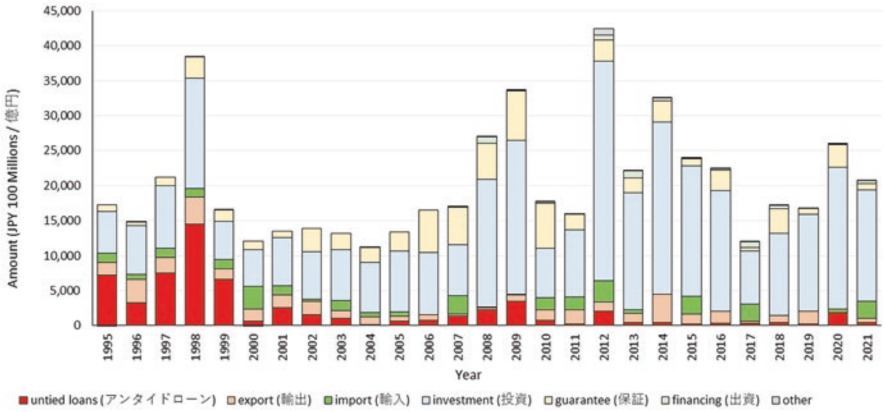

Fig. 2 Amount and allocation of type of JBIC financing (2000–2021) (Source: JBIC Annual Reports, https://www.jbic.go.jp/ja/information/annual-report.html).

infrastructure projects are established in the forms of Equity Back Finance (EBF) loans and Viability Gap funding (VGF) loans.[85]

Quality Cum Bankability

All these changes within Japan's public financing modality have led some scholars to argue the "resurgence of the Japan model"[86] in infrastructure financing within the context of loosening OECD public financing norms and Japan's geoeconomic competition vis-à-vis China. The emphasis on infrastructure quality demonstrates, however, that this is not the case. It is because a market-based economy like that of Japan faces major constraints when it comes to infrastructure financing competition, as they must rely largely on market assessment and private financing to expand these investments.

Hence, the pursuit of quality in infrastructure investment translates directly to the question of bankability.[87] Bankability means how to draw in private finance and investment. As stated by the 2022 OECD announcement of its support to the Blue Dot Network, "the current flows of private capital into infrastructure investment are

[85] Kanda 2014; Kratz and Pavlicevic 2019. EBF supports developing country governments and SOEs as their capital subscription as they start infrastructure projects in the areas of electricity, water, and transportation. VGF supports infrastructure projects where Japanese businesses are already invested in by providing funding when commercially based finance is difficult. Both mechanisms are untied.

[86] Sasada 2019

[87] Interview with a JBIC Official, June 2, 2022

insufficient."[88] For these creditor governments, the question of how to encourage private sector participation has become the most important component of the quality infrastructure. Although there are multiple variables that go into enhancing the bankability of large infrastructure projects, several components are crucial.

The first component consists of the income-generating and repayment capacity of projects, which underlies economic viability and debt sustainability. The Japanese officials point to the historically successful case where future loan repayments were guaranteed through future income generated by the project itself. The case of electricity generation is a good model of such quality infrastructure. In most of these projects, the agreements are made at the onset of the project where future income generated by fees that users pay through electric bills would be earmarked for repayment.[89] For that, robust assessment not only of the cost of projects but also of projection of income thorough future use of electricity by the local population and fee-level as well as fee collection capacity must be calculated in advance. Such calculation gets more complicated and less reliable when it comes to transportation, especially high-speed rails, because the amount of ridership is usually difficult to estimate. Failing to complete these assessments can lead to project failures as seen in the case of Sri Lanka's Hambantota port, where the income from the use of the port fell vastly short of the costs of borrowing for its construction.[90]

Second, the quality infrastructure investment practice must stand strong under the market discipline and not solely rely on the government guarantee or insurance. Neither the home (Japan) nor the host (borrowing countries) governments would or could cover the potentially massive losses that arise when multiple infrastructure projects fail to generate enough returns, and of course, they need to avoid moral hazard on the part of private investors. The middle-income East Asian governments have hesitated to provide full government guarantee on the loan repayment (the case of the Indonesian high speed rail in point).[91] In addition, in the last few decades, the host governments want to involve their local private sector and use of local bonds to finance these projects.[92] As discussed in the earlier section, the history of the Japanese government's engagement in infrastructure projects demonstrated ways of high-level de-risking capacity from blended finance and state-firm cooperation along with the recipient governments' commitment. The traditional tied aid practices and "trinity approach" of Japanese foreign economic engagement decreased its prominence, and now openness and transparency also become the requirements for private sector involvement that would allow the project viability.

[88] OECD op. cit.

[89] Interview with a JBIC official, May 10, 2022

[90] This case is usually cited as the prime example of China's debt trap diplomacy. However, Moramudali (2020) points out that the port lease agreement itself was not in exchange for debt cancellation by the Chinese authority. It is instead a way to supplement Sri Lanka's foreign exchange income.

[91] Liao and Katada 2022

[92] Muto and Hirota 2015

Third, bankability also relies on the actors' compliance with the laws and regulations, a requirement that goes beyond the individual projects themselves. Of course, transparent bidding practices and dissemination of information about the project costs and financial profile would be a start to counter corruption and abuse of multimillion (or even billion) dollar projects. Meanwhile, both recipient and host governments must foster the national legal structure that would ensure accountability. The Japanese government began its foreign aid funded efforts in the late 1990s in support of legal development and training to "promote and facilitate further economic interaction and mutual prosperity."[93]

In sum, the pursuit of quality infrastructure is a method to entice private financing into these projects by reducing their inherent risks. Not only have the thorough pre-project preparation but also institutional supports have become essential components for such efforts.

5 Conclusion

The fundamental strength of China's geoeconomic strategy through infrastructure finance came in the form of robust financing conducted by its policy banks, which have allowed China's big push infrastructure strategy. The Japanese government has, in contrast, promoted quality and bankability of the infrastructure projects with the hope of enticing private capital and business involvement. The Japanese government's strategy illustrates a vital part of the traditional donors' post-GFC "de-risking" strategy in the name of "quality infrastructure." Its aim is to channel abundant private funding in their own financialized economies to capital-thirsty but high-risk infrastructure investment in the emerging market countries and the Global South.

As such, infrastructure competition between big push and bankability has deep global financial roots, which go beyond the geostrategic competition. The financialization of both Chinese and Western economies, including Japan, has motivated them to target infrastructure as possible sites of high-return investments. The role of the state in this regard has been to de-risk this emerging "asset class" so that the barriers to investment would be lowered for private actors and PPP. The Chinese financial structure has so far allowed massive investment by utilizing the country's excess economic capacity, both material and financial, while it has been a struggle for Japan to make infrastructure projects in the developing world squarely bankable.

The massive increase of China's presence in infrastructure investment has motivated other governments to rethink their de-risking practice. The case of the Japanese government's policy changes, ranging from the promotion of quality infrastructure to revising of the JBIC law, as well as legal training for recipient

[93] The International Civil and Commercial Law Center was founded in 1996 to implement such efforts under Japan's Ministry of Justice. The quote is from the prospectus for the establishment of ICCLC. http://www.icclc.or.jp/english/prospectus/

governments, is an illustration of new de-risking tools. Although some parts of Japan's infrastructure geo-strategy seem to revive the old Japanese practices of its trinity approach, prominent market logic is the basis of how the Japanese government works to de-risk and encourage private sector involvement.

The Chinese practices have not stayed static, either. In the face of international criticism, the Xi government emphasized the high quality and debt sustainability of the BRI projects during the second BRI summit in 2019.[94] International condemnation was not the only or even the major reason behind such shift, nonetheless. The challenge of debt sustainability applies not only to borrowers but also to creditors. Despite the robust government support to channel financial resources to these infrastructure projects around the Global South, how long and how much loss China can sustain is an important future question. Alongside the COVID-shock, Chinese practitioners are doing some rethinking, and it is slowing and/or changing China's infrastructure investment in the last few years.[95]

Furthermore, with concerns over long-term costs and political consequences of investment overdependence on China, borrower governments, especially around Asia, are also thinking twice about the initial attraction of the BRI. Easy money has led to moral hazard and misguided decisions in the past, and there is a differentiated response to the big push infrastructure investment among borrowers these days.

The current "Wall Street Consensus"[96] will continue to call for de-risking efforts even at the time when the post-COVID debt sustainability challenge looms large among developing and emerging economies. Future research needs to inevitably focus not only on debt sustainability but also on the boom-and-bust cycle of infrastructure investment and the possible repercussions of the governments' role in de-risking what is inherently complex and long-term investment needs.

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[94] Xi's speech at the start of the second Belt-and-Road summit in April 2019 emphasized "open, green and clean" projects with commercial and financial sustainability. https://www.dw.com/en/chinas-belt-and-road-is-green-and-clean-says-xi/a-48495226

[95] For example, recommendations by the Advisory Council of the Belt and Road Forum for International Cooperation on "high quality belt and road cooperation" (https://www.google.com/url?sa=i&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=0CAMQw7AJahcKEwjIi4ytvYX7AhUAAAAAHQAAAAAQAg&url=https%3A%2F%2Fwww.fmprc.gov.cn%2Fmfa_eng%2Fwjbxw%2F202112%2FP020211218394332617729.pdf&psig=AOvVaw2srZ9aEfedid0Qd7kUS-gt&ust=1667133561603295)

[96] Gabor 2021

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Geo-economics of the Chinese Shipping Industry: Building Maritime Commercial Power from Bust to Boom, 2008–2021

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1 Introduction: A Tale of Divergent Crisis Responses

Containerization has been the single most important driver of globalization since the 1970s, with an impact greater than all the trade liberalization agreements combined.[1] In the first two decades of the twenty-first century, container ships have carried approximately 90 percent of globally traded goods. In 2020, the COVID-19 pandemic knocked some 1 billion tons of sea trade off the previous years' total volume of 12 billion tons.[2] Looking back, in the aftermath of the 2007–2009 global financial crisis, major carriers lost around $20 billion in 2009.[3] Chinese shippers lost around $900 million in the period 2009–2014. The COVID-19 pandemic presented similar supply, demand, and distribution shocks, yet this time around carriers "made a killing," particularly from the onset of the pandemic to the end of 2022.[4] The nine largest container carriers tripled earnings in 2020.[5] The leading carrier, Maersk, posted net profits of $2.9 billion in 2020, $18 billion in 2021, and $29.3

[1] The Economist Newspaper 2013

[2] Ibid.

[3] Notteboom et al. 2021, pp. 179–210

[4] The Economist Newspaper 2020a, b

[5] Holmstad 2021; Wackett 2021

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billion in 2022.[6] China's national champion, China Ocean Shipping Companys (COSCO), saw a net income of $1.47 billion in 2020, a 51 percent increase over the 2019 level.[7] This came on top of 2 years of government subsidies to COSCO of $358 million in 2018 and $1.03 billion in 2019 which followed a decade of single-digit billion-dollar annual earnings or losses from 2008 to 2020.[8] In 2021, the company's profits rose exponentially to $16 billion, with the industry as a whole hulling in $150 billion.[9] In 2022, COSCO reported a profit of $19 billion, with the industry heading for a record-breaking $208 billion in profits.[10]

Changes in the structure of the shipping industry compounded with the responses of major firms resulted in a different outcome to the demand shock posed after the COVID-19 pandemic. The shipping industry was far more consolidated in 2020 than in 2008 – both in the number of players and the market shares of the top three shipping alliances – which allowed a degree of informal coordination that supported price hikes while the industry reallocated vessel and container capacities. While we will review this factor, this chapter focuses on a related and important development – the rising market structural position of China's leading shipping company: COSCO. For the first decade and half of the twenty-first century, Beijing struggled to grow its domestic shipping industry in the face of cut-throat competition from global carriers. From 2015 to 2018, Beijing undertook regulatory actions and asset restructuring to consolidate the container shipping industry, placing COSCO in an advantageous position in the emerging global shipping oligopoly. When the COVID-19 pandemic hit in the first quarter of 2020, instead of responding to market downturns with capacity expansion that exacerbated market pressures, COSCO adopted capacity management strategies similar to those of other carriers in the industry, which allowed the company to benefit from the advantages of an oligopolistic market. Additionally, COSCO responded to Beijing's request to prioritize China's growing exports by securing favorable rates and influencing other carriers in the Ocean Alliance, the world's largest shipping alliance. This corporate strategy proved to be resilient, and in 2020–2021, it provided an opportunity for Beijing to leverage China's export recovery for geo-economic gains against other exporting countries such as the United States, India, South Korea, and Vietnam. Instead of relying solely on strategic trade policies, China has taken advantage of the transport and logistics chains of global maritime trade to achieve similar results in protecting its trade and diverting trade. As a response, the United States should address inefficiencies in its logistics industry and work with trading partners to address major shipping alliances.

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6 Møller and Mærsk 2023

7 COSCO Shipping Holdings Co Ltd. (CICOY)

8 Shipping Tribune

9 Knowler 2022; Etter and Murray 2022

10 Port Technology Int'l 2022, 2023; Thuermer 2022; DataMar News 2023

2 Geo-economics of the Chinese Shipping Industry

China as a maritime power has come under the spotlight regularly in the public discourse over the past decade. Pundits talk about the "Pacific Age,"[11] China "ruling the waves,"[12] and the strategic notion of the "Indo-Pacific,"[13] while military analysts suggest that China is undertaking state-directed projects in shipbuilding, overseas port acquisitions, and naval and "grey zone" assertiveness in the South China Sea as part of its ambition to establish a dominant presence both commercially and militarily in Asian seas and beyond.[14] Similarly, maritime economists have tracked the rapid growth of Chinese shipping and logistics capacities, with a particular focus on Chinese coastal ports as organizationally and technologically advanced interfaces with supply chains and markets around the world.[15] Typically, industry analysts emphasize the "fundamentals" of China's manufacturing prowess, large domestic market, and rising trade dependency since the late 1990s in driving Chinese carriers and port operators to invest in transport connectivity of far-reaching destinations of the Belt and Road Initiative (BRI).[16] While they recognize the nature of Chinese shipping companies as state-owned enterprises subject to Beijing's political directives and industrial and foreign investment policies, they tend to see them as "price-takers" of global shipping market signals, with corporate objectives and strategies not dissimilar from those of Maersk and other major carriers. The annual UNCTAD Review of Maritime Transport largely follows this industry perspective in tracking market movements and aggregate capacity changes by country and carriers, chastely devoid of geopolitical analysis.[17]

This section traces major market constraints and domestic policy impacts shaping the rise of Chinese shipping companies in their initial entry into the global shipping market during a trying period of persistent excess capacity in the 2000s. In emphasizing the importance of market contingencies and collective actions of market players, we move away from the state-centric paradigm of geopolitics that tends to see successful adaptation as outcomes of economic statecraft and "weaponization" of economic interdependence by purposeful state agents.[18] In contrast, Chinese planners appeared more concerned with salvaging a domestic industry that showed lagging competitiveness and faced imminent threats of being overtaken by collusive actions of powerful multinationals. However, due to the government's involvement

[11] The Economist Newspaper 2014

[12] Kynge et al. 2017

[13] Medcalf 2012

[14] Erickson 2021a, b; O'Dea 2019

[15] See PortEconomics for an excellent online newsletter edited by Theo Notteboom of the Shanghai Maritime University and the leading shipping industry journal *Maritime Policy & Management* edited by Kevin Li of the Ocean College of Zhejiang University.

[16] Haralambides and Merk 2020

[17] United Nations Conference on Trade and Development

[18] Drezner et al. 2021

in facilitating its entry into the global shipping market, COSCO was able to strategically take advantage of the rent-seeking margins of global shipping alliances and support Beijing's trade agenda during the COVID-19 pandemic.[19]

PRC as a Maritime Commercial Power

By most measures, China has been a success story of rapid ascendency as a shipping power. By 2019, the country had possessed the world's biggest container ship fleet, amassed the second largest dead-weight tonnage, became the biggest shipbuilder for bulk carrier and container vessels, was home to the biggest port terminal operator – COSCO – by throughput and capacity, and had the highest number of port calls by far.[20] China was also the only top-10 shipping power with the majority of its fleet carrying the national flag.[21] China has become the most connected maritime trading country, having improved its "liner shipping connectivity index" by 56 percent since the baseline year 2006, while the global average index went up by 50 percent during the same period.[22]

However, the above indicators do not directly translate into dimensions of power in international relations, much less provide direct evidence of successful economic statecraft by Chinese planners.[23] Contemporary national interest and military strategic concerns for interstate competition revolve around the governing of the country's key trade routes; whoever exercises more control over commercially vibrant trade routes witnesses a proportionate increase in maritime power. By this logic, an aspiring maritime power will seek to direct maritime trade flows and transshipment traffic through its ports and on its container ships, hence enhancing its "network centrality" in the global supply chain.[24] However, a nationalistic, flag-ship merchant marine approach no longer suffices for the realities of twenty-first-century global trade. Aside from managing the size and types of their fleets, carriers can establish ties with other carriers to shift costs, generate value, and change options for traders and freight forwarders in different regions. Powerful carriers with big ticket

[19] For a recent historical perspective on Chinese "opportunism" in participating in trade regimes, see Lin, K.-C. "Rhetoric or Vision? Chinese Responses to U.S. Unilateralism" in Aggarwal, V.K., Koo, M.G., Lee, S., Moon, C.I., ed., Northeast Asia: Ripe for Integration? Berlin: SpringerVerlag, 2008

[20] United Nations Conference on Trade and Development 2020

[21] Chen et al. 2017, pp. 22–28

[22] United Nations Conference on Trade and Development 2020. (*Index devised by UNCTAD and MDS Transmodal, and revised in 2019 to add a component covering the number of countries that can be reached without the need for trans-shipment, to the existing five components of the number of companies that provide services, the number of services, the number of ships that call per month, total annualized deployed container-carrying capacity, and ship sizes.)

[23] Lin 2019. For another conceptualization, see Li et al. 2005, pp. 160–167.

[24] Ibid.

capabilities and ideally placed port berths in key markets around the world can compel other actors from encroaching on their turf, creating new routes, or trading with competitors. When a network power is more concentrated rather than diffuse, policy interventions such as bilateral trade disputes and sanctions could have rippling effects on other trading partners and impose a systemic effect on the network's position in global trade beyond the bilateral effects. These effects were intended in the Trump administration's trade sanctions on China in attempting to reverse China's dominance in intra-Asian and North-South shipping since the Asian Financial Crisis of 1997.[25]

Riding the Wave of Industry Consolidation

To contextualize the consolidation of China's shipping industry, it is necessary to give attention to the broader consolidation of the global shipping industry. Shipping "conferences" were among the earliest cartels in international trade, starting with the UK-Calcutta route in 1875.[26] However, more recent shipping conferences have invited political scrutiny and accusations of oligopolistic market manipulation from a range of economic actors from exporters to truckers' unions. Since the dawn of the containerization of trade, shippers have attempted to self-regulate and make concessions to national regulators in the United States and Europe to avoid direct anti-trust interventions. Having largely succeeded in the 1980s and 1990s in securing shipping-specific exemptions from regulatory scrutiny – such as the United States Shipping Acts of 1984 and 1998 and the EC Regulation 4056/86 in 1986 – shippers eventually lost these exceptions around the time of the 2007–2009 global financial crisis.[27] Once again exposed to public criticisms of collusion and threats of regulatory intervention, shippers alleged that the industry was hyper-competitive, pointing to depressed freight rates, and proceeded to form "alliances" that enabled the world's biggest carriers to achieve economies of scale and increase service coverage by taking advantage of coordination on operational matters.[28] Cooperation in the alliances covers integration of service capabilities, including Slot Charter Agreements (SCA), Vessel Sharing Agreements (VSA), and coordinating rates and regulating capacity.[29] These anti-competitive measures are often seen as being disadvantageous to smaller shippers and users of container shipping, as well as being non-transparent to regulators, even as they generate efficiency, revenue, and route stability for the alliance members.[30] In the Pacific Ocean liner shipping market,

[25] Drezner 2019, pp. 7–24

[26] Tang and Sun 2018, pp. 4–19

[27] Chiu 2019, pp. 365–394

[28] Jensen 2019

[29] Kirstein et al. 2018

[30] Notteboom 2016; Yoshida et al. 2005, pp. 36–49; Tang and Sun 2018 pp. 4–19

most Asian export powerhouses offer antitrust exemptions for shipping companies' agreements, known as Voluntary Discussion Agreements (VDA), which often involve agreements on a general rate increase (GRI).[31] Liners had threatened countries with not maintaining their current service standards if their exemptions were not granted.[32] The cumulative result of these collusive practices was a major rise in the shipping alliances' leverage over the market and governments. By 2019, three major alliances dominated major trade routes, including the Ocean Alliance, THE Alliance, and 2M.[33] That year, the capacity shares for the Ocean Alliance, THE Alliance, and 2M in transpacific trade were 41 percent, 28 percent, and 20 percent, respectively. In transatlantic trade, those figures were 18 percent (OCEAN), 31 percent (THE), and 44 percent (2M). On the Asia-Europe route, capacity shares were 40 percent for 2M, 36 percent for OCEAN, and 23 percent for THE.[34] The oligopolistic market structure laid the foundation for the major alliances' coordinated response to the demand fluctuations in the first year of the COVID-19 pandemic.[35] While in 2014 Beijing accused global shippers of monopolistic intentions to crowd out Chinese competitors, it also sought to position COSCO in a favorable position by participation in alliances, which granted significant market power (Table 1).[36]

The Rise of the Chinese Shipping Industry Since 2000

China's expansion as a maritime commercial power has underpinned post-Mao China's developmental and national security strategies from Deng Xiaoping's Open Door Policy to China's accession to the WTO in 2001 and currently to the Belt and Road Initiative. China invested in port expansion during global economic and financial downturns that severely impacted container traffic flows in 1997–1998 (Asian Financial Crisis), 2009 (US subprime meltdown), and 2014–2015 (when global trade grew more slowly than the global economy).[37] Asia's rising trade dependency since the Asian Financial Crisis and China's export spurt after joining the WTO have driven both the rise of Asian ports and their intensified competition, resulting in China capturing the lion's share of container traffic expansion in the region.[38] In the first decade of the 2000s, approximately 65 percent of the world's container traffic came from Asian ports, with the top eight Chinese ports alone accounting for

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[31] Wakui 2019, pp. 54–74

[32] Ibid., p. 29

[33] Ghorbani et al. 2022, pp. 439–465

[34] MI News Network 2019

[35] For measures of shipping industry concentration, see Merk, O., Teodoro 2022, February. "Alternative approaches to measuring concentration in liner shipping", Marit Econ Logist

[36] Kirstein et al. 2018

[37] Lin 2019

[38] Lee et al. 2014 pp. 366–376; Li et al. 2005, pp. 77–140

Table 1 Shipping industry consolidation

Ocean carrier alliances									
	Ocean carrier	Ships	Total TEU	Ships	Owned TEU	Ships	Chartered TEU	Ships	Orderbook TEU
2M Alliance									
	1 Maersk	710	4,122,702	298	2,280,090	412	1,842,612	17	44,036
	2 Mediterranean shipping co.	591	3,902,661	157	1,047,070	434	2,855,591	22	451,544
Total		*1301*	*8,025,363*	*455*	*3,327,160*	*846*	*4,698,203*	*39*	*495,580*
THE Alliance									
	5 Hapag-Lloyd	255	1,774,132	112	1,052,321	143	721,811	6	141,600
	6 ONE (ocean network express)	223	1,612,250	69	500,971	154	1,111,279	15	266,152
	8 Hyundai merchant marine	74	750,872	28	449,074	46	301,798	6	90,060
	9 Yang Ming Marine transport Corp.	89	628,467	46	193,813	43	434,654	12	125,598
Total		*641*	*4,765,721*	*255*	*2,196,179*	*386*	*2,569,542*	*39*	*629,410*
Ocean alliance									
	3 COSCO group (includes OOCL)	501	3,022,125	177	1,567,423	324	1,454,702	12	276,000
	4 CMA CGM group	558	3,019,469	118	1,030,328	440	1,989,141	23	354,024
	7 Evergreen line	199	1,327,918	111	639,764	88	688,154	74	703,573
Total		*1258*	*7,369,512*	*406*	*3,237,515*	*852*	*4,131,997*	*109*	*1,333,597*
Alliances Total		*3200*	*20,160,596*	*1116*	*8,760,854*	*2084*	*11,399,742*	*187*	*2,458,587*

Source: Lauriat (2021, April 20), Ocean Carrier Alliances – The Tripartite. *AJOT* about a quarter of all container traffic. The rising Chinese ports have reduced the status of East Asian ports[39] and led to shifting cargo volumes from East Asia to the southern coast of China and Southeast Asia, consequently restructuring the regional supply chain network.[40]

Despite its export dynamism and market clout, China was in a relatively weak position in shipping for most of the 2000s.[41] Global carriers have gained increasing leverage over ports since the 2000s due to their oligopolistic status and asset mobility – i.e., the ability to switch allegiance to alternative ports and restructure their routes in a relatively short time. Hence, Beijing felt compelled to offset the leverage of the global carriers and to avoid deleterious competition among Chinese ports.[42] Beijing stepped up market interventions into the port and shipping sectors with a sustained political focus, financial investment, and policy prioritization.[43] These early state interventions operated under the assumption of increasing global interdependence and China's beneficial role in integration with the global transport and logistics networks.[44]

In the decade before the global financial crisis in 2008, Beijing promoted fleet capacity expansions of state-owned, subnational government-controlled, and private companies. In response to the 2008–2009 demand collapse, Chinese shippers scrambled to survive by expanding their fleets, incurring massive losses in the process.[45] As a result, while they boosted capacity and gained market shares in global container traffic, they fueled the decade-long excess capacity in the shipping industry which persisted until the onset of the COVID-19 pandemic. From 2008 to 2012, ocean-faring Chinese container ships increased in average tonnage while dropping in the relative share of the shipping market due largely to a disproportional growth in domestic coastal shipping of dry bulk and natural resources. Moderate growth for container ships continued until 2016 and 2017 when several Chinese shipping companies buckled under unrelenting global overcapacity pressures. Starting in 2015, the Ministry of Transport set down policies to consolidate the sector through mergers, acquisitions, or strategic partnerships, leading to the merger of COSCO and China Shipping Container Lines (CSCL) in 2016 and China Merchants and Sinotrans & CSC in 2017. Both episodes reduced overcapacity and financial losses and rationalized the division of labor and specialization in the Chinese shipping and logistics value chains.[46]

In 2014, the global shipping industry raised concerns about the potential international market impact of the COSCO-CSCL merger, which occurred shortly after the

[39] Notteboom and Yang 2017, pp. 184–200; Lee and Lam 2015, pp. 97–136; Song 2002, pp. 99–110

[40] Yap and Lam 2006, pp. 35–51

[41] Huang et al. 2020a, b

[42] Cullinane and Song 2006

[43] Blanchette et al. 2020; Notteboom and Yang 2017, pp. 184–200; Wang et al. 2004

[44] Yang et al. 2018

[45] Huang et al. 2020a, b

[46] Liang 2017; Dupin 2015

Chinese Ministry of Commerce blocked the formation of a strategic alliance between three of the world's largest ocean container shipping companies (Maersk, MSC, and CMA-CGM), citing anti-monopoly reasons.[47] China's regulation authorities warned of the proposed P3 Alliance, predicting that this close-knit alliance would command 47 percent of the market share in Asia-Europe container liner service and would result in a significant increase in the market concentration rate.[48] The aborted P3 alliance resulted directly from objections from China, which opened up an opportunity for COSCO to expand and become the fourth largest carrier. This led to a realignment of major global carriers into the two dominant alliances of 2M (i.e., Maersk and MSC) and the Ocean Alliance (i.e., COSCO, OOCL, CMA-CGM, and Evergreen) in 2017.[49] The state-led momentum to build a national shipping champion culminated in COSCO's $6.3 billion acquisition of the Hong Kong-based Orient Overseas Container Line (OOCL) in 2018, creating the world's third-largest container shipping group. The merger particularly enhanced COSCO's coverage of trans-Atlantic and Southeast Asian routes and allowed more ships to benefit from Chinese domestic and overseas investment in intermodal (e.g., railway, highway, inland waterways) transport links over the past decade.[50]

3 Directing Traffic: Managing Container Shipping Bottlenecks, 2020–2021

The COVID-19 pandemic precipitated considerable disruptions in global shipping, putting stress on supply chains and affecting the ebb and flow of international trade.[51] The onset of the pandemic was something of a "perfect storm" for the global shipping industry, as carriers had already been experiencing significant capacity shortages resulting from ongoing bottlenecks at ports. These issues were aggravated by pandemic conditions which ultimately complicated capacity deployment and induced negative externalities that reverberated across the global economy. For example, the capacity insufficiencies were in part a reflection of short-term changes in consumer behavior that emerged as the pandemic unfolded. While Western countries went through repeated lockdowns that had protracted disruptions on domestic logistics and production, the Chinese state ensured the resumption of manufacturing activities. Global consumer demands for Chinese exports rose dramatically after the first lockdown was lifted in the summer of 2020, and created pressures for shipping liners to redistribute vessels and containers, which benefited Chinese shippers.[52]

[47] Lui and Ouyang 2014; Atlas Network; News Desk 2019

[48] Nair 2016, pp. 89–97

[49] Szakonyi 2020a, b, c

[50] Hellenic Shipping News Worldwide 2019

[51] United Nations Conference on Trade and Development 2020

[52] United Nations Conference on Trade and Development 2021

These market adjustments created at least two sets of political-economic reverberations. First, due to an increase in demand for Chinese goods, Chinese regulators requested that COSCO and other companies provide shipping rates and supply vessels that would stabilize container routes and volumes for Chinese exports. Second, the redirection of container traffic created winners and losers, leaving stranded US exporters and several countries seeking to earn a bigger slice of global trade from US-PRC "decoupling" and the related restructuring of global supply chains.

COVID-19 Impact: Shortages and Misplacement of Vessels and Containers

Major carriers responded to the upswing in import demand in major economies starting in the summer of 2020 in a coordinated fashion by implementing revenue-enhancing strategies. Shipping alliances shifted from the pre-pandemic strategy of safeguarding market shares to one focusing on managing supply to prop up and escalate freight rates, typically by reducing the frequency of calls and number of services and deploying fewer ships.[53] In a coordinated fashion and underpinned by recent experience with GRI practices, shipping giants like Maersk, COSCO, Hapag Lloyd, MSC, and CMA-CGM charged record-high spot freight rates on their shipments. In the second and third quarters of 2020, rate hikes first hit the major Asia-US and Asia-Europe routes, with the most dramatic increases on trans-Pacific routes.[54] Spot rates from China and East Asia to the US-East Coast rose over 50 percent YoY, while rates to the US-West Coast ballooned 145 percent YoY. By the end of 2020, container freight rates reached then-historic highs which continued to rise

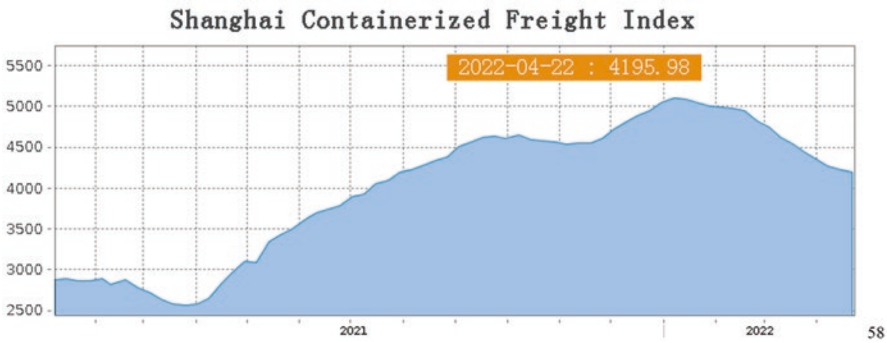

Fig. 1 Rising shipping costs, 2021–Q1 2022 (Source: Shanghai Containerized Freight Index)

[53] Ibid., p. 21, 79

[54] The Economist Newspaper 2020a, b

throughout 2021 (see Fig. 1).[55] According to the Robinson Containership Charter Index, the cost of chartering a giant container ship in October 2021 went up by 10 times over 2020.[56]

The shipping alliances used different strategies to manage their supply chains across various regions and countries. They implemented "blank sailing" programs which involved canceling scheduled stops at certain ports or even entire journeys in order to prioritize Chinese cargo over other trades. This affected container traffic between China and the United States and Europe, as well as other interregional routes. Collectively, they had voided, or "blanked," more than 400 sailings in 2020, removing 10 percent of nominal 20 foot equivalent units (TEU) capacity from active service.[57] Consequently, freight rate increases were passed to the final consumers.[58] By June 2020, the three alliances announced 126 voided sailings on Asia-North America trade through August and 94 blanked sailings on Asia-Europe trade, according to the Sea-Intelligence Maritime Consulting. In the third quarter of 2020, THE Alliance and the 2M Alliance announced the cancellation of 75 sailings through September to match capacity with weak anticipated volume levels.[59] The proliferation of blank sailing practices contributed to resource shortages and uneven capacity distribution, thereby worsening the ongoing container shortage and aggravating severe logjam at key American ports including Los Angeles, Long Beach, New York, and New Jersey. Capacity shortages also afflicted Asia-Latin America and Africa routes as ships were diverted from these secondary regions to primary consumer markets.[60]

The bottlenecks in maritime transportation proved consequential for global trade patterns. China's total trade surplus grew considerably in 2020, as the US goods trade deficit reached record levels. The pandemic, coupled with geopolitical factors, triggered similar trade account trends in a wide-ranging set of adversely affected countries, spanning export-oriented nations such as Vietnam and India to developed import-oriented countries in Europe and in South Korea. The development of such perturbing trade balance trends prompted national port and shipping authorities in affected countries to monitor and consider actions to alleviate export challenges, port congestion, and spikes in freight rates, further reinforcing public suspicions of the oligopolistic nature of shipping alliances.[61] As discussed in the following section, national regulators pushed back against rate increases and capacity management strategies, but alliances continued to coordinate to sustain their strategies.

[55] For updated figures, see Shanghai Shipping Exchange.

[56] Serwer and Zahn 2021

[57] Hickin and Griffiths 2020

[58] Ezinna et al. 2022

[59] Knowler 2020

[60] United Nations Conference on Trade and Development 2021

[61] Ibid.

Chinese State Intervention

The high freight rates and unreliable vessel and container supplies also imposed costs on Chinese ports and exporters. Transpacific trade to the US West Coast for weeks held firm above $3000 per 40 foot equivalent units (FEU), peaking at a record level of $3813, while the China Containerized Freight Index (CCFI) soared 44 percent from the start of the pandemic.[62] This resulted in a balancing act for the competing interests of the shipping and export sectors.[63] Given the broader constituency of the latter group, Beijing chose to intervene selectively via its market position and COSCO's membership in the Ocean Alliance. The Chinese Ministry of Transportation (MOT) has played an active role in coordinating pricing and capacity management among Chinese carriers, including COSCO and OOCL.[64] Preceding a planned September 15, 2020 general rate increase announced by the major alliances, the MOT asked carriers not to increase rates.[65] According to an MOT document obtained by the Journal of Commerce, Chinese regulators convened consultations for which they sought information from major carriers on "how much trans-Pacific capacity has been suspended between July and October; what percentage of their volume is spot cargo; how spot rates are established; why spot rates have increased; and what carriers are doing to curb freight rates."[66]

Regulators urged carriers to inject more capacity and to raise rates less aggressively in trans-Pacific trade, with particular attention on US-China trade routes.[67] They pointed to reduced fuel costs and port fees at many cargo gateways as reasons to cap prices. Under administrative direction from the government, COSCO made the decision to postpone its scheduled trans-Pacific GRI; it also suspended blank sailing for the period leading up to and through the national holiday from October 1 to October 7.[68] Other members of the Ocean Alliance group – namely, CMA and Evergreen – also postponed GRI.[69] Throughout 2021, China's Ministry of Commerce and the MOT urged carriers to increase shipping capacity and cap freight rates, with apparently favorable allocation outcomes.[70] The increase in freight costs in 2021 suggests that government intervention had a limited impact. However, it is noteworthy that major carriers complied with Chinese government requests, even though it could potentially harm profitability and stability, which are not typical behaviors for them. Industry analysts at the time flagged this as likely to cause an "unprecedented

[62] Lennane 2020

[63] Author's conversations with shipping industry experts, October 2020 to March 2021

[64] Lennane 2020

[65] Shen 2020

[66] Szakonyi 2020a, b, c

[67] Ibid.

[68] Linton Nightingale 2020

[69] Worldwide Logistics Group 2020

[70] China Daily 2021; Shen 2022

impact on the market… that [could] potentially derail the carriers' ability to manage capacity in the face of extreme demand volatility."[71]

Impact of Container Traffic on the Allocation of Shipping Capacities in Asia

From 2020 to 2022, global supply chain disruptions resulting from equipment shortages and capacity constraints had a noticeable impact on some of the world's major exporting countries. This led to economic setbacks, as several Asian countries, which are deeply integrated into the global value chain including those that had benefited from Trump-era trade policies, experienced export losses due to empty container shortages and shipping practices that were perceived to be unfair. Cargo shortages in South Korea, Asia's fourth largest economy, stunted its ability to export goods. While several factors contributed to the trade slowdown, container shortage was a principal factor. The logistical problems were amplified by strategic maneuvers utilized by carriers to squeeze out higher profits. Carriers displayed a preference for Chinese cargo over South Korean exports. The rates that carriers charged for transporting containers with Chinese goods on the trans-Pacific route were higher than what they could earn from transporting Korean exports, which led to order cancellations for Koreans. When shipping companies unilaterally canceled their orders, they contributed to port congestion and thwart distribution flows, creating a logjam for businesses as their inventories overflowed.

On top of clogging ports in primary commercial hubs such as the port of Busan, shippers' diversionary actions left behind steep container shortages which aggravated Korea's trade flows amid the pandemic. By mid-way through 2020, exports in South Korea reached lows not recorded in the country since 1963 when it was in the infancy of its industrial development.[72] The logistical and economic downturn motivated Korea's Ministry of Oceans and Fisheries to threaten to punish shipping companies engaging in "destructive behavior."[73] In January 2022, the South Korean Fair Trade Commission imposed a fine of $79 million on 23 shipping companies – including 11 foreign ones – for alleged collusion in freight rates on Korea-China and Korea-Japan routes over a 15-year period and announced its intention to expand the list of firms to be fined.[74] In response, the Chinese government threatened to retaliate.[75]

There was also a second-order effect of container ships being directed away from Korea, which compelled Korean exporters to "transship" their goods through

[71] Szakonyi 2020a, b, c

[72] BBC 2020

[73] Szakonyi 2020a, b, c

[74] Wallis 2022; Li 2022

[75] Korea Times 2022

Chinese ports in order to feed into the mainline trans-Pacific services.[76] Despite a strong economic rebound in the second half of 2020, the discombobulation of South Korea's supply chain continued apace, demonstrating vulnerabilities in a maritime-oriented economy to logistical volatility and the leverage carriers in the major alliances held over a nation's supply chain resilience.[77] In response, the Korean government provided short-term relief for SMEs with subsidized container rates, pledged further logistics investment, and pushed Korean carriers to pursue a self-sufficiency policy of container and vessel capacity expansion.[78] Korean regulators convened consultative meetings with carriers in the late 2020s, but their leverage was unclear and did not appear to change behavior.[79]

Similar trends were also observed elsewhere. Vietnam and India, two emerging economies deeply integrated in international manufacturing supply chains, faced export challenges in key trading sectors because of container and vessel shortage-induced rate hikes. Patently observed in the Indo-Pacific, COVID-19 produced a surge in empty container shortages as container shipments slowed on order cancellations and unloading delays at major ports. In turn, national shipping industries suffered reduced export capacity, leaving suppliers struggling to meet demand while presenting carriers the opportunity to overcharge accordingly. Seafood shipping rates from Vietnam to the EU, one of Vietnam's chief seafood importers, rose between 145 and 276 percent (depending on the port) in January 2021 compared to December 2020.[80] To remedy the surging costs, the Vietnam Maritime Administration held a meeting with exporters and foreign carriers to address the distribution bottlenecks and inflated prices, making it known that actions would be taken to rectify deliberate violations of transparency rules.[81]

Similarly, Indian exports were constrained during the pandemic by the scarcity of shipping containers.[82] Anecdotal evidence suggests that exporters were forced to raise costs to compensate for the rate surges. In turn, customers were hesitant to purchase goods at the adjusted margins.[83] India's situation was complicated by geopolitical tensions with China. China has consistently been one of India's top trading partners. Therefore, a steady inflow of Chinese imports should have brought sufficient shipping capacity for Indian exports. However, as Umesh Grover, Secretary General at the Container Freight Station Association of India, succinctly stated: "After Chinese imports came under scrutiny and bans were placed on Chinese goods, the imports to the country have gone for a toss, resulting in this equipment

[76] Wallis 2022

[77] Wallis 2021a, b

[78] Kim 2021; Angell 2022a, b; Wallis 2021a, b

[79] Szakonyi 2020a, b, c

[80] Vietnam Plus 2021

[81] Dao 2021

[82] Srivastava 2020

[83] Divekar 2020

imbalance for India."[84] In other words, increased protectionism in India dovetailed the carriers' diversionary actions in driving up container shortages, thereby exacerbating export contractions. Having been dependent on Chinese-made containers and missing a strong shipping industry, the Indian government responded to exporters' call to enter the container-making business by setting up a hub in the state of Gujarat, proposing the "Irish model" of a liberal tax regime to attract global shipping firms to Indian ports and continuing reimbursements on freight charges (which had more than tripled since 2020) for Indian farm exporters.[85]

US Exporters Left High and Dry

A paucity of available containers and significant port congestion also delayed the capability of American exporters to distribute their goods, the effects of which have harmed US trade balance and its reputation as a reliable trading partner. According to the US Census Bureau, the US goods trade deficit reached a record of $915.8 billion in 2020.[86] In 2021, it reached a new record $1.09 trillion – only to be exceeded by $1.182 trillion in 2022.[87] While it is difficult to unpack the various factors contributing to these trends, regulators and interest groups have zeroed in on the maritime transport problems. The Federal Maritime Commission (FMC), the US agency in charge of regulating ocean-borne international transportation, identified three main issues contributing to congestion at US ports: (1) demurrage and detention practices; (2) empty container returns; and (3) the refusal by some lines to carry US exports as they expedited the return of empty containers to Asia to be refilled with higher-paying import cargoes.[88] These developments have affected a swathe of export-oriented industries including agriculture.[89] Exporters also suffered cash flow problems as they were not paid for orders committed until the goods had reached customers.[90] For example, for California walnut, almond, and citrus growers, their 2022 crops had no place to go, while their 2021 crops rotted in local warehouses. The conspicuous supply chain crisis in 2020 compelled the Federal Maritime Commission to launch an investigation into foreign ocean carriers' business practices at American ports. In the March 2022 State of the Union Address, US President Joseph Biden announced new initiatives to ramp up regulatory oversight of the container shipping industry, blaming capacity-sharing alliances as a contributor to consumer price hikes and further prompting the FMC and the Antitrust Division of the

[84] Ibid.

[85] The Economic Times; Tribuneindia News Service

[86] Scott 2021

[87] Scott 2021; EPI Staff 2023

[88] Mongelluzzo 2020

[89] Larocco 2020

[90] Grimes 2022

Department of Justice to investigate ocean shipping lines for potential violations to the Shipping Act and other US laws.[91] US Representatives Dusty Johnson and John Gerimundi co-sponsored an Ocean Shipping Reform Act that aimed to protect the domestic agricultural supply chain by empowering the FMC to investigate and restrict port access to carriers imposing high costs on American exporters.[92]

In truth, the effects of container traffic disruptions on the global supply chain have been compounded by inefficiencies in the US logistics industry which has been exposed for poor coordination across key players, spotty information sharing, outdated infrastructure, and overworked truckers.[93] "Static" factors – i.e., the lack of resilience in American logistics and supply chains and the inability of American policymakers and regulators to make immediate adjustments – interacting with "dynamic" factors of shifting concentration of global container traffic in favor of Chinese exports have significantly undermined the intended effects of the trade sanctions and supply chain restructuring by the Trump and Biden administrations. UNCTAD reported that the "substitution effect" from the US-China trade war in 2019 had been reversed in 2020. The effects included a contraction of the volumes on the East-West lane, including a decrease of 7.4 percent on the peak leg, East Asia-North America, and a 3.8 percent drop on the return leg from North America to East Asia.[94] The slump in trade flows was partially offset by the substitution of Chinese volumes by exports to the United States from other Asian economies including Malaysia, Thailand, and Vietnam.[95]

The long-term diversification trends in the global supply chain are likely to continue to shift away from the world's second-largest economy. According to a survey of more than 700 firms across the world in March 2021, the proportion of EU- and US-based companies that listed China as one of their top 3 sourcing countries dropped from 100 percent and 96 percent in 2019, respectively, to 80 percent and 77 percent in 2021.[96] The direction of EU and US policies does not suggest an immediate return to the earlier trend of outsourcing to China, giving further value to state manipulation of shipping as a geo-economic response to these structural changes. For incidence, European shipbuilding and maritime equipment manufacturing industries have sought sector-specific support measures to reduce dependence on Asian suppliers for maritime technology and promote their own technological development and innovation to ensure carbon-neutral shipping by 2050.[97]

[91] Holt 2022

[92] 2022

[93] Serwer and Zahn 2021; Lynch 2021

[94] UNCTAD Review of Maritime Transport (2020), Table 1.10

[95] Ibid., p. 16

[96] Zhou 2021; Cheng 2022

[97] UNCTAD Review of Maritime Transport 2020, p. 48

4 In a Holding Pattern? Directions for Further Research

Showing consistency in its competitive approach with other sectors such as telecommunication equipment makers, China entered the global shipping market through costly capacity expansion without following a grand strategy to challenge Western multinationals' dominance of a largely self-regulating market.[98] Its industrial policy for promoting domestic shipping giants in the early 2000s mainly sought to temper over-competition under the pressures of a global supply glut. Beijing's regulatory interventions and state-directed market consolidations contributed to the emergence of COSCO as a key player in the mid-2010s, helping the company to join the mega-shipping alliances that were able to respond to the COVID-19 pandemic. At the same time, the glaring negligence of the US and Asian governments in building resilience of domestic supply chains and upgrading transport infrastructure has proved to be their main source of vulnerability. Our analysis focused on the "inflection points" in the mid-2010s and 2020–2022 when new power relations emerged in the market, allowing certain actors to steer market forces in their favor. Beijing's veto of the P3 alliance and their preference for alliances involving COSCO are examples of this. We argue that the impact of these actions should be taken into account when evaluating US-China trade relations and strategic competition in global supply chains.

Chinese firms and the central government can prioritize their own interests in the market, which may not always align with broader industry trends. Like other industries, the shipping industry experiences cycles of ups and downs. For example, the "order book" for new container ships had declined since 2008, reaching lows in 2020 not seen since 2003.[99] The historic profit levels from the fall of 2020 through 2022 will likely create temptations for major carriers to expand their fleets, especially if they remain undeterred by governments or exporters in their supply management tactics. It appeared to be the case in March 2022 when 2M reintroduced "blank sailing" at the first sign of plateauing Asia-North Europe spot rates in Q1 – which had hit a historical peak of around $15,000 per 40 ft. at the end of January.[100] The last quarter of 2022 saw flagging shipping demands from economic troubles in the United States and Europe and the zero-COVID restrictions in China, prompting 2M and THE alliances to implement blank sailing to curtail trans-Pacific vessel capacity.[101] The effectiveness of their coordinated strategies was reflected in the historic profitability of carriers through 2022.[102]

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[98] For broader debates over the approaches and tools of Chinese state interventions in industries, see Barry Naughton (2021), The Rise of China's Industrial Policy, 1978 to 2020. Academic Network of Latin America and the Caribbean on China. Eaton 2015; Hsueh 2011

[99] The Maritime Executive 2020

[100] LaRocco 2020; Baertlein 2023

[101] Angell 2022a, b; Whiteman 2022; Wallis 2022; Chambers 2022

[102] Thuermer 2022

Carriers also face more stringent marine environmental regulations and changing trade patterns, i.e., a greater share of intra-regional trade in global trade, which requires smaller vessels. These factors may turn around the historic trend of ever-increased tonnages per vessel which, as maritime economists have pointed out, had started to show signs of diminishing returns to scale even before the COVID-19 pandemic.[103] While China may be an exception to this trend, as it pushes for larger vessels and greater fleet capacity to protect its export orientation, the long-term success of this politically determined corporate strategy remains uncertain. Only time will tell whether COSCO's investment in an excessive number of large vessels will ultimately be successful.[104] In the future, COSCO may face challenges if it has invested in too many large vessels. On the other hand, it's possible that the company may benefit from having a significant share of global container traffic, regardless of profitability. The divergent responses to the changing market condition are notable in shipping alliance realignments. In 2019, the members of the Ocean Alliance extended the arrangement until 2027.[105] Might COSCO have second thought now that Maersk and MSC have announced their intention to end 2M and go separate ways by 2025, with each free to pursue capacity expansion plans?[106]

Our paper has suggested that the analysis of economic statecraft should be independent of short-term outcomes and critical of imputing rationality in the governments' crisis-response strategies. We further suggest the utility of a broader "geoeconomic" analytical scope rather than the traditional focus on strategic trade policy and domestic regulatory actions in explaining outcomes in bilateral trade and industrial competitiveness. Fundamental to this perspective is how the spatial distribution of transport nodes and traffic patterns constitutes resources for state and non-state actors to exert control for power and influence for geopolitical ends.[107]

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[103] This is a very general observation. There are significant reversals prompted by the demand spike and route-specific opportunities for new entries such as for the Asia-US West Coast traffic in late 2021 and early 2022, which led smaller carriers such as South Korean HMM to go on shopping sprees for new vessels.

[104] Placek 2021

[105] News Desk 2019

[106] Xchange 2023; The Loadstar 2023

[107] Scholvin 2016, pp. 274–283

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Part IV
Middle Power Case Studies

The US-China Strategic Competition and Korea's Economic Statecraft: Combining Bilateral and Regional Strategies

Seungjoo Lee

1 Introduction

The US-China strategic competition has spread from trade to technology, supply chains, and security. The Trump administration prioritized bilateral approaches in implementing its policy toward China. The Trump administration's penchant for bilateralism stemmed from the recognition that multilateral and institutional engagement policies, which were the basis of the Obama administration's strategy with China, revealed fundamental limitations in driving China into the liberal international order. In terms of negotiation strategy, the Trump administration assumed that bilateralism was more effective in drawing maximum concessions from China by utilizing the asymmetric economic relations between the United States and China.

On the one hand, the Trump administration's bilateral approach produced some achievements, as demonstrated in the phase one deal US-China agreement in January 2020 where the Chinese government agreed on a "numerical target" to secure increased imports to the United States. On the other hand, the limits of bilateralism were also clear. Notwithstanding its constant pressure on China, the US government failed to not just resolve the trade imbalance, which was the direct cause of the trade war, but brings about a structural change in China.[1]

Under the circumstance, the US government began to combine the bilateral approach with regional strategy, resulting in a change in the dynamics of the

[1] Trump 2015

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US-China competition.[2] The United States and China are currently engaged in a strategic competition that has extended to the Asian region. Both countries are working to shape the regional order. China has placed great emphasis on the Belt and Road Initiative (BRI) since 2013, which is an important foreign policy objective of the Xi Jinping government.[3,4] The Xi government has broadened the scope of the BRI to include information technology, digital infrastructure, satellite navigation, and health as demonstrated by the Digital Silk Road (DSR), Space Information Corridor, and Health Silk Road.[5] The United States seeks a full-fledged Indo-Pacific strategy at the regional level to counter the BRI while putting pressure on China at the bilateral level as well.[6]

Seen this way, the United States and China continue to upgrade their regional strategies by closely reflecting on bilateral relations with countries in the region. At the same time, the regional strategy has become an area of competition between the United States and China to establish their influence on the global stage through multilateral cooperation.[7] It is possible that this competition could extend beyond the regional level and into the broader global context. As such, the US-China strategic competition is multi-dimensional and complex.[8]

Korea is under increasing pressure to choose between the United States and China, making the diplomatic principle of separation of the economy and security untenable. Experts critical of China's economic power urged a shift from strategic ambiguity to strategic clarity.[9] As the strategic competition between the United States and China intensified, in this view, it was difficult for Korea to maintain a strategy of delaying choices on major issues.

Korea's strategic dilemma has also emerged at the regional level. The Xi government has promoted the BRI initiative as a response to the Obama administration's rebalancing policy. Meanwhile, the Trump administration introduced the Indo-Pacific strategy with the aim of limiting China's growing influence in the region through the BRI.[10] As the US-China strategic competition intensified at the regional level, the Korean government needed to come up with a regional strategy to cope with it, culminating in the New Southern Policy.

This paper examines the causes of Korea's pursuit of economic statecraft based on strategic ambiguity amid intensifying strategic competition between the United States and China. Korea's strategic ambiguity is primarily a result of the interaction of structural factors such as the influence of the ROK-US alliance as a key axis of

[2] Scobell 2021
[3] Goldstein 2020
[4] Bharat 2018
[5] Mardell 2020
[6] Choong 2019
[7] Lee 2017
[8] Lee 2019
[9] Hyun 2021
[10] Department of Defense 2019

foreign policy and high dependence on China. In addition, Korea's strategic ambiguity is also related to the difference between Korea's dual perception of China and Korea and Japan's perception of China.[11] Korea's dual perception of China makes Korea pursue a China policy that focuses on maintaining the status quo, while the difference in perception between Korea and Japan on China has resulted in the deterioration of Korea-Japan relations.

This paper analyzes the emergence of Korea's economic statecraft based on strategic ambiguity in the context of such complex changes. First, I examine Korea's attempt to strengthen cooperation with Southeast Asia as a regional strategy, especially in the case of the intensification of strategic competition between the United States and China at the regional level. Second, in the process of restructuring the supply chain, I explore how Korea has strengthened its cooperation with the United States while gradually diversifying the existing supply chain from China. Third, I reexamine Korea's efforts to expand cooperation with like-minded countries based on the Korea-US alliance.

The Korean government pushed for a two-pronged strategy to cope with the regional strategies of the United States and China. On the one hand, the Korean government attempted to manage the US-China strategic competition at the bilateral level. On the other hand, the Korean government has pursued a coalition with Southeast Asian countries as a means of exercising collective hedging to avoid being squeezed between the United States and China. This approach is reflected in the New Southern Policy, which seeks to address the dilemma of choosing between the United States and China by strengthening economic cooperation with Southeast Asian countries. Through this policy, Korea aims to achieve economic benefits by linking it to both the Indo-Pacific strategy and the BRI.

2 The US-China Strategic Competition and Korea's Strategic Ambiguity

The Origins of Strategic Ambiguity in Korea

During the Cold War, Korea focused on expanding foreign economic relations based on the ROK-US alliance. As a result, the economy and security could be tightly integrated into Korean diplomacy. However, the rise of China in the twenty-first century emerged as a driving force that pushed Korea to seek a new diplomatic posture. In the face of China's economic rise, strategic ambiguity emerged in Korea as a strategy to adapt to the changing external environment.

Strategic ambiguity aims to maintain and expand economic ties with China while continuing and strengthening security cooperation with the United States. Strategic ambiguity posits that the dilemma of choice between the United States and China

[11] Jung et al. 2020

can be alleviated by delaying or avoiding, as far as possible, clear choices on issues in which the United States and China are in sharp conflict. The Korean government at the time believed that the separation of the economy and security was inevitable to maintain the strategic ambiguity.

Under this strategic stance, Korea showed two features in its response to the strategic competition between the United States and China. First, despite its robust security alliance with the United States, Korea attempted not to take an outright position on the issues that could be interpreted as an attempt to contain or alienate China in a situation where the US-China strategic competition intensifies. Second, recognizing its fundamental limitations in responding to the United States and China in bilateral terms, Korea pursued a regional strategy to strengthen cooperation with regional countries to respond to the US-China strategic competition.

Korea's strategic posture was evident in the process of restructuring its supply chain. This feature was found in Korea's "China+α" push in the process of restructuring the supply chain in the wake of the US-China strategic competition and the spread of COVID-19. "China+α" strategy hinges on building new supply chains outside of China while maintaining or gradually reducing supply chains in China. Over-reliance on a specific country is dangerous to reduce supply chain fragility. In this regard, a consensus was formed within Korea that it was necessary to reduce dependence on China and secure production bases in countries other than China.

It is for this reason that the Korean government and businesses have set supply chain diversification and strengthening resilience as the core of their supply chain restructuring strategy. At the same time, the Korean government recognized that a hasty departure from China was also risky given China's huge market and the competitiveness of its supply chain ecosystem. Rather than quickly withdrawing the existing supply chain in China, Korea pursued the strategy of establishing additional supply chains in Southeast Asia such as Vietnam and India.[12] Considering that China has a huge domestic market and a competitive supply chain ecosystem, a hasty exodus from China increases the risk.

What motivated Korea to pursue strategic ambiguity? Korea's strategic ambiguity was inseparable from the US-China strategic competition. The dual perception of rising China resulted in Korea's pursuit of strategic ambiguity. Korea's strategic ambiguity aimed to minimize the strategic burden that may arise from a choice between the United States and China by separating economy and security. "The U.S. for security, China for the economy" symbolized Korea's strategic ambiguity. Meanwhile, policymakers and experts engaged in fierce debates on the feasibility of strategic ambiguity in Korea.[13] Those who were skeptical about the strategic ambiguity argued that it is practically impossible for Korea to pursue a separation of economy and security, under circumstances where major countries including the United States and China have increasingly linked the economy and security.

[12] Lee and Kim 2021

[13] Heo 2022

Meanwhile, Korea's pursuit of strategic ambiguity had to do with the Trump administration's policy changes toward Korea. As the Trump administration turned protectionist against its allies, including Korea, and demanded a sharp increase in defense burden-sharing, the fear of the US abandonment increased in Korea which was forced to seek alternatives.[14] Furthermore, as evident in the decision to withdraw from the TPP, the Trump administration substantially reduced institutional engagement in the stability and development of the regional economic order. Korea had to find an alternative to balancing China at the bilateral and regional levels. Although the ROK-US alliance is the backbone of its foreign strategy, it has become difficult for Korea to fully cooperate with the strategy of the United States.

Second, the deterioration of Korea-Japan relations also became a factor in promoting strategic ambiguity in Korea. The deterioration of Korea-Japan relations was triggered by differences in the handling of past history, but it also stemmed from a structural cause of differences in the perceptions of China between the two countries. As shown in July 2019, when the Japanese government removed Korea from the whitelist of three materials required for semiconductor production, the deteriorating bilateral relations have spread beyond historical issues into economic ones.[15] Since then, Korea pursued a strategy to increase self-sufficiency for materials and parts that were highly dependent on Japan. In this regard, the deterioration of Korea-Japan relations meant a weakening of the triangular cooperation between Korea, the United States, and Japan in response to the rise of China. From Korea's point of view, it signified that there is a limit to keeping China in check within the traditional alliance system.

Third, a competitive relationship between Seoul and Taipei began to form in the process of reorganizing the supply chain, which was exposed to vulnerabilities due to the great power strategic competition and the spread of COVID-19.[16] Since Korea and Taiwan went through different development paths during the high-growth period, they formed a complementary relationship. While Korea pursued an export-oriented strategy mainly based on the production of final goods, Taiwan pursued a development strategy of supplying parts to countries that produce final goods. However, after the catch-up strategy came to an end, Korea formed its own supply chain in the IT and auto industries, and as a result, competition with Taiwan began to form. The competitive relationship between Korea and Taiwan became more visible as the United States, which entered the strategic competition, pushed for supply chain reorganization. The rivalry between Samsung in Korea and TSMC in Taiwan is actively cooperating in the Biden administration's reshoring strategy. Moreover, Taiwan is stepping up its cooperation with Japan by digging through the cracks in the deteriorating relations between Korea and Japan. As the great power strategic competition and the shortage of semiconductor supply due to the COVID-19 pandemic continued, the Japanese government decided to attract investment from

[14] Sohn 2019

[15] Kim et al. 2019

[16] Chung 2022

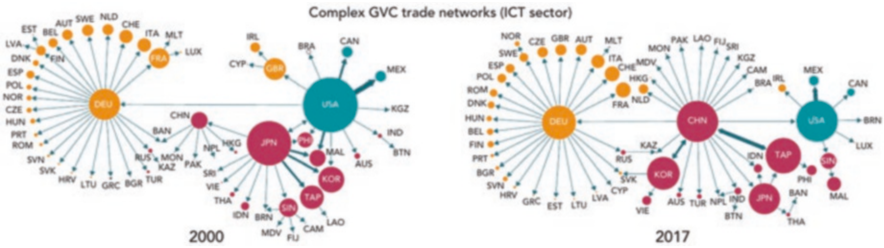

Fig. 1 Changes in GVCs in ICT sector. (Source: WTO (2019))

TSMC to build a new semiconductor factory in Kumamoto and to support half of the investment cost of up to 1 trillion yen.

As shown in Fig. 1, Korea is forming a two-way relationship with Taiwan in the ICT supply chain. Amid the intensifying great power technology competition, Korea and Taiwan have emerged as the core of the US-led supply chain restructuring. If Seoul and Taipei actively cooperate with Washington's reshoring policy, they are in a position to have a significant impact on the existing regional supply chain system.

Korea has a competitive relationship with Taiwan in the restructuring of the supply chains and reshoring policy. At the "Korea-U.S. Business Round Table" hosted by the US Department of Commerce right after the Korea-US summit in May 2021, Samsung Electronics unveiled a plan to invest $17 billion to build a US semiconductor plant.[17] TSMC also announced to invest $12 billion to build a semiconductor plant in Arizona. Samsung Electronics and TSMC requested that the Biden administration be included as the beneficiary of a $52 billion subsidy raised through the CHIPS Act. Moreover, Taiwan has stepped up its cooperation with Japan by digging through the cracks in the deteriorating relations between Korea and Japan. As the great power strategic competition and the shortage of semiconductor supply due to COVID-19 continued, the Japanese government decided to attract investment from TSMC to build a new semiconductor factory in Kumamoto and to support half of the investment cost of up to 1 trillion yen.

Hedging Between the United States and China

One can point out two main reasons why Korea pursued strategic ambiguity. First, the rise of China has been both an opportunity and a threat to Korea, which prompted Korea to develop a dual perception of China. The high dependence on China not only caused Korea's structural weakness in responding to China but also encouraged Korea to diversify its economic relations. China overtook the United States in 2003 to emerge as Korea's largest trading partner. Since then, Korea's trade volume

[17] Doh 2021

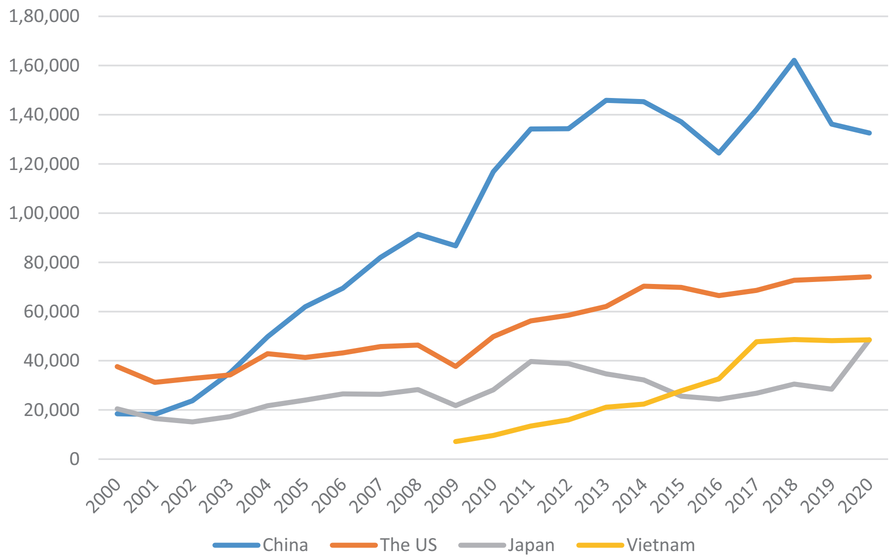

Fig. 2 Korea's top trading partners (USD million). (Source: https://unipass.customs.go.kr/ets/index.do?menuId=ETS_MNU_00000176)

with China has exploded, and in 2018, when the US-China trade war broke out, it was larger than the trade volume of the second to fourth trading partners, the United States, Japan, and Vietnam combined (see Fig. 2).

Korea's dependence on China has also increased in major industries' dependence on materials and parts. A report by the Federation of Korean Industries found that among Korea, the United States, and Japan, Korea has the highest dependence on imports of intermediate goods, including parts and materials. In the case of parts and materials, Korea's dependence on China was 29.3%, higher than the United States 12.9% and Japan 28.9%. For intermediate goods, Korea recorded 27.3%, which is higher than the United States (8.1%) and Japan (19.8%). In semiconductors, batteries, pharmaceuticals, and rare earth included in the supply chain review launched by the Biden administration shortly after taking office, Korea showed the highest dependence. In the case of semiconductor materials and components, Korea's dependence on China is 39.5%, which is much higher than that of the United States (6.3%) and Japan (18.3%). Korea's dependence on Chinese materials and parts increased the most since the outbreak of the US-China trade war.[18]

The rapid increase in trade between Korea and China provided an opportunity for Korea to effectively respond to uncertainties in the external environment, such as the 2008 global financial crisis, but also acted as a source of structural vulnerability to China's economic power. When the Korean government decided to deploy THAAD in February 2017, the Chinese government responded with economic

[18] Federation of Korean Industries 2022

Table 1 US allies' position on key issues

	Australia	France	Germany	Italy	Japan	Poland	Korea	UK	US
Signed statement to UN opposing Hong Kong National Security law	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes
Signed statement to UN opposing China's policies on Xinjiang	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes
Restrictions on Chinese 5G vendors	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes
South China Sea: Refuted legality of China's nine-dash line claim	Yes	Yes	Yes	No	Yes	No	No	Yes	Yes
BRI agreement	No	No	No	Yes	No	Yes	No	No	No
Screening rules on Chinese investments	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Support for Taiwan's participation in the WHO	Yes	No	Yes	No	Yes	No	No	No	Yes

Source: Ford and Goldgeier (2021)

retaliation, centered on retail, tourism, and entertainment. As a result, the loss of Korean companies is estimated to reach up to 22.4 trillion won.[19]

Table 1 shows significant differences among US allies on key issues related to China. A statement submitted by the German government criticizing the Chinese government for human rights issues was signed by 39 member states of the United Nations. Twenty-three of the 30 NATO member states joined the statement. Of the five US allies in Asia, only two joined the statement: Australia and Japan. Korea and Thailand did not express an official position on this statement, and the Philippines even signed a statement supporting the Chinese government's position on the Hong Kong issue. The diversity of US allies' policies toward China is also reflected in the economic realm. Germany, which has close economic ties with China, is reluctant to openly criticize China.[20]

In responding to US policies toward China, such as Hong Kong National Security Law and restrictions on Chinese 5G vendors, Korea shows the most distinctive features. Korea, unlike other US allies, has taken strategic ambiguity on key issues, except that it has not officially signed a BRI agreement with China.

Furthermore, the experience of Chinese economic retaliation has also pushed Korea to take a cautious approach to significantly strengthening cooperation with the United States in the context of US-China strategic competition. Korea's strategic ambiguity is evident when compared to other US allies.

Even considering the diversity among US allies, Korea's response to China issues stands out in particular. As shown in Table 1 with regard to major issues, such

[19] Industrial Technology Research Center 2017

[20] Ford and Goldgeier 2021

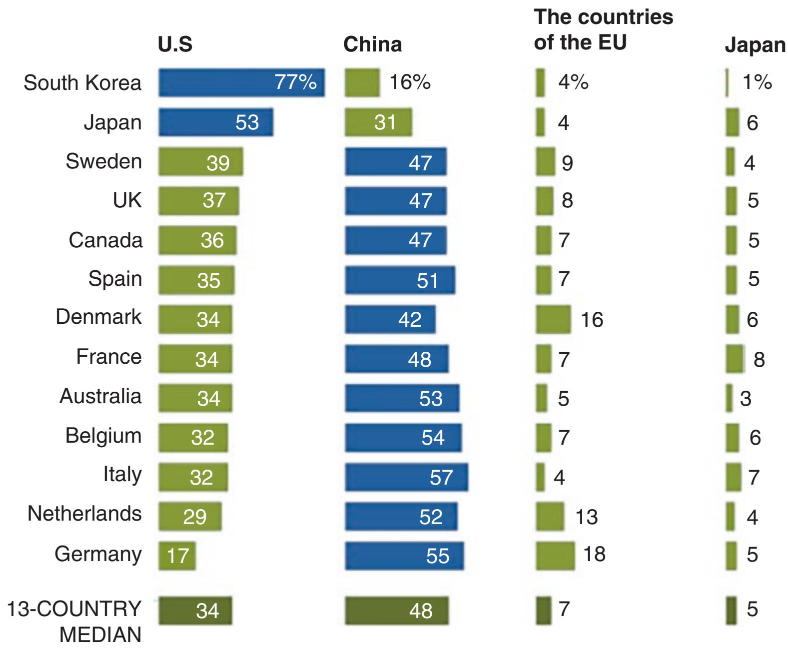

Fig. 3 Korea's perception of the United States and China. Source: Pew Research (2020)

as criticism of China in the field of human rights, restrictions on the adoption of Chinese technology, disputes in the South China Sea, the conclusion of the Belt and Road Agreement, strengthening of Chinese investment screening, and Taiwan's accession to the WHO, Korea has taken a very reserved attitude, avoiding explicit and active choices (see Table 1).

Second, in contrast to the growing economic dependence on China, Korea's perception of China has deteriorated. Figure 3 shows that, among the 13 countries surveyed, Korea had the most favorable perception of the United States while displaying the most unfavorable perception of China. Even compared to Japan (53%), which has actively strengthened alliances with the United States, the share of recognition of the United States as friendly (77%) is much higher. By contrast, the favorable perception of China was only 16%, much lower than the average of 48% in 13 countries. Moreover, in contrast to the tendency of older people to have higher unfavorable perceptions of China, in Korea, the young generation was found to be more unfriendly to China. This phenomenon is very peculiar compared to other countries. In most countries, the proportion of "unfriendly" perceptions of China is higher among the old generation than among the young, whereas in Korea, the "unfriendly" perception of China is higher among the young generation (see Fig. 4). The young

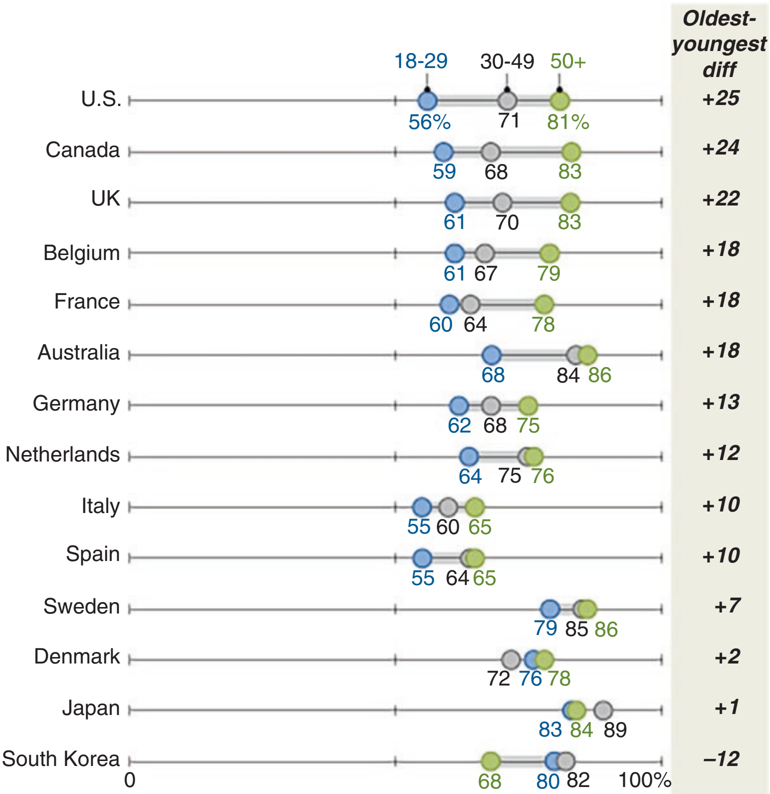

Fig. 4 Age gap in the perception of China. (Source: Pew Research (2020))

generation in Korea formed a very critical view of the deterioration in Korea-China relations.[21]

The economic dependence on China and the friendly perception of the United States symbolize the strategic ambiguity pursued by Korea. As competition between the United States and China intensified at the regional level, high dependence on China served as a constraint on Korea's ability to strengthen cooperation with the United States. However, as a result of China's increasing economic power and asymmetric interdependence between China and Korea, Korea's perception of China rapidly deteriorated. Selective strengthening of cooperation with the United States and maintaining the status quo and economic diversification with China are key features of strategic ambiguity. This is the reason why the Korean government has established and implemented its own regional strategy in response to the intensifying strategic competition between the United States and China in Asia.

[21] Pyo 2021

The Restructuring of Supply Chains and the "China+α" Strategy

In the wake of the US-China strategic competition, Korea has also attempted to remedy its structural problems, which required linkage to regional strategies. At the core was to reduce vulnerabilities to China by reducing its dependence on China where both Korean and Southeast Asian countries had common interests. Since 2017, when the US-China strategic competition erupted, Southeast Asian countries have managed not to increase their dependence on trade with China. As a result, Southeast Asia's trade with the United States has steadily increased.[22] Having experienced China's economic retaliation in 2016 about the Korean government's decision to deploy the THAAD, Korea also found it absolutely necessary to diversify its economic relations. The repercussion of the COVID-19 further prompted Korea actively to reconfigure supply chains.

The gist of strategic ambiguity was also reflected in restructuring supply chains. Meanwhile, both the Korean government and firms carefully crafted the China+α strategy so that it is not misunderstood as a "China exit" or "containing China" strategy. Because the need to complement the vulnerability of the supply chains revealed by COVID-19 has increased, the Korean government conceptualizes the "China+α" strategy as a part of a strategy to strengthen and diversify the supply chains rather than as a Chinese strategy. Korea pursues a "China + α" strategy rather than forming a new supply chain to replace the Chinese-centered supply chains.

The Biden administration made it clear that it would pursue multilateral cooperation to establish a rule-based international order. Pointing out that the supply chains for high-tech products as well as medicines and personal protective equipment turned out to be vulnerable in the wake of the pandemic, the Biden administration indicated that it would push for reshoring to reduce vulnerabilities and revive the US manufacturing capacity, which is intertwined with the restructuring of the supply chains. Furthermore, as shown in "Made in All of America by All of America's Worker," the Biden administration attempts to closely link the restructuring of the supply chain to strengthening labor-related regulations.[23]

Despite numerous discussions about the feasibility of decoupling supply chains between the United States and China, Korea consistently pursued the China + α strategy to diversify. Southeast Asia emerged as a natural candidate for the diversification of the supply chains. In short, Korea broadened its supply chains into Southeast Asian countries while maintaining the existing supply chains in China. The Korean government linked the China+α strategy to the regional strategy, the New Southern Policy, expecting that such an attempt is less likely to be construed as an attempt at "China exit."

Second, the Korean government had to resolve the time mismatch between the restructuring of the supply chains and China's economic power. That is, the Korean

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[22] The Economist Intelligence Unit 2020

[23] Shih 2020

government was concerned that while supply chain restructuring would take a significant amount of time, active cooperation with the Biden administration on reshoring could result in an immediate loss of access to the Chinese market. Korea could not help but find ways to respond flexibly to the Biden government's reshoring and supply chain strategies.

It is against this backdrop that the Korean government considers participating in the Biden administration's efforts from the perspective of China + α, rather than seeking drastic changes. In the long term, the Korean government thought that Korea would be able to secure a position to link the existing Chinese-centered supply chain and a newly formed supply chain led by the United States. By securing such a position, the Korean government expected that Korea could contribute to strengthening the manufacturing capacity of the United States without causing China's economic retaliation.

The Korean government considers taking advantage of its position within supply chains as a means of cooperation, not confrontation or conflict with China. The Korean government tries to find measures to prevent the deterioration of Korea-China relations. The Korean government approaches the restructuring of the supply chains in terms of diversification and resilience of the supply chains. Nonetheless, in the face of the Chinese government's demands for Korea not to cooperate with the Biden administration's reshoring and supply chain, the Korean government was forced to come up with measures to reduce the risk of China's retaliation. Since it cannot rule out the possibility of retaliation, the Korean government carried out a close review of the types and effects of leverage that it can mobilize depending on the development of the situation that should be implemented.[24] Despite its high dependence on China as a whole, Korea can utilize its crucial position in the supply chains as one of the few countries that secure the hub position in the key high-tech industries.

In addition to strategic considerations, the Korean government also had to take into account the Southeast Asian countries' unique position to adopt the China + α strategy. In the course of the US-China strategic competition, Southeast Asian countries emerged as the main beneficiaries of the restructuring of the supply chain, because MNCs found Southeast Asia as an alternative destination for FDI. While widely sharing concerns about protectionism caused by the US-China strategic competition, Southeast Asian countries as major beneficiaries of the US-China strategic competition were tempted to attract FDI to Southeast Asia.[25] The Korean government had to work out a detailed plan to reflect the intersects and concerns of Southeast Asian countries simultaneously while executing the restructuring of the supply chain.

[24] Park 2021

[25] The divergent responses of Southeast Asian countries to Chinese regional strategies are closely related to restructuring the supply chains (Zhang 2018).

The Korea-US Alliance and Cooperation with Like-Minded Countries

The regional competition between the United States and China poses a complex challenge not only for Korea but also for Southeast Asian countries. For Korea to cope effectively with such complex challenges, it is necessary to formulate and implement a coherent regional strategy. The Korean government attempted to upgrade the New Southern policy to effectively incorporate the changing regional dynamics into its regional strategies.

Korea preferred a strategy to induce the United States to return to regional multilateralism under the premise of shared interest with the United States. While rejecting protectionism, the Biden administration sought to restore leadership in the rules-based order by reforming fragmented and outdated multilateralism.[26] The Biden administration focuses on establishing the twenty-first-century trade rules as a means to hold China in check. Contrary to the Trump administration's unilateralism, the Biden administration made it clear that the United States would create a regional and global order where it can share economic benefits while strengthening security cooperation with allies and partners in the region. The Biden administration highlighted that it would strengthen cooperation with Asian allies and partners.[27] Criticizing the Trump administration, Biden claimed that the United States would rejoin international treaties, agreements, and bodies. He specifically mentioned that the Trump administration made a dire mistake in allowing China to use Asian trade rules by leaving the TPP.[28] After presenting a regional economic vision, the Biden administration began to take concrete steps to enhance the viability of the Indo-Pacific strategy.

The conclusion of RCEP negotiations in November 2020 marked a turning point for the Asian economic order. It is likely to provide a strategic rationale for the US return to regional multilateralism in Asia. Unlike TPP and CPTPP, RCEP has a symbolic meaning of "Pan-Asian Mega FTA" as well as has significant strategic values in that it is the first mega FTA that China has participated in. Moreover, India's eventual withdrawal from RCEP made it even more difficult to keep China in check. In this regard, President Biden himself expressed the view that the TPP is not a perfect agreement, but an effective means of keeping China in check. From a domestic political point of view, however, it is not likely for the Biden administration to attempt an early return to the TPP.[29] Rather, the Biden administration is likely to take a step-by-step approach to push for TPP renegotiation externally to place a higher priority on incorporating domestic political consideration into foreign economic policy, which ultimately culminated to "Build Back Better."[30]

[26] Ikenberry 2018

[27] The White House 2021

[28] Maizland 2021

[29] Bremmer 2020

[30] Reuters 2020

Because the Biden administration's return to the TPP is not likely in the foreseeable future, Korea, along with other countries in the region, pursued a dual-track approach. First, by upgrading the ROK-US alliance, the Korean government pursued a strategy to utilize it to establish a new standard for regional order. Immediately after taking office, President Biden launched a "100-day supply chain review" and. in June 2021, released "Building Resilient Supply Chains, Revitalizing American Manufacturing, and Fostering Broad-Based Growth." It also announced "Executive Order on America's Supply Chains: A Year of Actions and Progress, in February 2022." What the two reports emphasize in common is to reduce dependence on foreign, especially China, for key high-tech technologies, increase domestic production capacity, and reorganize the industry-industry-university ecosystem to strengthen domestic technological innovation capabilities.

The Korean government attempted to elevate the bilateral cooperation with the United States, focusing on reshoring and high-tech cooperation, which the Biden administration places a high priority. Given concerns that the United States accounts for just 12% of semiconductor production worldwide, despite it having a 47% share of the semiconductor market, the Biden administration unveiled CHIPS Act, which provides the semiconductor industry with US$55 billion to boost the domestic manufacturing capacity. The Biden administration found it imperative to expand partnerships with Seoul and Taipei in order to secure the stability of the supply chains in semiconductors. In the case of the battery sector, as emphasized in the "100-day supply chain review," it is highly important to "secure an end-to-end domestic supply chain for advanced batteries," expand production capacity in the United States, and build a resilient supply chain.[31]

Reshoring has emerged as a means of reducing dependence on China by increasing domestic production capacity. However, the Biden administration itself is aware that reshoring will not make the US high-tech industry self-reliant. The reason the Biden administration expressed its will to "build bridges, not walls" is because it is difficult to guarantee the effectiveness of reshoring without international cooperation. This approach could potentially be effective in that the Biden administration seeks network cooperation. Contrary to the Trump administration's unilateral and indiscriminate pressure on China, the Biden administration narrowed the scope of coercion on China and raised the level of containment as vindicated by "small yard, high fence." The Biden administration's international cooperation means working with countries to help achieve these goals. As a result, a common ground for cooperation was formed between Korea and the United States. The Korean government took advantage of the Korea-US alliance to pursue a strategy to secure a key position in international cooperation in the high-tech industry by cooperating with the reshoring of the high-tech industry under the Biden administration.

Second, Korea also placed a higher priority on enhancing cooperation with like-minded countries. The Korean government expected that regional cooperation would provide Korea with strategic space to maneuver in the US-China strategic

[31] The White House 2021

competition.[32] Given that the US-China strategic competition is playing out in the context of regional strategies, it is important for both the United States and China to seek partners rather than relying solely on unilateral pressure. Regional countries face dilemmas in their relationships with both the United States and China, and they have responded in a variety of ways. China has used economic retaliation to pressure some countries to comply with its foreign policy objectives. While some Asian countries view China's Belt and Road Initiative and Digital Silk Road as opportunities for infrastructure development, others have concerns about Chinese influence and intentions. It is important for countries in the region to strengthen solidarity with one another, even as they try to avoid economic retaliation.

3 Korea's Regional Strategy as Economic Statecraft

The response to the US-China strategic competition has been a top priority in Korea. As the US-China strategic competition intensifies, Korea faced increasing pressure from the United States and China. Given that the majority of countries in the region sought a hybrid approach to the US-China strategic competition rather than outright balancing or bandwagoning,[33] the Korean government pursued strategic flexibility. The Korean government primarily relied on the posture of strategic ambiguity, which delayed decisions about the key issues in the region. As for the matter of choice between the United States and China, the Korean government thought that it needed to ensure that cooperation with one country on certain issues should not be perceived as hostile to another country.

However, the perception that it would be more difficult to maintain strategic ambiguity began to be widely shared in Korea, as a competitive structure was created in specific issue areas between the United States and China. The focus of the regional strategy was on China's response to its attempt to focus on Korea as a weak link. For example, viewing Korea as a weak link in the Indo-Pacific strategy or the Korea-US-Japan triangle cooperation, China has attempted to separate Korea from the US-led cooperation in the region.[34] Unable to deal with the Chinese attempt in bilateral terms, Korea actively examined other alternatives including regional strategies.

The Korean government believed that the regional strategy rather than the bilateral strategy could be more effective in easing pressure arising from the US-China strategic competition. The Korean government's stance was affirmed in the Fourth Korea-US High-Level Economic Consultative Meeting in November 2019, where the Korean government expressed its intention to strengthen Korea-US economic

[32] Lee 2021a, b
[33] Kuik 2016
[34] Pak 2020

cooperation by linking the Indo-Pacific strategy and the New Southern Policy.[35, 36] The Korean government launched the New Southern Policy to establish cooperative partnerships with Southeast Asian countries and India by diversifying strategic and economic relations.

Rather than pursuing its own strategic choice, the Korean government tended to utilize its leverage in negotiations with China by securing a common negotiating position through close coordination with its allies and partners.[37] The Korean government thought that the New Southern Policy would serve as a platform to strengthen cooperation with like-minded in the region and ameliorate the pressure arising from a choice between the United States and China. The Korean government reformulated its regional policy to take advantage of this strategic room more effectively, which aims to reshape regional order based on cooperation with countries in the region.

First, the main thrust of the Korean government's strategic ambiguity was to make preemptive efforts to avoid the situation where it should take sides between the United States and China and, if inevitable, prepare fallback strategies to minimize the negative effects of strategic choice. Realizing that it could not seek bilateral cooperation based on values and norms with China, the Korean government concluded that it is neither possible nor desirable to pursue a fully expanding or deepening of Korea-China relations. Drawing on this policy direction, the Korean government has placed a high priority on managing the status quo while paying attention to risk factors that could undermine Korea-China relations.

The Korean government came up with the New Southern Policy as an alternative to complement the built-in limitation of strategic ambiguity that it has implemented in dealing the United States and China at the bilateral level. The Korean government designed the New Southern Policy as a diplomatic tool linking the BRI and the Indo-Pacific strategy, thereby expanding strategic room between the United States and China. The Korean government believed that it could dispel the perception of Korea as a weak link.

Second, the Korean government sought to maintain a flexible stance on the US demand for Korea's cooperation with its China policy. Aware that it was not feasible for Korea to separate economic relations with China to cooperate with the US-China policy, the Korean government needed to find a way to cooperate with the United States without risking its economic relations with China. While Korea agreed to link the Indo-Pacific strategy with the New Southern Policy in the Fifth High-Level Economic Dialogue in October 2020, the Korean government tried to identify specific areas of cooperation to improve the bilateral relations in the broad context of regional cooperation. Korea has accumulated experience in carrying out a number of development cooperation projects in Southeast Asia in the process of promoting

[35] Huynh 2021

[36] The US government also stresses that Korea's participation in the 5G Clean Path will be of great benefit to Korean companies such as Samsung and SK Hynix, which need to consider the economic effects of emerging as a new alternative to EPN and 5G Clean Path.

[37] Boustandy and Friedberg 2019

the New Southern Policy. The Korean government particularly attempted to take advantage of such experiences to align the New Southern Policy with the BDN. In doing so, the Korean government thought that it could help the United States transform the BDN from an overall vision to a concrete and comprehensive implementation strategy.

Quad is a crucial case to test the validity of Korea's strategic posture.[38] Korea has been under increasing pressure from the United States to join the Quad. The Korean government thought that the Quad Plus, which was convened in March 2020 to discuss international cooperation measures on COVID-19, would gradually turn into more regular consulting mechanisms. In May 2020, Quad Plus plans to expand its scope of cooperation to discuss economic cooperation measures after COVID-19.

Instead of joining the Quad in a wholesale manner, the Korean government pushed for two alternative responses. First, the Korean government chose to participate in the Quad Plus on an issue-by-issue basis, placing a high priority on a partnership with the United States to address cooperation for regional responses to fight COVID-19. The Korean government also sought an "emerging security partnership" in order to prevent the recurrence of pandemics and other new types of threats. The Korean government particularly chose to cooperate on issues related to universal values and norms within the framework of Quad Plus rather than joining the exclusive framework that might be construed as targeting China.

The Korean government thought that it could take advantage of its successful track record of combating COVID-19 to share its experiences with other countries in the region to enhance regional cooperation without alienating China. The Korean government's decision to join regional efforts to deal with COVID-19 along with New Zealand and Vietnam manifests Korea's efforts to maneuver between the United States and China.[39] Second, the Korean government attempted to come up with measures to promote Quad Plus cooperation in conjunction with existing regional cooperation organizations. Even if Korea participates in Quad Plus, the Korean government stressed that it does not resonate with Quad's goal of responding to China's offensive diplomacy in an integrated manner. To this end, the Korean government worked on measures to promote Quad Plus cooperation by building upon existing regional organizations.

It is against this backdrop that the Korean government was forced to find a way to alleviate uncertainties in the rapidly changing international and East Asian order. The Korean government attempted to create a "peace" foundation by developing its own regional strategies, which aimed to ease competition between the United States and China. Recognizing that it would be unable to mediate the competition between the United States and China, the Korean government thought it paramount to enhance cooperation with Southeast and Central Asian countries. Under the circumstance where the global economic order turned protectionist since May 2018, Korea as a highly tradedependent country, was desperate to expand cooperation to find a

[38] Panda 2022

[39] Mathur 2020

way to sustain the momentum for the rules-based order. The aggravating global economic order amplified the difficulty for Korea as it did not fully recover from China's economic retaliation in the aftermath of its decision to deploy the THAAD. Under the circumstance, the Korean government recognized that strengthening relations with Southeast Asia and India could be an alternative to reduce economic uncertainties.

The Korean government attempted to devise a regional strategy distinctive from the existing policies designed to strengthen the bilateral relations with individual countries in Southeast Asia. Rather than seeking its own short-term interests, the Korean government aimed to establish reciprocal relationships based on trust with Southeast Asian countries. In doing so, the Korean government thought that it could contribute to building trust between regional and non-state actors.

The Korean government unveiled the New Southern Policy, hoping that it could serve as a platform of communication and cooperation between countries that share interests in easing the US-China competition structure. By developing platforms to promote regional cooperation, the Korean government ambitiously envisaged providing a venue for countries in the region to coordinate interests across a variety of areas.

The Korean government has worked with Southeast Asian countries in digital and high-tech areas to utilize the aid-investment nexus, departing from the existing strategies centered on ODA projects. For this objective, the Korean government closely reviewed ASEAN's perception and response to strategic competition in the United States and China. First, ASEAN's *ASEAN Outlook for Indo-Pacific* in June 2019 suggested that the Asia-Pacific region is at the center of geopolitical competition and forecasted that dual dynamics of "cooperation and zero-sum behavior" between the United States and China would coexist. Both Korea and ASEAN have a common view that it is critical to creating an "inclusive regional architecture" because the contention of US-China regional strategies will result in increased uncertainty in the regional order. Given that ASEAN has long played a role as a leader in promoting regional cooperation, the Korean government perceived ASEAN as a natural candidate for creating an inclusive regional architecture because it was crucial for ASEAN to prevent further intensification of US-China competition. In line with this thinking, the Korean government thought that it could find an area of cooperation with ASEAN. As ASEAN designated maritime cooperation, strengthening connectivity, sustainable development goals, and economic and technological cooperation as four major areas of cooperation, the Korean government could find areas of cooperation. The Korean government designed the New Southern Policy to address non-traditional security issues such as economic cooperation, trade, environment, and energy.

Second, the Korean government noted that the US-China strategic competition is highly likely to pose challenges to ASEAN centrality. Because ASEAN has stressed that the design of regional architecture should be an "ASEAN-led process," the Korean government made it clear that the New Southern Policy would harmonize with ASEAN centrality. By utilizing the framework of cooperation centered around the "ASEAN-led process," the Korean government thought that it could produce a significant impact on the regional order.

Third, the Indo-Pacific strategy and the BRI have shifted to digital infrastructure projects.[40] While actively reflecting on these changes to develop new areas of cooperation, the Korean government aspired to meet ASEAN's goal to strengthen cooperation in emerging issues such as digital infrastructure cooperation, smart cities, industrial clusters, and financial cooperation centers. In order to facilitate cooperation in these areas, the Korean government found it necessary to enhance cooperation with the United States, including sharing information on regional projects and implementing joint pilot projects, as demonstrated in the fact that the Ministry of Finance and Strategy (MOSF) signed the Korea-US Infrastructure Cooperation MOU in October 2019. Both countries subsequently agreed on the Korea-US Working Group Meeting and the Round Table for Private Agencies.

Fourth, cooperation with ASEAN also indicated that Korea preemptively pursues cooperation with like-minded countries by taking advantage of concerns over the leadership vacuum in the wake of COVID-19. COVID-19 revealed the limitations of individual country-level responses and the need for transnational cooperation. Furthermore, China used COVID-19 as a means of diplomatic tools. In addition, the Chinese government used COVID-19 as an opportunity to normalize the BRI. As a result, China faced severe criticism for strategically projecting Chinese geopolitical interests into "mask diplomacy" and offensive diplomacy against Hong Kong and Xinjiang. Under this circumstance, the Korean government thought that it was time to expand the scope of the regional policy. It was vital for Korea to attract ASEAN as a partner for regional cooperation, which would ultimately pave the way for the global fight against pandemics.

Fifth, the restructuring of the regional supply chain emerged as an area where cooperation is most needed, as COVID-19 revealed the vulnerability of GVCs. Korea and Southeast Asian countries had common interests in restructuring the GVCs to reduce the structural dependence on China.

4 Conclusion

Given that the strengthening of the US-China strategic competition is already shaping the region, it is inevitable that a competitive structure will be formed between the BRI and the Indo-Pacific strategies. The intensifying competition of regional strategies between the United States and China means that the key problem facing Korea could also increase pressure on the choice between the United States and China. It has become obvious for Korea to manage the uncertain situation in bilateral terms. Considering these practical restrictions, Korea was forced to seek complex strategies to combine bilateral and regional policies. In addition, the Biden

[40] Liu 2020

administration seeks to strengthen international cooperation with countries in the Indo-Pacific while clarifying its goal of not allowing China to lead the regional economic order, prompting Korea to systematically respond to systematic challenges. Korea needed to seek ways to flexibly tap the Biden administration's regional strategy to its regional strategy without incurring China's economic retaliation. The Biden administration's regional strategy is an opportunity and challenge for Korea to take preemptive action.

The Korean government's regional strategy, represented by the New Southern Policy, has contributed to diversifying Korea's diplomacy, breaking away from traditional diplomacy centered around the four great powers. The New Southern Policy has relatively effectively filled the diplomatic vacuum between bilateral diplomacy and multilateral diplomacy centered on international institutions. ASEAN has long played a role as a leader in enhancing regional cooperation, but the rise of China and intensifying competition between the United States and China pose challenges to ASEAN centrality. Considering that Korea and ASEAN can have a certain impact on the direction of change in regional order, it is necessary to pursue cooperation with ASEAN.

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Vietnamese Geoeconomics in a Polarized Global Economy: Understanding Bamboo Diplomacy and Its Viability

Tung Bui

1 Introduction

In recent years, Vietnam has found itself in a position where it is reinforcing its decade-long bamboo geoeconomic policy. Using bamboo as a metaphor, Vietnam's foreign policy seeks to combine firmness in principles with flexibility in tactics. In the face of a VUCA[1] world (vulnerable global supply chains, uncertain state of the local and global economy and finance, complex international relations, and ambiguous economic statecraft of many of its trade and political partners), Vietnam has maintained its stance of not siding with any particular superpower. While solidifying its principles with China, its giant neighbor up North, Vietnam has also strived to sustain its alliance with Russia and expand its collaborations with more geographically distant powers, such as the United States, the European Union, South Korea, and ASEAN.

In this paper, we propose a three-force framework to explain the rationale behind Vietnam's bamboo policy in the new world geopolitical context. Our goal is to assess the sustainability of this policy and, more conceptually, to explore whether Vietnam's statecraft could serve as a viable pilot model for emerging regional middle powers. Although a hegemonic power has returned in the first decades of the twenty-first century, Vietnam has been increasingly seen as an emerging middle power that has effectively asserted its political stance and skillfully maintained

[1] Barber 1992

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positive relations with countries that have conflicting interests, including the United States and China.

We also examine whether the relative success of Vietnam's bamboo strategy is the result of skillful statecraft, pure circumstantial luck, or a combination of both. However, we also argue that Vietnam's geopolitics could be a double-edged sword, as it walks a tightrope between the superpowers, and the question remains whether the rope will become too thin to manage. We raise the concern of whether the multiplying bilateral agreements with different protagonists are sustainable in the long term.

2 Vietnam's Emergence in the Intensification of World Polarization

Recently, some have claimed that the first two decades of the twenty-first century have trended toward ideological extremes that have shaken societies around the globe. To a few researchers, one of the earlier visible fallouts of political divisions at the global scale started with the narrow decision of the UK citizens to exit the European Union in 2016. However, it is the renewed tension between the United States and China that has heightened polarization, with a domino effect on the shaping of global geopolitics.

Despite recent heightened media and political attention, the tension between the United States and China is not a new issue. It dates back to the establishment of the People's Republic of China in 1949, with periods of both tension and cooperation since then. Historical events include China's support of North Korea in 1950, the Taiwan Strait Crisis in 1954, the Tibetan Uprising in 1959, the Vietnam War in 1964, the US-China rapprochement following the Sino-Soviet border conflict in 1969, the use of ping-pong diplomacy in 1971 leading to the signing of the Shanghai Communiqué to improve relations in 1972, and the One-China Policy in 1979.

Arguably, the genesis of today's US-Sino tension started with the initial American support of China's admission to the World Trade Organization (WTO) in 2001 paving the way for China to become, just a few years later, the world's second largest economy and US's largest foreign creditor. Soon after, the support was transposed by a series of concerns over China's new political standing. In 2013, the United States and China made an initial attempt to establish a "new type of great power relations" between the two countries under Presidents Obama and Xi. However, this effort soured over time due to mutual accusations of trade technology theft, cyber hacking, and the militarization of disputed territories in the South China Sea. The situation was exacerbated by the escalation of tariffs between the two nations during the Trump administration, with both sides engaging in tit-for-tat measures.

Vietnam's position in the region has been strengthened by recent events such as the US-China trade war and disruptions in the global supply chain. As a result, Vietnam has become an important ally to East Asian nations and the United States.

As a reaction to mitigate the supply chain disruption, countries that have heavily invested in China as a manufacturing outlet – notably, the US, EU, Japan, and Korea – contemplate Vietnam as one of their major alternate supplier partners. The Wall Street Journal reported that Apple Inc. has precipitated its plans to move productions out of China; Vietnam and India would fill in the void. Korea has made Vietnam its third largest economic partner after China and the United States.

While proactively engaging with the rest of the world as a rising manufacturing powerhouse, Vietnam continues to emphasize its special relationship with China. This is evidenced by the China-Vietnam meeting in Beijing on October 30, 2022, between the two heads of state just a week after President Xi Jinping was elected for the third term. In the meantime, Vietnam is seeking alliances with the United States, the European Union, and many of its partners in ASEAN to secure its national security.

In a world marked by starker asymmetry of power, Vietnam is definitely pursuing its bamboo strategy to bridge between rivalries.

3 Statecraft of Emerging Regional Middle Powers

Gilley[2] and Shin[3] claim that a nation would rise to the middle power status when it is capable to deploy political and economic actions to defend its national interests against greater powers. To achieve this goal, Cooper and Dal[4] suggest that in order to pursue its national interests, middle powers craft a geopolitical strategy that seeks to navigate through international conflicts via multilateral compromises while portraying themselves as good international citizens.

This navigation effort depends on a number of unique traits of the middle power (Erskine[5]):

- *Middle-range positional trait*: Middle power's statecraft is expressed by a complex combination of political positioning, economic status, and diplomatic proficiency in the current geopolitical hierarchical order
- *Distinct geographical trait*: With the unique resources and capabilities enabled by its geographical space, the middle power actively engages with its neighboring state actors
- *Normative belief trait:* The middle power believes it can bridge the gap between the superpowers and the lower-tier powers, with the intention to provide peaceful stability and collective security and economic growth within the system of states that it belongs to.

[2] Gilley 2012

[3] Shin 2015

[4] Cooper and Dal 2016

[5] Erskine 2022

Erskine further argues that the traditional middle powers, as conceptualized and formulated in the 1970s in the context of the post-WWII (e.g., Cox[6]), are no longer adequate for the realities of the twenty-first century. Holbraad[7] posits that middle powers are the nations that strive to use their geographical and economic resources to cooperate with the greater powers with the hope to join their ranks in a not-to-distant future. According to this viewpoint, middle powers implicitly admit and support the hegemony of leading nations and align with the hierarchical order, one that is led by the great powers, followed by the middle powers and trailed by the smaller powers. Krasner[8] contends that this normative view of sovereignty is a form of organized hypocrisy.

In today's realities of the new world order, Erskine[9] postulates that middle powers, in pursuing their national interests with other nations, now attempt to find a *collective advantage*. They would assertively nurture a stewardship strategy in adapting their historical heritage to the new realities that include a complex mix of great power competition, power politics, and multipolarity. Furthermore, a middle power could be regional, showcasing power disparity within a geopolitical space. Alternatively, it could advance strategic alliances to promote a regional or global rule-based order. Erskine[10] cites the creation of the Quadrilateral Security Dialogue between Australia, India, Japan, and the United States (QUAD) is an example of the last two nations attempting to assert themselves as global actors in geoeconomic resiliency and geopolitical security.

In this paper, we propose a three-factor framework to expand the new perspective of regional middle powers. We will next apply this framework to assess Vietnam's bamboo strategy as it steadfastly rises to the rank of regional middle power in East Asia.

4 A Three-Force Framework for Understanding the Regional Middle Power Concepts

By its very nature, geopolitics focuses on the geographical factors that affect world politics and international relations. Gray[11] asserts that geography is invariably the most permanent fundamental factor dictating foreign policy of states. The extent to which a nation would rise to a regional middle power status would depend heavily on three factors: spatial proximity, historical heritage, and factors that are exogenous to the state but are sufficiently forceful in the shaping of international and regional relations.

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[6] Cox 1989

[7] Holbraad 1971

[8] Krasner 1999

[9] Erskine 2022

[10] Ibid.

[11] Gray 1977

Spatial Proximity

With climate change and food security in the backdrop, the political effects of geography have become more critical in the eyes of national leaders. At the regional level, neighboring states formulate international relations strategies based on the perceived importance of land territory and territorial waters in correlation with national interests and security. States look at borders as economic channels to accomplish their economic, political, cultural, and military objectives. They form regional alliances to mutually boost their economies. They also take advantage of the geographical proximity to flex their competitive advantage. When a country has a neighbor that is significantly stronger in land, resources, cultures, and technology, it would face a tyranny of geography due to the permanent presence of power asymmetry.[12] Womack[13] postulates that, in an asymmetric relationship, the perspectives of the states are indeed different based on the power difference. The weaker state likely perceives that it was more at stake than its stronger counterpart and, thus, seeks to reduce its vulnerability through the preservation of its sovereignty and economic resilience.

In the physical world, Garrity[14] revisits the concept of sea power in the age of Eurasia. Gresh[15] insists that, in an era of increased global competition and yet the growing unification of maritime use between Asia and Europe, space (lands, rivers, and seas) would become remarkable means to exercise geoeconomic powers.

With the rapid pace of digitalization of the world economy, the industrial revolution 4.0 seems to only intensify power asymmetry.[16] Nations that are able to take advantage of the technological disruption would accelerate its geopolitical power, to include the possibility of creating a new digital diplomacy landscape with social media.

Historical Heritage and the Kinship System

Each nation has its own history, and it formulates its international relationships (political, economic, and trade) as a continuation of historical ties with their counterparts. State actors either formulate strategies based on ancient or recent memories, those that seem to matter them most, or on the collective memories. The effect of colonialism in the nineteenth and twentieth centuries still haunts many nations in East Asia. The horrors of the world wars are still being remembered across the world.

[12] Thayer 2011
[13] Womack 2016
[14] Garrity 2021
[15] Gresh 2020
[16] Bjola 2018

Agnew[17] talks about the time-space compression as time and space are the fundamental contexts of all historical experience and help contextualize political behavior and international relations. Space matters tremendously in determining the territory-specific patterns of economic development and geographical culture, whether they are unique or similar to those of their neighboring states. However, he further argues that relentless technological progress leads to an increasingly homogenized global space in that, in the long term, location would be significantly less critical, materially or culturally. On the other hand, time as expressed in terms of the pace a state can accelerate toward a stronger geopolitical power would transcend the power of space. As neighbors, history has shown that, for the sake of national security, states either form alliances or engage in territorial disputes. In that regard, states that are conscious of their relative positioning within the geopolitical sphere develop a keen appreciation of power asymmetry and disparity, determine their desired position in the geopolitical zone, and allocate national resources accordingly.

External Driving Forces

The recent rise of authoritarian leadership around the world has resulted in an increase in the intensity and frequency of exercise of power of stronger states over weaker ones. This constitutes an exogenous domino effect beyond national boundaries. In addition to the permanent geographical factor, there are exogenous factors that invariably influence the shaping of economic statecraft. Data compiled by WIPO for its annual Global Innovation Index (2022) show little change in the composition of the most innovative economies, while a few countries have reinforced their regional positions.

The recent decision by leading nations to move their industrial productions out of China is an example of a double opportune event for Vietnam. With the disruption of the global supply chain, many multinational corporations from Japan, the United States, and the European Union have taken steps to move some of their factories to Vietnam. As if luck can strike more than once, the US-China trade war intensified under the Trump administration which has triggered an increase in Chinese FDI to Vietnam.

However, the desire of multinational companies to establish new factories in Vietnam and elsewhere outside China such as India would take a significant amount of time and resources. It has taken China decade-long efforts to develop necessarily the skill set and fabrication capacity. The events triggered by forces that are out of the control of Vietnam have nevertheless created an opportunity for the emerging

[17] Agnew 2001

nation to eventually catch up with China in producing quality products and competitive prices.

Other external factors could simply be driven by natural forces, ranging from depleting natural resources to man-made conflicts that affect the global and national political, economic, and social landscapes and thus the ability of a nation to adapt its economic, social, and political actions to defend its national interests. The deployment of China's Silk Road strategy and its maritime expansion has elevated Vietnam as a necessary alliance for the East Asian nations.

The three factors listed above appear to be consistent with, but different from, Blanchard and Ripsman's[18] concept of "stateness." Their political theory of economic statecraft is anchored in the notion of *autonomy* (i.e., the ability of a nation to make its own decision when facing domestic opposition), *capacity* (i.e., the aptitude to employ incentives or sanctions to those that matter to national interests), and *legitimacy* (i.e., the capability to rally disaffected domestic groups).

Their concept of "stateness" seems to give more weight to the importance of domestic convergence. The three-factor model presented here would emphasize more on the factors – domestic and international – that would influence the determination of the rising middle power statecraft.

We argue that it is the spatial proximity and the historical heritage that provide the legitimacy of the nation's statecraft. In this context, legitimacy also reflects the constraints of sovereignty of the rising middle power. Instead of adopting a dogmatic approach to sovereignty, the middle power would constantly monitor the impacts (positive and negative) caused by these factors and attempt to translate them into opportunities or costs. In order to maintain its autonomy, the rising middle power would seek to demonstrate its continuing relevance within its circle of influence by orchestrating a complex web of international relations. Using its growing economic capacity, the middle power would use their many areas of national strengths and weaknesses to shape the most favorable networks of international relations *within* networks of international relations. The first strategic goal would be to bridge the gap between strategic partners and between the stronger powers and the weaker powers.

5 Vietnam's Statecraft in the Three-Factor Framework

In this section, we apply our three-factor framework to understand the shaping and development of Vietnam's geoeconomics.

[18] Blanchard and Ripsman 2008

Spatial Proximity: The Chinese Factor

With a shared border of more than 1306 km (811 miles), Vietnam has an entangled relationship with China, its political and economic powerhouse neighbor. The two economies share a resembling political system and have had century-old trade exchanges. On the one hand, and for the last 30 years, Vietnam has greatly benefited from the spillover effect as it has received substantial investments from many multinational corporations (MNCs). With established production centers in China, these MNCs find Vietnam to be a logical extension of their manufacturing facilities to utilize the still-inexpensive labor costs and the close proximity to the Chinese supply chain network. As a neighbor of Guangdong Province, the largest manufacturing province in China, Vietnam has become an important adjacent production hub. China's major seaports Fangchenggang, Behai, and Basuo on the western coast of Hainan island have been Vietnam's main gateways to the world. Thanks to this close partnership, Vietnam has swiftly made China its top export market,[19] providing unique opportunities for the developing economy to raise its living standards.

The China-Vietnam relationship continues to exhibit a geoeconomic context like no other. As neighbors, the century-old friend-and-foe relationship has recently taken a new turn with the relocation of some manufacturing centers, notably the moves by Samsung and Apple Inc. in 2018 and 2019, respectively, to assemble smartphones, tablets, and earbuds. One of the much-publicized rationales is for Samsung and Apple to reduce the risks of relying only on China for their flagship products. Yet, as many electronic components of the products assembled in Vietnam still come from China, the competition-cooperation dilemma is in full play, resulting in complex import-export taxation policies between the two economies.

On the other hand, Vietnam has cautiously welcomed China's offer to help the country's effort to develop its national infrastructure. To enhance its competitiveness, the Vietnamese government claims that it needs to raise more than US$605 billion for the improvement and development of roads, rails, air and sea ports, water and electricity, and telecommunications. It has explored the possibility of securing loans from the China-led Asian Infrastructure Investment Bank to fund projects that the Chinese have competed successfully overseas: coal-fired power plants, steel mills, high-speed highways and railways, and 5G technologies. However, the Vietnamese government is aware of the potential risks involved in doing business with China. They have had some concerns regarding the quality of work provided by Chinese contractors in the past, which may impact their decision-making going forward.

Although it has followed many of the economic, political, and social policies of its influential neighbor in the North, Vietnam has never adopted China's one-child policy (1980–2021) seen as a policy to poverty alleviation. Instead, the Vietnamese government has limited its role in promoting the concept of an ideal family as one that consists of two children and focused on attracting FDI in all sectors of the

[19] OEC 2022

economy. The population has grown steadily since 1987, reaching an estimated population of 91 million in 2021, providing a young and better nourished labor force to an economy that has been able to modernize its agricultural sector, expand its industrial base, and establish a solid foothold in the service sector, in particular, tourism and IT outsourcing.

Historical Heritage and the Kinship System: The Chinese Factor, Again

In Vietnam, there is a growing concern among citizens about the relationship with China, particularly due to the tensions surrounding the South China Sea dispute and the purchase of land by Chinese investors in key locations across the country. This has led to a decline in the overall sentiment toward China among the Vietnamese population.

China and Vietnam have a complex history of disputed borders and economic dependence. Vietnam has a long and proud history of hard-fought independence, and some Vietnamese people may still be concerned that China has territorial ambitions over their country due to ancient China's domination that lasted almost ten centuries (111 BC–938 AD). The 1979 Sino-Vietnam border war, which lasted for 5 weeks, resulted in a border agreement that caused Vietnam to lose some land. China's territorial claims have contributed to political and military tensions with Vietnam, as well as other Southeast Asian countries.

With this historical context, Vietnam feels the challenges of competing effectively against its Northern neighbor. At the time of this writing, Vietnam is far behind China in the seven economic instruments enumerated by Blackwill and Harris.[20] Consequently, it has to find an economic model that differs from that of China, if at all possible.

Facing the power asymmetry with China, Vietnam seems to have practiced *geopolitical dualism*. On the one hand, and as discussed later, Vietnam intensifies economic and trade exchanges with China. While the United States is Vietnam's largest export market in 2021, China is its largest trading partner. The Southeast nation relies substantially for raw materials and machinery from its northern neighbor for its industrial base. The spatial proximity with China has been benefiting Vietnam. As a consequence of the disruption of the global production chain, MNCs currently having their production facilities in China have decided to relocate some of their manufacturing projects to Vietnam.

Vietnam has been able to expand its trades with two key allies during the war time – China and Russia. Both partners have served as main providers of raw materials and inexpensive technology transfer as well as substantial markets for its steady increases in production and services (e.g., agri- and aqua-products, coal, and

[20] Blackwill and Harris 2016

oil). In parallel, Vietnam has also taken advantage of its image of a stable government structure to fully engage in the world economy (with many free trade agreements (FTAs) and the accession to the WTO in 2007). Such a geopolitical strategy has made the United States and EU to become among top economic partners slightly after China. In 2019, the United States became Vietnam's top export destination, surpassing China and Japan. In addition, Vietnam offers market access to ASEAN free trade bloc with more than 650 consumers.

External Factors: Dualism in a Polarized World

Within the geopolitical space of East Asia, Vietnam showcases a unique power disparity through its proximity to China, with its willingness to restore unipolarity toward the "Middle Kingdom," and its complex contemporary history involving both China and the United States as both friends and foes.

Perhaps the most visible display of Vietnam's skillful statecraft was the visit of Vietnam's communist party secretary and the country's top leader, Mr. Nguyen Phu Trong, to China, on 20 October 2022, just a week after the third-term reelection of Chinese President Xi Jinping. In their communiques, China and Vietnam reiterated their "strategic community with a shared future." This is a statement from China in response to the decade-long offer by the United States to Vietnam, raising the US-Vietnam relationship to a "strategic partnership." As Vietnam is in the whirlwind of the intensified tug-of-war between China and the United States, it takes a pragmatic strategy – dualism in a polarized world.

We will focus on two dimensions of this dualism: economic policy and national security strategy.

Since the implementation of the "Doi Moi" (Reform) policy implemented in the late 1980s, Vietnam has grown into a manufacturing hub for high-tech industry, particularly in the consumer electronic products. The country's exports of electronic products rose significantly to a record high of over $100 billion in 2021, equivalent to about 30 percent of its total exports, compared to less than $1 billion 20 years ago. This achievement has demonstrated that an increase in the complexity of the products Vietnam can make is the driver to long-run sustainable development to becoming an upper middle-income status. Harvard's Atlas of Economic Complexity ranked Vietnam 93rd in 2000 and climbed up to 52nd out of 133 countries in 2020, revealing the rising trend of the country's ability to produce high value-added products. As economic growth has declined 2 years in a row to 2.58 percent in 2021,[21] the party has reaffirmed in its 13th national meeting in May 2022 its commitment to recover from the pandemic crisis.

The spatial proximity with China and the China-US tension, as a driving exogenous force, has benefited Vietnam. Multinational companies have selected Vietnam

[21] World Bank 2023

as one of their preferred alternative or complementary options to their manufacturing facilities in China. Japan and the EU have established fiscal incentives for their national companies to diversify their production factories out of China. Given the experience learned from its factory in Jiaxing, China, Denmark's LEGO Group inaugurated its $1.3 billion and first carbon-neutral factory in Binh Duong Province (South of Ho Chi Minh City). Even Chinese firms are moving their factories to Vietnam for both political and economic reasons. The "Made in Vietnam" brand seems to gain traction as an alternative to Chinese-made products. And labor costs remain lower than that of China, while the spatial proximity between the two countries would minimize logistical costs. According to Statista,[22] 11 out of the 20 top manufacturing-based FDI in the first half of 2022 in Vietnam are from Chinese companies (e.g., Trina Solar's panels, Autel's robotics and drones, HMT Xiamen's automobile airbags).

On the national security front, Vietnam reiterates its "4 No's" principles at the 19th Shangri-La meeting in October 2022 in Singapore – no military alliance, no affiliation with one country to counteract the other, no foreign military base in the Vietnamese territory to act against other countries, and no force or threatening to use force in international relations. Perhaps as a lesson learned from successive century-long conflicts, Vietnam's policy is to remain neutral. This policy has been recognized by multinational corporations as a necessary condition to move some of their factories to Vietnam and, as a consequence, has successfully helped Vietnam, since the polarization of the world powers, in particular between the United States and China, the sustained political stand is not to side with a single power.

As Vietnam moves forward with its regional and global integration, it is steadily finding creative ways to comply with requirements set forth by international bodies (WTO, ASEAN, etc.), while global economic and financial institutions praised Vietnam for its economic success.

6 Middle Power as a Good International Citizenship: Vietnam and Other Asian Nations

Vietnam and other nations in Southeast Asia (SEA) and East Asia have been pivoting around China, the world production and trading center. As underdeveloped nations, and by virtue of regional collaboration and competition, these countries have adopted similar geoeconomic strategies – promoting export-driven industries, providing incentives to attract foreign direct investments (FDI), encouraging knowledge transfer, and accelerating global supply chain integration.

Given favorable conditions in the three-factor framework, Vietnam is trying to portray itself as a good international citizen, working within its networks of state actors to preserve national sovereignty and to promote economic resilience.

[22] Statista 2022

Along with countries in the Pacific, Vietnam joined the Agreement for Trans-Pacific-Partnership (TPP), a trade agreement originally signed in 2005 by four countries in the Pacific Rim: Brunei, Chile, New Zealand, and Singapore. The United States initiated talks with the earlier TPP members in 2008. Seen as a centerpiece of his geostrategy in Asia, President Obama saw the alliance with 12 economies of the Pacific Rim that collectively account for more than 40 percent of the world's GDP, as a means to create domestic jobs by expanding US trade abroad while lowering domestic consumer prices. Furthermore, TPP – with China strategically sidelined – would have helped the United States position itself as a renewed geoeconomic power in the Far East, counterbalancing China.

But, critics of the TPP argued that this massive trade agreement would force American companies at home to lower wages to remain competitive, precipitating US decline in manufacturing, and bilateral trade negotiations would serve US interests better. As the United States withdrew from TPP in 2017 under the Trump administration, Japan took the lead to keep the trade agreement alive under a new acronym: CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership). With China interested in joining the pact, the United States, currently under the Biden administration, has expressed the willingness to reconsider joining the TPP with the condition to include more labor and environmental provisions. The uncertain future of the CPTPP and its effectiveness have forced Vietnam and other members to look for alternative ways to push their economic agenda forward.

Being a peripheral nation, Vietnam outlines a geopolitical strategy to protect national sovereignty, peace, and stability. Seeking to avoid at all costs any military future conflict, Vietnam reinforced its peace-seeking position in 2019 by re-affirming its "four-zero" geopolitical principles: (i) do not engage in military alliances; (ii) do not take side in international conflicts; (iii) do not allow any foreign military forces to use Vietnam as a base to fight against another country; and (iv) do not use military power in international relations.

Although not explicitly discussed in public venues, it seems that Vietnam is seeking to achieve a double resilience objective. To join in the global effort of limiting the risks related to supply chain disruption, Vietnam attempts to position itself as a reliable and promising alternative to China's production powerhouse. In parallel, it seeks to reduce economic and political dependencies on foreign economies affecting its domestic economy. In extending its three-decade-long effort, mostly led by the private sector, to catch up and leapfrog through innovation, Vietnam is looking at implementing the concept of circular economy as a new geoeconomic instrument (Table 1).

7 Discussion: The Viability of the Bamboo Diplomacy

In this paper, we have attempted to conceptualize and analyze the formulation of statecraft of an emerging middle power using a three-factor analytical framework. Recognizing that only a handful of nations have adequate leverage on economic

Table 1 The three-factor framework for understanding emerging middle power statecraft

3-Factor statecraft	Vietnam's rise as regional middle power: bamboo diplomacy
Spatial proximity	Neighbor's' collaboration: Economic co-existence through collaborative supply chains and competition under power asymmetry (China's availability of raw materials and superior production technologies)
	Neighbor's' threat: Forced alliance or territorial disputes under the "tyranny of geography"
Kinship heritage	Leadership's perspective on geo-culture: Emphasis on similarities/kinship (Confucianism) and shared political ideology (communism)
	Secular national security rivalry: Sustained collective memory of colonialism with ten centuries of love-hate relationship with China and with France and the United States
	Complex international relationship building: Rhetoric alliance with China while cautiously forge security cooperation with distant powers (United States, Australia and Korea, and soon EU)
Opportune circumstances from external forces	World's supply chain disruption: Positioning as an alternative to manufacturing hub in East Asia
	Superpower rivalries: Firm principles of non-alignment (4 no's) and flexible policies, strategies, and tactics (multi- and bilateral alliances seeking balance of powers and conflict avoidance)
	Intensity and frequency of great powers' exercise on less powerful nations: Geoeconomic resiliency and geopolitical security through economic collaboration and military alliances with both greater and lesser powerful nations
	Good citizenship with peripheral nations: International accommodationism through intensification of strategic partnerships, from weak ties to stronger ties

tools to engage in geoeconomic cooperation or coercion, we argue in this chapter that there are other economic means that developing countries could explore to overcome their power limitations. In particular, there are opportunities for rising middle powers to assert themselves as a potential actor in the regional, or even global, scene. We contend that this engagement process could be framed in a three-factor model. Geopolitical strategies and economic statecraft are anchored in three distinct but interrelated factors: (1) Spatial proximity matters as international relations with neighboring countries are of paramount implications affect either positively or negatively the economic, social, cultural, and political life of a nation; (2) kinship heritage can affect a nation's collective mindset and the current leadership's choice of policies or can prevent the nation from rationally interacting with other nations; and (3) fast, oftentimes unpredictable, exogenous events, either man-made or natural, that are beyond the control of a nation may affect many domestic issues and forcefully alter its geoeconomic policies.

In the East Asian context, we discussed how Vietnam has been trying to defend its national interests through a pragmatic approach known as the "bamboo strategy." As a plant, bamboo is a fast-growing perennial, with stems that are hollow between the rings. It is flexible, elastic, and resilient. Using this metaphor, a bamboo strategy would exhibit the same strength of the plant it carries the name:

- Strong roots (historical traits)
- Continuous growth (spatial expansion)
- Strength and resilience through flexible adaptation (external events)

From a statecraft perspective, the bamboo diplomacy is expressed in terms of dualism: firm rhetoric principles and adaptable policies and tactics.

As a firm principle, the neutral position (4 No's) seems to have worked well for Vietnam. It has helped Vietnam avoid military conflicts over the last three decades. More recently, it was left alone in the world reaction to the Russia-Ukraine conflict. In spite of the fact that Vietnam was among a handful of countries that did not join the global movement to sanction Russia's invasion, there has not been any consequential criticism about its decision. International trade seems to even accelerate between Vietnam and Western countries, Japan, Korea, and China. As a reaction to the shortage of supplies due to the pandemic and the Russia-Ukraine conflict, Vietnam quickly positions itself as an additional hub of manufacturing and has identified itself as a potential player to ensure food security around the world.

Most recently, as a signal of its commitment to national security, Vietnam hosted its first international defense exposition on December 8–10, 2022, in Hanoi. With more than 170 defense firms from 30 nations showcasing their arms, both Russia and US weapon makers were present at the exhibitions, attempting to be part of Vietnam's new effort of diversifying and modernizing its defense capability. VietTel, Vietnam's largest defense company, also displayed its surveillance systems to potential buyers.

The apparent success of Vietnam's bamboo diplomacy has earned recognition among many of the nations that it has some bilateral interests. Indeed, Russia and China continue to reaffirm their solid partnership with Vietnam, despite some push-backs from the Vietnamese side. Vietnam has shown its hesitancy in participating in military drills with Russia and has announced it would equip non-Russian arms for its national defense. It also engages open discussion with the United States to "diversify" its weapons systems, especially in maritime warfare, a move that would certainly irritate its Northern neighbor. In December 2022, at the summit in Brussels, Vietnam as a key ASEAN member assumed a key role in devising a reliable supply chain between ASEAN and the European Union. As the US's ninth economic partner, Vietnam is keen on President Biden's plan to visit the country, promoting their bilateral relations to strategic partnership. Such a state visit would certainly not please Vietnam's two long-time partners – Russia and China.

Vietnam has recognized the importance of building alliances with neighboring countries and major powers to address challenges in the region. With China exerting power, Vietnam has sought to respond through peaceful means. Recent developments have presented opportunities for Vietnam to pursue this strategy, including the pushback China is facing from other countries. Vietnam's approach has helped to reduce tensions and maintain economic ties with its northern neighbor.

The bamboo strategy in the current VUCA (vulnerability, uncertainty, complexity, and ambiguity) world seems to allow Vietnam to move from a conventional perception of peace, a static position of inactivity, to a proactive process at all aspects – diplomacy, trade, and investment. We also argue that as Vietnam keeps securing strategic partnership with key trade and strategic partners, the network would be so densely intertwined that it would achieve its middle power objective – charting a culture of peace so that it could focus on economic development and growth. We argue that as Vietnam keeps securing strategic partnership with key trade and strategic partners, the network would be so densely intertwined that it would achieve its middle power objective – charting a culture of peace so that it could focus on economic development and growth.

Nevertheless, Le[23] reports that a segment of the Vietnamese leadership has expressed concern about the negative consequences of the bamboo strategy. By trying to not to unilaterally side with either China or the US to preserve its autonomy, Vuving[24] claims that Vietnam is walking a tightrope between the superpowers, and the rope could become too thin to walk if the level of conflicts between these powers reaches an untenable threshold. If this situation becomes real, we argue that Vietnam could put itself in a precarious situation, not knowing which end of the rope is the most secure place to protect its national interests or when all forms of alliances could fall apart. Nguyen[25] would further argue that the language of neutrality embedded in the implementation of the bamboo diplomacy is just a means to refrain from criticizing or condemning the injustices caused by close and more powerful partners.

A plausibility probe of our proposed three-factor framework is to question the continued viability of the bamboo diplomacy to ensure national sovereignty and secure economic prosperity.

We consider here two lines of arguments. Krasner[26] contends that, throughout history, national leaders have invariably been motivated by a desire to stay in power, and if their national interests are at stake, they might choose not to honor international legal sovereignty. Krasner[27] coined the term "organized hypocrisy," a situation in which long-standing norms are frequently violated, and principles and rules do matter only if they consider logics of consequences as well as logics of appropriateness. Under the presence of hegemony of great powers, it seems that the bamboo diplomacy could help the lesser power to find a niche statecraft to affirm self-identification and gain regional and international recognition. We contend that the bamboo diplomacy of the middle power would remain viable and effective as long as its diversification of multilateral ties activities does not negatively impact the organized hypocrisy of greater powers.

Another line of argument about the soundness of the bamboo strategy is to borrow Marquis de Condorcet's paradox in social choice. Condorcet[28] argues that a safe

[23] Le 2016

[24] Vuving 2022

[25] Nguyen 2022

[26] Krasner 1999

[27] Krasner 1999

[28] Condorcet 1785

choice under the presence of multiple selection criteria would be one that would meet two conditions: concordance and discordance. The condition of concordance would be met if the majority of the selection factors are in favor of the chosen action. The condition of discordance would be met if there is no single criterion that is critically against the chosen action. As such, if the wide spectrum of economic policies can collectively help promote and achieve mutual benefits, and if only if none of these policies runs violently against the interests of the greater powers, the bamboo diplomacy would likely work and survive.

As shown in Table 2, there are clear differences in the formulation of geopolitics between China, the United States, and Vietnam. But, Vietnam's statecraft appears to fit in with those of the United States and China, one that seems to act as both a buffer and a bridge between the two superpowers.

8 Conclusion

As many nations in the world are adjusting their strategies in response to China's actions, countries located in the vicinity of the South China Sea may feel the impact of China's increasing presence in the region. It can be difficult for these nations to resist China's influence. Among these peripheral countries, Vietnam stands out as an emerging regional middle power. With its geographical proximity and cultural similarities with China, Vietnam is perceived as a nation that could bring some economic, political, and military stability to the region. The heightened tensions between China and the United States significantly affected Vietnam's economic statecraft. This economic statecraft is shaped by three major forces: historical heritage, geographical proximity, and the emerging impacts triggered by external international forces.

Table 2 Differences in statecraft – as identified from the perspective of spatial proximity, historical heritage, and exogenous factors

United States (as superpower)	China (as superpower)	Vietnam(as an emerging regional middle power)
Geoeconomic power from knowledge creation	Geoeconomic power from efficient massive production	Fill in the void in the world supply chain
Science and technology	Leapfrogging knowledge creation	Strategic leverage among superpowers either by own or through alliances (ASEAN) – Bilateral vs. multilateral
Social sciences (including business/finance)	Knowledge building and creation	Knowledge building (190 k students studying abroad, majority in the United States)
Immigration as a source of knowledge creation/import and innovation	Political stability	Political stability

To navigate between the hegemony of the superpowers, Vietnam has its own version of bamboo diplomacy, characterized by the tyranny of geography[29] and the historical heritage and kinship vis-à-vis China. The combination of firm neutrality principle and flexible strategies and tactics to preserve national cultural identity and diplomatic identity seems to have worked in a polarized world. In theory, choosing neutrality and seeking alliances to secure national interests and security seem to be rooted in the rhetoric of international justice and peace. But, for all practical purposes, the implementation of bamboo diplomacy (see Table 1) appears to be more on the pragmatic side of diplomacy, preserving the status quo or balance of organized hypocrisy. While Nguyen[30] questions the theoretical foundations of the bamboo diplomacy as a noble means to achieve international justice and harmonious peace, Do[31] already claimed that thanks to its bamboo strategy, Vietnam has successfully diversified its relationships with other major powers, such as the West, Japan, Australia, Korea, and ASEAN, in order to achieve a more balanced position in the region. This has enabled Vietnam to reduce its dependence on any one country like China and better protect its interests (Table 3).

The effectiveness of Vietnam's current geoeconomics remains to be seen in the future. On the one hand, Vietnam continues to nurture a stable relationship with its two long-bonded alliances, China and Russia, through increasing economic cooperation. On the other hand, it has stepped up its hedging strategy through comprehensive multi-tiered bilateral and multilateral alliances. It also has steadfastly moved forward with its military modernization with Western technologies. To date, Vietnam has been able to stay away from armed conflict, and its integration into the world economy is progressing better than that of its neighbors. We argue that this pragmatic strategy might work as long as it does not affect the balance of power through a sustained form of organized hypocrisy, or it might not reach an

Table 3 A synopsis of Vietnam's bamboo diplomacy

Bamboo features	Bamboo diplomacy and statecraft
Strong roots	Stable single-party political system
Fast growing, slender grass	Fast-growing economy
Flexible and elastic	Multi-tiered bilateral and multilateral alliances
Hollow inside between the rings	Omni-directional engagement with great and middle powers and extending diplomatic allies and economic cooperation with neighboring countries
	Maintain ambiguous positions (e.g., toward Russia in R-U conflict)
Resilient against strong winds	Dualism in action: Coopetition (cooperation/competition)
	Nurture a stable relation with its two key allies (CN and RU)
	Modernize military readiness with Western technologies (incl. US)

Source: Table created by author

[29] Thayer 2011

[30] Nguyen 2022

[31] Do 2016

irreversible level of irritation from its influential partner states. For now, Vietnam seems to be in the honeymoon phase with the world still trying to figure out a new economic world order. It should take advantage of this historical opportunity, as long as it lasts.

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Establishing Multilateral and Regional Rules on Digital Trade: The Role of Japan and Middle Powers

Hideyuki Miura and Shujiro Urata

1 Introduction

The growing awareness of the importance of data for economic growth has prompted many countries, especially developed ones, to establish a free, open, and rules-based environment for digital trade. In contrast, many emerging countries, particularly China, have pursued protectionist measures for economic and national security reasons. The condition of differing approaches to data governance is consequently posing many challenges in the international society. The World Trade Organization (WTO) has made several attempts to establish multilateral rules for digital trade; however it has not been successful yet. Instead, digital trade rules for governing the control, storage, and transfer of data have been adopted regionally or bilaterally through free trade agreements (FTAs) or digital trade agreements (DTAs). One of the most innovative digital trade rules was adopted by the Trans-Pacific Partnership (TPP). After the United States' withdrawal from the TPP, Japan led the remaining TPP members to establish the Comprehensive and Progressive Agreement on Trans-Pacific Partnership (CPTPP) with the support of other middle powers, such as Australia. In addition, as the host nation of the G20 Summit in 2019, Japan successfully launched the Data Free Flow with Trust (DFFT) initiative to promote discussion on a multilateral framework for digital trade rules. In the absence of US involvement in the Asia-Pacific economic order due to its withdrawal from the TPP,

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the United States has recently sought to establish a new digital trade framework in the Indo-Pacific with middle power like-minded countries, like Japan and Australia.

Digital trade is a relatively new concept that has emerged in the last decade.[1] However, digital trade still has no unified definition, and its fundamental concept remains indeterminate.[2] Although the concept of digital trade remains ambiguous, there is a growing consensus that it encompasses digitally enabled transactions of trade in goods and services which can be either digitally or physically delivered involving consumers, firms, and governments.[3]

In light of these issues and developments surrounding digital trade, we analyze the possible roles of Japan and other middle powers to contribute to the establishment of multilateral digital trade rules by considering the following questions: (1) why are digital trade rules important; (2) how do developed countries perceive data protectionism in emerging countries, especially China, and how have they responded; (3) how and why are middle powers, particularly Japan, taking the initiative to form multilateral and regional digital trade rules with like-minded major powers, such as the United States and the EU, in response to US-China geoeconomic competition; and (4) what are effective strategies for Japan and middle powers to facilitate discussions about establishing a multilateral digital trade rule. The remainder of this paper is structured as follows. Section 2 explores divergent approaches to data governance and data regulations in China and emerging economies. Section 3 analyzes the formation of a multilateral and regional digital trade rule. Section 4 examines a new phenomenon arising from the formation of rule on digital trade in the Asia-Pacific and Indo-Pacific Region. We then present our conclusions and provide policy recommendations in the final section.

2 Divergent Approaches to Data Governance in China and Emerging Economies

Current regulatory approaches to cross-border data flow differ considerably between major countries.[4] While some countries emphasize the significance of cross-border data free flow, which enhances productivity and innovation, some countries argue for the necessity of a legal framework that protects privacy and data, intellectual property rights, and national security. There is a large gap between the ideas of major countries and regions, such as the United States with its policy of liberalizing digital trade, the EU with its emphasis on reliability and personal data security, and China with its focus on sovereignty and support for developing countries. In this section, we will review the data governance of China and other emerging economies

[1] Aaronson 2016a

[2] Azmeh et al. 2020; Aaronson and Leblond 2018

[3] Monteiro and Teh 2017; López Gonzalez and Jouanjean 2017; López Gonzalez and Ferencz 2018

[4] Kuner 2013

which have a strong sense of national security regarding data and consider what challenges it poses for digital trade rule-making in terms of cross-border flow of data in the international society.

China's data governance policy is based on state control of data and aims to impose restrictions on foreign companies from freely using domestic data.[5] There are currently three fundamental data protection laws in China: The Cybersecurity Law, the Data Security Law, and the Personal Information Protection Law which provide the legal foundation for data governance in China, all of which allow broad state direction.[6] First, the Cybersecurity Law came into effect in June 2017. The law aims to secure China's national sovereignty, security, and public interest in cyberspace. Its scope is wider than the EU's General Data Protection Regulation (GDPR), which focuses on personal data protection.[7] The most distinctive feature of the law is that operators are obliged to store the personal and critical data collected in China. Moreover, they are also required to install a data server in China. Second, the Data Security Law, which introduced security requirements for data activities conducted within mainland China, came into effect on September 1, 2021. The Data Security Law is aimed at regulating the collection, processing, control, and storage of data involving national security, business secrets, and personal data.[8] Moreover, it classifies data based on its importance to the state's economic development, national security, and public interest while also providing additional safeguards for critical data. The Data Security Law also imposes a set of obligations on entities and individuals who conduct data activities. Entities and individuals who fail to comply with the requirements of the law may face potential penalties and sanctions, including demands for reparations, warnings, forfeiture of illegal gains, and closure of businesses, as well as the revocation of business licenses and other applicable criminal, administrative, or civil liabilities. Third, the Personal Information Protection Law came into force on November 1, 2021. Many of its provisions are inspired by the EU's GDPR.[9] The law, which contains 70 articles, is China's first comprehensive law regarding the protection of personal data. It would apply to the processing of personal information of individuals located in China conducted outside of the country and would encompass Chinese and foreign businesses as well as other individuals under certain circumstances, including those who provide products or services to individuals located in China or who analyze and evaluate the behavior of individuals located in China. The Personal Information Protection Law proposes more expansive data localization requirements for critical information infrastructure operators than those contained in the Cybersecurity Law, which currently requires critical information infrastructure operators to store personal information collected or generated in China within the country.

[5] Aaronson 2018; Cory 2022

[6] Kokas 2021; Ishimoto et al. 2022

[7] Sack 2018

[8] Cory 2022

[9] Ishimoto et al. 2022

China's measures are more restrictive than those in other countries, as it imposes data retention obligations and regulates the transfer of important data and personal information data abroad. There is an analysis that China's Personal Information Protection Law is similar to the EU's GDPR in that it gives Chinese consumers the right to access, correct, and delete their personal data gathered by businesses[10]; however, detailed contents of those laws are different.[11] China's Personal Information Protection Law and the GDPR share the similar principle of obtaining consent for the handling of personal information and provide for certain exceptions. However, while the GDPR provides for exceptions to obtaining consent in cases of "legitimate interests," the China's Personal Data Protection Law does not provide for such exceptions. In addition, in the context of the regulation of extraterritorial provision of personal information, while the GDPR provides an exception for provision based on an adequacy decision, there is no such exception in the China's Personal Data Protection Law. Moreover, under China's Personal Data Protection Law, operators that meet certain requirements are obligated to store personal information in China, but there is no such provision in the GDPR.

China launched the Global Initiative on Data Security (GIDS) in 2020 in order to safeguard global data and supply chain security, promote development of the digital economy, and provide a basis for international rulemaking for data.[12] In a 2020 speech on the GIDS, Chinese foreign minister Wang Yi explicitly advocated against digital protectionism and data localization while also championing the centrality of sovereignty and the state's ability to manage the Internet and protect data without restrictions.[13] These explicitly indicate that China has ambitions to extend its own way of data governance to other countries.

Other emerging countries have also seen an increase in data regulations. According to the Digital Trade Restrictive Index published by the European Institute for International Political Economy, China has the strictest domestic regulations, followed by Russia, India, Indonesia, and Vietnam.[14] Regulations have been tightened in India, following the example set by China. The Indian government released its draft Personal Data Protection Bill in July 2018. India has never had a comprehensive data protection bill; however, the published Personal Data Protection Bill governs the treatment of personal data, which is defined as personal data that can be identified either directly or indirectly.[15] The draft law states that at least one copy of personal information should be stored on a domestic server or data center, and critical personal data may only be processed in India. However, India withdrew the Personal Data Protection Bill in August 2022, and it released its Digital Personal Data Protection Bill. The new bill offers a mixed bag for privacy with some

10 Chen and Zhou 2022

11 JETRO 2022

12 MOFA of PRC 2020

13 Cory and Dascoli 2021

14 ECIPE 2018

15 Parsheera 2022

requirements for companies to receive individual "consent," correct inaccurate personal data, and protect data rights alongside concerning provisions for government data access.[16] Vietnam, which participates in the CPTPP, is also implementing data-related regulations. In Vietnam, the CPTPP rules have been in effect since January 2019, and the Cybersecurity Law came into effect in the same month. This law stipulates that data, including personal information, should be stored in the country and that data should be disclosed when requested by authorities.[17] In addition, there are similar regulations of data localization in Brunei and Indonesia. It is possible that similar regulations will continue to develop in emerging countries.

The condition of differing approaches to data governance and data protectionist measures by China and other emerging economies has consequently posed a challenge to the international society, particularly developed countries. Such examples of issues include the security risks associated with setting up servers in within the target country and data centers in outside of the target country, potential software leakage due to mandatory source code disclosures, concerns that critical technical information such as research data may be stolen, the inability to veto data disclosure requests from the authorities, and the possibility that confidential corporate information may be diverted from the government to the private sector. In particular, China continued to engage in unfair trade practices, including the illicit acquisition and infringement of intellectual property rights, coercive technology transfer, censorship, and other restrictions related to the Internet and digital economy, resulting in several issues that could not be resolved through the existing international frameworks, even though China joined the WTO.[18] According to Azmeh and Foster, the Great Firewall which has served to filter and censor information from outside of China has made it difficult for IT firms in Western countries, such as Google or Facebook, to enter the Chinese market.[19] These regulations have helped Chinese IT firms grow, serving as digital industrial polies and enabling infant IT industries to catch up to Western IT technology. The Great Firewall has yet to be challenged under the existing WTO rules, despite numerous arguments to that effect.[20] Little progress was made in the 2000s regarding the rules and commitments regulating data protectionist measurements.[21] These challenges call for regulations concerning how international society control issues surrounding digital trade. In the next section, we will analyze how developed countries have attempted to counter these challenges through the formation of multilateral and regional digital trade rules.

[16] Sherman 2022

[17] Liu 2018

[18] USITC 2010

[19] Azmeh and Foster 2016

[20] Palmer 2010

[21] Meltzer 2014

3 The Formation of a Multilateral and Regional Digital Trade Rule

The Formation of Regional Digital Trade Rules

Since the adoption of the "Declaration on Global Electronic Commerce," which called for the establishment of a work program on e-commerce at the WTO Second Ministerial Meeting held in May 1998, a number of international forums such as the WTO, OECD, UNCITRAL, and APEC have discussed the legal disciplines or regulatory frameworks for digital trade. Due to the slow progress in updating international trade rules for the multilateral trading system, global governance of digital trade has gradually migrated to bilateral and regional frameworks.[22,23] For example, the US-Jordan FTA, which was signed in 2000, established the first e-commerce provision. Since then, a growing number of FTAs have incorporated specific provisions related to digital trade. Currently, two-thirds of the WTO membership is party to an FTA that includes such digital trade-related provisions.[24] Australia, the United States, and Singapore were the first to include an e-commerce chapter in their FTAs, followed by Canada, the EU, Japan, and South Korea.[25] The Economic Partnership Agreement (EPA) enacted by Japan also includes an e-commerce chapter, starting with the Japan-Switzerland EPA, Japan-Australia EPA, Japan-Mongolia EPA, CPTPP, Japan-EU EPA, Japan-US Digital Trade Agreement, and Japan-UK Comprehensive Economic Partnership Agreement (CEPA). The structure, content, and scope of each e-commerce chapter are strikingly different, as shown in Table 2. A number of e-commerce chapters include provisions for the elimination of customs duties, consumer protection, authentication methods, electronic signatures, and paperless trading, but provisions for data localization, cross-border data flows, and forced disclosure of source code are rare.[26] This section examines how the United States has led the way in the formation of high-level digital trade rules to counter digital trade protectionism measurement taken by emerging countries like China in mind and to promote US IT industries and companies.

The US government has consistently taken a positive stance toward promoting a data-driven economy. On July 1, 1997, Bill Clinton's administration issued a visionary policy statement entitled "A Framework for Global Electronic Commerce," which put forward the first set of global principles for ensuring cross-border data flow.[27] In this memorandum, President Clinton asserted that "for this potential to be realized, governments must adopt a market-oriented approach to electronic

[22] López Gonzalez and Ferencz 2018

[23] See METI 2017, "Addendum-3, e-commerce" for more detailed information.

[24] Willemyns 2020

[25] Herman 2010

[26] Willemyns 2020

[27] Clinton 2011

Table 1 Lobbying spending by IT firms and organizations, in millions of US dollars

Company/ association	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Google/Alphabet	5.16	9.68	16.48	14.06	16.83	16.66	15.43	18.37	21.74	12.54	8.60
Amazon	2.05	2.22	2.50	3.46	4.94	9.44	11.35	13.00	14.40	16.79	18.72
Facebook Inc.	3.51	1.35	3.85	6.43	9.34	9.85	8.69	11.51	12.62	16.71	19.68
Apple	1.61	2.26	1.97	3.37	4.11	4.52	4.67	7.15	6.68	8.41	6.65
Microsoft	6.91	7.34	8.09	10.49	8.33	8.49	8.71	8.66	9.59	10.26	9.46
eBay	1.71	1.63	1.56	2.24	1.56	1.56	2.15	1.82	1.65	1.32	1.17
Netflix	0.13	0.50	1.02	1.20	1.26	1.32	0.80	0.80	0.80	0.85	0.75
SalesForce	0.09	0.12	0.42	0.44	0.44	0.63	1.25	2.05	2.10	2.03	2.05
Alibaba	–	0.10	0.46	0.43	0.45	0.41	1.02	2.01	2.74	2.62	3.16
BSA	2.07	1.82	1.62	1.34	1.52	1.70	2.01	1.42	1.55	1.74	1.63
IA	–	–	–	1.60	1.56	1.44	1.20	1.20	2.60	2.83	1.48
ITIC	2.50	1.08	1.08	1.08	1.08	1.14	1.51	1.63	1.75	1.57	1.80

Source: Center for Responsive Politics, Influence and Lobbying

commerce, facilitating the emergence of a global, transparent, and predictable environment to support business and commerce." The Clinton administration used this framework to build a common ground for governing international data flow.[28] US IT firms remained competitive for some time but were gradually exposed to market competition in the late 2000s. Under the Bush administration, e-commerce chapters were included in the FTAs they signed.[29] Since the e-commerce chapters of early FTAs stipulated only the elimination of customs duties, consumer protection, authentication methods, electronic signatures, and paperless trading, they did not solve problems related to digital trade, such as data protectionism measures in emerging economies like China, which is described in Sect. 2.

In the absence of a clear venue for addressing these issues, US trade policymakers and IT firms increasingly saw the international digital trade regime as a suitable arena for creating binding international rules.[30] US IT firms and organizations have actively lobbied the US Congress, White House, and other policymakers to establish international trade rules governing digital trade. The political influence and lobbying power of IT firms and affiliates are increasing not only in the United States but also in other countries.[31] Over the past decade, the political activities of US IT firms and their affiliates, such as lobbying and campaign contributions, have substantially increased (see Table 1), making them a powerful lobbying force in the United States. Notably, these IT firms and organizations were key supporters of the Obama administration, which, in turn, strongly supported the industry. As a result, Obama was called the "first tech president," as reported by the Washington Post.[32]

[28] Aaronson 2016b; Aaronson and Leblond 2018

[29] The 2003 US-Chile FTA was the first time that the United Sates included the e-commerce chapter in its FTA.

[30] Azmeh et al. 2020; Aaronson 2018

[31] Azmeh and Foster 2016

[32] Kang and Eilperin 2015

In 2014, the Obama administration appointed Robert W. Holleyman, CEO of the Business Software Alliance (BSA) from 1990 to 2013, as deputy representative of the United States Trade Representative (USTR).[33] The BSA published a report titled "Lockout: How a New Wave of Trade Protectionism is Spreading Through the World's Fastest-Growing IT Markets and What to Do About It," highlighting measures that affect digital trade to suggest that eliminating these barriers should become key agenda items in bilateral, regional, and multilateral trade talks.[34] The Obama administration wanted to create the rules and processes governing digital trade to promote the digital economy through a free and open Internet.[35] Holleyman spearheaded the creation of a new digital trade working group at the USTR, which identified and combated barriers to digital trade and promoted policies for advancing global digital trade.[36] The Obama administration sought to solve these issues by expanding trade remedy measures, utilizing the WTO, and establishing bilateral or regional frameworks such as the TPP. According to Solis, the TPP was instrumental in achieving diplomatic engagement in the Asia-Pacific region.[37] The United States recognized the TPP as a twenty-first-century agreement that set a new standard for global trade while taking up next-generation issues.[38] IT firms and organizations expected the TPP to establish digital trade rules. The BSA expressed its hope that the TPP would play an important role in advancing the modernization of digital trade.[39] Moreover, the Information Technology Industry Council (ITI) stated that advancing the TPP negotiations was one of its key trade priorities, and promoting tech-friendly outcomes from the negotiations would include greater regulatory transparency, stronger intellectual property rights enforcement, binding provisions to support the cross-border flow of data, and light-touch approaches to encryption regulations.[40] Those IT firms' and organizations' claims were finally reflected in USTR's trade policy, entitled the "Digital Dozen" principles, which centered on securing and protecting innovation, a free and open Internet, and barrier-free commerce.[41] According to Holleyman, the Digital Dozen principles reflected the Obama administration's decision to lead the development of a global legal framework that supported the digital economy.[42]

As a result, the digital trade chapter of the TPP included the following three principles: (1) ensuring the free flow of data across borders, (2) preventing data localization, and (3) protecting against forced disclosure of proprietary source code.

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[33] USTR 2014
[34] BSA 2012
[35] Obama 2015
[36] USTR 2016
[37] Solis 2013
[38] Schott et al. 2013
[39] BSA 2015
[40] ITI 2015
[41] USTR 2015a
[42] USTR 2015b

For the first time in a trade agreement, TPP parties committed to enabling individuals covered by the agreement to electronically transfer information across borders in order to conduct their business. According to Froman, a representative of USTR, the TPP allowed the United States and its allies, rather than China, to set the rules regarding data flow.[43] However, Solis mentions that China, like any other APEC economy, has the right to request entry into the TPP and it is important to dispel the notion that the TPP precludes Chinese entry.[44] It aims to eventually develop an Asia-Pacific-wide platform of economic integration, not to draw lines encircling China. Hence, the United States hoped that China would change its unfair trade practices by establishing a high-level trade and investment framework like the TPP. In other words, it was necessary to make China understand the importance of following the principles of the TPP, since China could lose economic opportunities in the future if it did not enter this framework.

Ratification of the TPP by the Obama administration was imminent, but the situation drastically changed with the election of President Donald J. Trump in 2016. President Trump repeated the slogan "America First" emphasizing the United States' withdrawal from international regimes and calling for a radical shift in economic and foreign policy in his inauguration speech on January 20, 2017.[45] Immediately after taking office, President Trump announced that he would withdraw from the TPP and instructed the USTR to shift its focus to bilateral negotiations in all future trade negotiations.[46] Thus, the United States, which had been the foremost proponent of rules for governing digital trade and curbing digital protectionism, abandoned the only binding language regulating digital protectionism.[47]

After the United States announced sanctions against China based on Article 301 of US Trade Law in March 2018, US-China trade tensions escalated.[48] Economic competition continued to escalate, as demonstrated by the tariff battle between the two countries. Along with US-China trade competitions and prompted by the United States' withdrawal from the TPP, the remaining 11 TPP member countries agreed on a modified framework called the CPTPP to bring the agreement into effect on November 10, 2017, and it was signed in March 2018. Given the size of its economy and its importance to international trade in goods and services, the United States' refusal to participate in this agreement was significant; nevertheless, thanks to Japan's strong initiative, the CPTPP has managed to succeed in maintaining high standards and binding rules, such as those for digital trade.[49] According to Katada, the Japanese government shifted its regional geoeconomic strategy from one based on neomercantilism to a more liberal one that established rules and institutions for

[43] Froman 2017

[44] Solis 2013

[45] White House 2017a

[46] White House 2017b

[47] Aaronson 2018

[48] USTR 2018

[49] Terada 2019

the region's public good.[50] The intent was to gain advantages in Asia's regional economic competition amid expanding Chinese influence and the increasingly precarious commitment from the United States.

Since the conclusion of the CPTPP, the US-Mexico-Canada Agreement (USMCA), the Japan-US Digital Trade Agreement (Japan-US DTA), the Japan-UK EPA, and the RCEP have also established digital trade disciplines based on the three TPP principles as listed in Table 2. Recent regional digital trade rules have included the three TPP principles in some form as well as other principles. The exception to this was RCEP which entered into force on January 1, 2022.[51] It was Japan that insisted on the addition of an e-commerce chapter to RCEP, the first trade agreement involving China to include a provision on e-commerce.[52] However, out of the three digital trade provisions in the CPTPP, the RCEP has introduced regulations for free data flow and prohibition of data localization requirements. However, these commitments would exclude the financial services sector and remain subject to exceptions that allow parties to implement security and public policy measures. In addition, the prohibition on requesting source code disclosures was not included in the RCEP, and the discussions on including dispute settlement procedures in the digital field have been postponed due to opposition from China. This is a result of China's digital protectionism. For these reasons, it is unclear at this point whether these provisions are actually effective for countering China's protectionist measurements.

During the US-China trade competition, market-distorting measures have become serious problems not only for the United States but also for Japan and the EU. To deal with those issues, Japan's Minister of Economy, Trade, and Industry, Hironari Seko, proposed a Trilateral Meeting of the Ministers for Trade from Japan, the United States, and the EU. As US-EU tensions intensified, Japan as a middle power country intended to bridge the United States and Europe in order to keep the United States in the international economic order. In addition, Japan tried to maintain the United States' continuous involvement in the multilateral forum of the WTO by emphasizing cooperation between Japan, the United States, and the EU.[53] On December 12, 2017, the First Trilateral Meeting was held on the occasion of the 11th WTO Ministerial Meeting to jointly deal with these market-distorting measures.[54] The agenda of the trilateral meeting included non-market-oriented policies and practices by third countries, such as industrial subsidies, state-owned enterprises, forced technology transfer policies, WTO reforms, and digital trade. At the Sixth Trilateral Meeting in Paris in May 2019, Japan, the United States, and the EU affirmed their intention to achieve high-level results in establishing e-commerce

[50] Katada 2020

[51] Japan, China, South Korea, Australia, New Zealand, and 10 ASEAN countries participate in the RCEP. While India was one of the original negotiating partners, it declined to join after walking out of discussions.

[52] Nikkei Asia, December 30, 2020

[53] Tamura 2019

[54] METI 2017

Table 2 Types of provisions on e-commerce in selected FTAs

Agreement		CPTPP	Japan-EU	USMCA	US-Japan	Japan-UK	RCEP
Signatory		Mar 2018	Jul 2018	Nov 2018	Oct 2019	Oct 2020	Nov 2020
Effective date	Provision	Dec 2018	Feb 2019	Jul 2020	Dec 2019	Jan 2021	Jan 2022
General	Definition	○	○	○	○	○	○
	Scope and general provisions	○	○	○	○	○	○
Liberalization	Non-discriminatory treatment of digital products	○		○	○	○	○
	Prohibition on customs duties on electronic transmissions	○	○	○	○	○	○
	Cross-border transfer of information by electronic means	○	[a]	○	○	○	○[b]
	Prohibition on requiring location of computing facilities	○		○	○	○	○[b]
	Prohibition on requiring location of financial service computing facilities			○	○	○	○[b]
	Prohibition on requiring the disclosure of source code	○	○	○	○	○	
	Prohibition on requiring the disclosure of algorithm			○	○	○	
	Prohibition on requiring the disclosure of cryptography				○	○	
	Principles on access to and use of the internet for electronic	○		○		○	

(continued)

Table 2 (continued)

Agreement		CPTPP	Japan-EU	USMCA	US-Japan	Japan-UK	RCEP
Signatory		Mar 2018	Jul 2018	Nov 2018	Oct 2019	Oct 2020	Nov 2020
Effective date	Provision	Dec 2018	Feb 2019	Jul 2020	Dec 2019	Jan 2021	Jan 2022
Trust	Online consumer protection	○	○	○	○	○	○
	Personal information protection	○	○	○	○	○	○
	Unsolicited commercial electronic messages	○	○	○	○	○	○
	Cooperation on cybersecurity matters	○		○	○	○	○
	Interactive computer services			○	○	○	○
Facilitation	Domestic electronic transactions framework	○	○	○	○	○	○
	Electronic authentication and electronic signatures	○	○	○	○	○	○
	Paperless trading	○		○			○
	Open government data			○	○	○	
	Internet interconnection charge sharing	○					
Others	Cooperation	○	○		○	○	○
	Dispute settlement	○			○	○	○
	Transparency						○

Source: Authors' tabulation based upon each FTAs

[a]Japan and EU shall reassess within 3 years the need for inclusion of provisions on the free flow of data into this Agreement; however, since Japan and the EU mutually have an adequacy level of data protection to transfer personal data, it became possible to transfer personal information from Japan to the EU or from EU to Japan, across borders

[b]RCEP provides for significant exceptions, allowing regulatory restrictions on cross-border data flows that are effectively unchecked by a dispute-settlement process

December 30, 2018, CPTPP went into effect in six member countries: Australia, Canada, Japan, Mexico, New Zealand, and Singapore (MOFA 2019a, b). *The Formation of Multilateral Digital Trade Rules*

rules through the WTO, with the participation of as many member countries as possible.[55] Although Japan, the United States, and the EU have different views on digital trade measures, the three countries have been jointly urging other countries to improve market-distorting measures through international forums such as the WTO, OECD, G7, and G20, as well as the Trilateral Trade Ministers' Meeting.

Developed countries have sought to create plurilateral frameworks for digital trade, and under the initiative of three middle power countries, Japan, Australia, and Singapore, in December 2017, 71 of the 164 WTO member countries and regions issued a joint statement on digital trade at the WTO 11th Ministerial Meeting held in Buenos Aires, Argentina.[56] In this statement, the participating countries agreed to start joint exploratory work toward future WTO negotiations on the trade-related aspects of e-commerce.[57] WTO member countries that did not sign this statement also participated, and discussions began in March 2018 with an eye toward the formulation of e-commerce regulations. On January 23, 2019, at the World Economic Forum Annual Meeting in Davos, Switzerland, Prime Minister Shinzo Abe passionately advocated for the concept of DFFT.[58] He called for the creation of international rules for cross-border data flow and unified data management talks to begin at the G20 in Osaka in June[59,60] On January 25, 2019, at the WTO informal ministerial meeting e-commerce initiative hosted by Japan and co-conveners Australia and Singapore, on the margins of the World Economic Forum in Davos, 76 WTO member countries and regions, including the United States, the EU, Japan, China, and Russia, issued a second joint statement announcing their intention to begin electronic commerce negotiations at the WTO.[61] According to Iwata, the purpose of the joint statement was to upgrade informal digital trade discussions to WTO formal negotiations.[62] This was the consensus of major WTO member countries, including Japan, the United States, the EU, China, and Russia. Since then, negotiations have begun in earnest with 78 countries and regions.[63] The first negotiation round took place in May 2019. As of January 2021, there are 86 WTO members participating in these discussions, accounting for over 90 percent of global trade.[64] The text proposals submitted by members and subject to negotiation revolved around 15 topics:

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[55] METI 2019a

[56] Kuroda 2019

[57] WTO 2017

[58] The DFFT is a commitment to achieving the free flow of data while ensuring trust in privacy and security.

[59] MOFA 2019a

[60] Before Prime Minister Abe insisted on the need for DFFT, "the direction of new IT policies in the digital age" was announced in Japan in December 2018. The document claimed the necessity of mutual trust for "establishing an international framework to promote secure data-free flow" (Prime Minister for Japan and His Cabinet2018).

[61] WTO 2019

[62] Iwata 2019

[63] METI 2019b

[64] WTO 2020

facilitating electronic transactions, consumer protection, transparency, customs duties on electronic transmissions, the flow of information, personal information protection and privacy, cybersecurity, telecommunications, digital trade facilitation and logistics, access to Internet and data, business trust, capacity building, technical assistance, market access, cross-cutting issues, and legal issues.[65]

In addition to participating in intensive discussions at the WTO, at the G20 Summit in Osaka in June 2019, which was the first summit chaired by Japan and held during the US-China trade competition, Japan successfully included the DFFT, proposed by Prime Minister Abe at the World Economic Forum in 2019, in the Leaders' Declaration. On the sidelines of the summit, a special event on digital economy gathered G20 leaders and other countries who are currently participating in the informal plurilateral negotiations on e-commerce at the WTO. Together, they issued the Osaka Declaration on the Digital Economy, announcing the launch of the Osaka Track, a process that will intensify efforts in international rule-making on the digital economy, especially in regard to data flows and e-commerce. The process will also promote enhanced protection for intellectual property, personal information, and cybersecurity. Regarding the launch of the Osaka Track and gaining consensus for the DFFT, the Ministry of Economy, Trade, and Industry expressed that Japan made a great achievement in confirming the basic concept of data at the G20 summit, especially considering the adverse circumstances of the US-China conflict, US-European mutual distrust, and the conflict between developed and developing countries.[66]

The terminology of the Japanese initiative reflects the need for balance. While the free flow of data appeals to the United States, trust was meant to appeal to the Europeans.[67] On the other hand, developing countries do not necessarily see the economic benefit of opening their markets and sharing their data; therefore, they are reluctant to support DFFT. While 24 countries, including the United States, China, Russia, the EU, and several Latin American and East Asian countries, agreed to participate in the Osaka Declaration on the Digital Economy,[68] India, Indonesia, South Africa, and Egypt chose not to sign it.[69] There are mainly two reasons why these countries decided not to participate in the Osaka Declaration. First, they believe that data should be discussed through the WTO, and a plurilateral agreement like the Osaka Track would undermine the core WTO principles for arriving at multilateral consensus-based decisions, which take place under the WTO Work Program

[65] Ismail 2020

[66] METI 2019

[67] Carter 2019

[68] Argentina, Australia, Brazil, Canada, China, the European Union, France, Germany, Italy, Japan, Mexico, the Republic of Korea, the Russian Federation, Saudi Arabia, Turkey, the United Kingdom, the United States, Spain, Chile, Netherlands, Senegal, Singapore, Thailand, and Vietnam

[69] Egypt is not a member of the G20; however, President Abdel Fatah al-Sisis attended the summit in his capacity as chairman of the African Union.

on Electronic Commerce.[70] Second, plurilateral treaties would deny the space for policies on data governance such as data localization rules in some countries, which would likely be undermined by the DFFT.[71]

Japan, Australia, and Singapore strove to accelerate negotiations to achieve a high standard and commercially meaningful outcome by the WTO's 12th Ministerial Conference (MC12), which was originally planned to take place in Nur-Sultan, Kazakhstan, in June 2020. However, due to the COVID-19 pandemic, MC12 was postponed to November 2021, and it was once again postponed to June 2022 in Geneva.

Formation of Rules on Digital Trade in the Asia-Pacific and Indo-Pacific Region

While it is difficult to predict where the multilateral negotiations would lead, a new digital trade framework has been explored in the Asia-Pacific or Indo-Pacific region in recent years. One of the pioneering attempts taken by Asia-Pacific countries was the Digital Economy Partnership Agreement (DEPA). The DEPA is a wide-ranging agreement on digital economy issues that was initiated by Chile, New Zealand, and Singapore. DEPA was signed on June 12, 2020, and entered into force for New Zealand and Singapore on January 7, 2021.[72] It builds upon the digital trade or e-commerce chapters of existing free trade agreements, such as the CPTPP, adding enhanced commitments on facilitating digital trade and multi-party cooperation on a range of advanced technologies. DEPA takes a modular approach, and modules are intended to be building blocks. It has 16 modules covering a wide range of digital issues, such as treatment of digital products, data issues, digital identities, innovation and digital economy, small- and medium-sized enterprises (SMEs) cooperation, transparency, and dispute settlement. Goodman argues that DEPA expands digital inclusivity and attempts to increase information and tools available to SMEs to participate in the globalized digital economy.[73]

A number of countries have now expressed interest in participating in DEPA. Both Canada and South Korea expressed interest in joining DEPA. China's bid to join the DEPA came as a surprise. After President Xi Jinping announced China's interest in

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[70] For example, Foreign Secretary of India Vijay Gokhale mentioned that the discussions and negotiations pertaining to data should be held within the context of the WTO (The Indian Express, June 29, 2019).

[71] According to the document "Draft National E-commerce Policy for Stakeholder Comment" by the Department of Promotion of Industry and International Trade, India, it was said during negotiations that policy space must be retained to seek source code disclosures for facilitating transfer of technology and development of applications for local needs as well as for security. Space for policies to grant preferential treatment of digital products created within India must also be retained.

[72] MTI Singapore 2020

[73] Goodman 2022

joining the DEPA during a speech at the G20 leaders' summit in Rome in October 2021, the Chinese commerce ministry sent a formal application to New Zealand, the depositary of the DEPA.[74] The DEPA is a new type of standalone trade agreement that focuses exclusively on facilitating digital trade; however, the agreement lacks many binding rules, instead focusing more on cooperation in areas such as data transfer, e-commerce, privacy protection, and artificial intelligence. However, many of the commitments in DEPA are merely to affirm existing obligations, share best practices, begin discussions, and establish frameworks for future cooperation. It seems that the DEPA text on data flow and data localization simply repeats the CPTPP provisions, but for many provisions, parties can comply by simply endeavoring to comply. In addition, DEPA does not stipulate a prohibition on mandatory disclosure of source code as CPTPP does. It means that the agreement should not pose any major implementation challenges for China. In other words, China's accession to DEPA can be seen as a symbolic gesture attempting to join an international framework and expand that framework to be desirable for China while maintaining its own digital protectionist practices.

While multilateral digital trade frameworks, such as the CPTPP and DEPA, were being actively established in the Asia-Pacific region, the United States was left out of the trend, partly because it withdrew from the TPP. Since the Joseph R. Biden administration took office, the US trade policy experts have been actively advocating for the formation of digital trade rules in the Indo-Pacific region. For example, Jennifer Hillman, a former member of the WTO Appellate Body and a former Ambassador and General Counsel in the USTR, claimed the United States should start negotiating sectoral trade agreements with important regional partners, starting with digital trade agreements, and working to improve and then join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership to strengthen the multilateral countermeasures China's Belt and Road Initiative.[75] Moreover, Wendy Cutler, who served as an USTR Acting Deputy Representative in the Obama Administration and led the TPP negotiation and Joshua Meltzer from the Brooking Institution argued that the time is ripe for a regional digital trade agreement with US leadership in the Indo-Pacific.[76] According to Cutler and Melzer, they believe that a regional digital trade can get the United States back in the trade game in Asia, while it considers the merits of rejoining the CPTPP. Developing a digital trade agreement for the Indo-Pacific region would have the advantage of building on the high-standard digital commitments in the CPTPP, drawing on the more recent US-Japan Digital Trade Agreement, the Singapore-Australia Digital Trade Agreement, and the DEPA.

On the other hand, Goodman insisted that President Biden should announce the United States' intention to join DEPA and make this a centerpiece of his regional

[74] Reuters, November 1, 2021

[75] Hillman and Sacks 2021

[76] Cutler and Meltzer 2021

economic strategy in order to make the path back to TPP.[77] Goodman pointed out three potential problems of digital trade agreements. First, it would likely take significant time to conclude. Trade negotiations always take longer than expected, especially if they involve many diverse parties, complex issues, and high ambition. Second, the domestic politics will be challenging. Aligning business, labor, consumer, and government interests on sensitive digital issues will be difficult, and Congress will take an intense interest in the negotiations. Third, trade is only one dimension of the digital economy where rules and norms are in play. There are a range of other issues from digital inclusivity to ethical standards for artificial intelligence. In order to cope with those issues, Goodman strongly recommended the United States to join the DEPA which enables experimentation and an ability to address new issues quickly.

While it was unclear what new rules the United States would seek in the Indo-Pacific region, in July 2021, Bloomberg reported that the White House officials are discussing proposals for a digital trade agreement covering Indo-Pacific economies as the administration seeks ways to check China's influence in the region.[78] Although no concrete moves were indicated by the United States, the situation changed drastically when reports circulated that China would apply to join the CPTPP on September 16, 2021.[79] In response to China's application to join the CPTPP, Kurt Campbell, coordinator for Indo-Pacific affairs at the National Security Council, argued that the situation is "deadly serious."[80] President Biden reaffirmed the enduring US commitment to the Indo-Pacific and announced at the East Asia Summit that the United States will explore with partners the development of an Indo-Pacific economic framework (IPEF) that will define US's shared objectives around trade facilitation, standards for the digital economy and technology, supply chain resiliency, decarbonization and clean energy, infrastructure, worker standards, and other areas of shared interest.[81]

In order to establish the IPEF, Commerce Secretary Gina M. Raymond and USTR representative Katherine Tai visited Asian countries at the end of November to discuss the issues with each country.[82] The idea of launching the digital trade framework in Indo-Pacific was also supported by the US Congress and industry. For example, 18 business associations, including the US Chamber of Commerce and the Information Technology Industry Council (ITI), urged USTR representative Tai to negotiate digital trade agreements in the Indo-Pacific region to strengthen and support US businesses and workers.[83] Also, the US Senate Finance Committee Republicans, led by Senator Ben Sasse, sent a letter to President Biden requesting

[77] Goodman 2021a, b, c

[78] Bloomberg, July 13, 2021

[79] Bloomberg, September 17, 2021

[80] Inside US Trade, November 19, 2021

[81] White House 2021

[82] Nikkei Asia, November 18, 2021

[83] ITI, September 13, 2021

that the Administration begin digital trade negotiations with US allies and partners in Asia.[84] In addition, House Foreign Affairs Subcommittee on Asia, the Pacific, Central Asia, and Nonproliferation, led 22 bipartisan Members of Congress in a letter to USTR representative Tai urging the Biden Administration to pursue a digital trade agreement with partners in the Indo-Pacific.[85]

In February 2022, Biden administration released its long-awaited Indo-Pacific Strategy which projects a narrative of American support to the Indo-Pacific in various areas, but particularly as part of a collective response with US allies and partners to a growing and malign influence of China, which is said to be transforming beneficial rules and norms and pursuing a sphere of influence in this region where its “coercion and aggression…is most acute”.[86] The United States pursues regional prosperities, by proposing the IPEF, through which digital economies and cross-border data flows are governed according to open principles, including through a new digital economy framework. Although the Indo-Pacific Strategy has been issued, its concreted contents are still uncertain at this moment. What is clear, however, is that the Biden administration would pursue a framework which does not take the form of a trade agreement emphasizing on the binding rules. The reason for pursuing a non-binding framework is that it does not require congressional approval, making it relatively easy to reach a domestic consensus. This is largely due to the fact that the “Presidential Trade Promotion Authority (TPA)” expired in July 2021. TPA is said to be essential for the United States to conclude trade agreements with other countries. Without TPA, Congress can require any number of changes before approving the contents of an agreement negotiated and concluded by the administration. Thus, if the form of a trade agreement is to be pursued, the Biden administration must first obtain a TPA, which is difficult under the current circumstances. One possible reason for the Biden administration’s desire to avoid the congressional approval process is the upcoming midterm elections in November. The Democrats, whose main support base is labor unions and who are said to be historically backward-looking on free trade, would have little incentive to prioritize negotiating the TPA and trade agreements that leverage it in the time approaching midterm elections. While it is understandable that the United States has chosen a non-binding approach to the IPEF in light of its domestic situation, it may be less effective than the CPTPP, which is legally binding as a treaty, in terms of international rule formation. In addition, participating countries may not engage seriously without incentives such as better access to the US market and binding digital trade rules. According to Goodman, in order to implement the stricter rules and standards that the United States wants, the United States needs to get support from other countries, and the Biden administration should offer tangible benefits to regional partners, especially less-developed ones.[87]

[84] United States Senate Committee on Finance, November 8, 2021

[85] Inside US Trade, November 22, 2021

[86] White House 2022

[87] Goodman 2022

As a result, at the first IPEF ministerial meeting in Los Angeles in September 2022, ministers of 14 nations agreed to start formal negotiations on building a rules-based economic order in the fast-growing region, where China is expanding its clout.[88] Negotiations for the IPEF involve four policy pillars which include fair trade, supply chain resilience, clean energy with decarbonization and infrastructure, as well as proper taxation and anti-corruption. While 13 countries were able to participate in all four pillars, only India postponed its participation in the trade pillar. Indian Minister of Commerce and Industry Piyush Goyal decided not to participate in the IPEF trade pillar because future arrangements for data localization and labor and environment may not benefit developing countries. Indian experts are divided in their views in terms of not participating into the trade pillar of IPEF.[89] Biswajit Dhar, Professor and Head of Centre for WTO Studies, Indian Institute of Foreign Trade, mentioned that the Indian government's position is logical, as India has also distanced itself from the WTO's digital trade area talks.[90] On the other hand, Pradeep S Mehta, expert of trade, claimed his skeptical viewpoint toward the government's unwillingness to participate in the IPEF, which is a more flexible framework compared to RTAs and other agreements, saying if India wants to become a developed country, the government should explore ways to grow the economy by promoting exports.[91] It is believed that the issues surrounding digital trade were a major factor behind India's decision not to participate in the trade pillar. In order to involve an emerging country like India, it is necessary to think about possible benefits for LDCs promoting efficiency and economic growth using digital economy.

4 Conclusion

While the United States has pursued cross-border data free flows, EU has emphasized the significance of legal framework for protecting privacy and data to ensure trust. Moreover, many emerging countries, particularly China, have pursued protectionist measures for economic and national security reasons. These factors may lead to not only parallel lines in the WTO's multilateral digital trade rule-making process but also hurdles to introducing high-level disciplines in Indo-Pacific. With the absence of the US initiatives over the formation of multilateral and regional digital trade frameworks, Japan, as a middle power, has been examining how it can overcome these differences. In order to overcome those differences, Prime Minister Abe of Japan used the occasion of the presidency of G20 to put his concept of DFFT on the global agenda.

[88] USTR 2022

[89] The Hindu, September 10, 2022

[90] The Hindu Business Line, September 11, 2022

[91] Economic Times, September 12, 2022

Though DFFT gained the support of the G20 participants including the United States, China, and the EU, this apparent consensus on data free flow hides many differences between the United States, the EU, and China. Moreover, India, Indonesia, and South Africa, which are G20 members, rejected participating in the declaration. The ambiguity of the meaning of trust has given each country room to interpret the trust differently. Director General of the Economics Bureau of Japan's Ministry of Foreign Affairs Noriyuki Shikata acknowledged that trust is a broad concept subject to different interpretations, but said the term allowed room for international discussions among relevant stakeholders to develop common rules addressing different dimensions of trust.[92] Nonetheless, global expansion of DFFT appeared to be stalled even though the G7 and G20 continuously have discussed. However, since the Action Plan Promoting DFFT was adopted at the German Digital Affairs Ministers Meeting in 2022 which intended to strengthen the evidence base for DFFT, the focus of discussions on DFFT has shifted from the "trade track" to the "digital track" which envisions to foster future interoperability, continue regulatory cooperation, and promote DFFT in the context of digital trade.[93] In other words, the digital track began to examine what can be done to make use of the data.

Although progress in multilateral negotiations has been slow, Japan's desire for the adoption of high digital trade disciplines has not changed. In other words, the reason Japan wants high digital trade discipline is because of the consensus of developed countries on the need to eliminate or reduce digital protectionist or digital authoritarian market-distorting data governance with China in mind. So, in which international fora should the Japan achieve a high degree of discipline in digital trade? DEPA is currently attracting interest in the Indo-Pacific; however, there are several issues with DEPA. First, although DEPA is said to be highly disciplined, it is in fact TPP-minus. For instance, it does not include any provision on source code. Secondly it lacks binding rules, instead focusing more on cooperation. Many of the commitments in DEPA are simply to affirm existing obligations; hence, DEPA would not pose any major implementation challenges for China. Because of these reasons, DEPA may have unexpectedly prompted China's surprise application for membership. Japan's participation in DEPA in the midst of China's application for membership would send the wrong message not only to China but also to other countries because participation of Japan could be perceived as Japan's admission of DEPA's standards, so that Japan should consider its participation in DEPA cautiously at this moment.

So which international fora is appropriate as a framework for digital trade? It is very important that the United States proposed the IPEF in order to prevent China from establishing an economic order in the Indo-Pacific while China has applied to join the CPTPP and DEPA. Japan as a middle power needs to actively participate in the IPEF; however, it is questionable whether the IPEF can establish rules for digital trade that retains the same high degree of discipline as the CPTPP. The IPEF may

[92] Goodman 2021a

[93] Mizutori 2022

not be the best approach as a catalyst for rule-making in the Indo-Pacific economies, especially because it does not include commitments on market access, with few benefits to developing countries. It is not certain how actively ASEAN countries would participate in the IPEF, given that the IPEF lacks attractiveness as an economic framework. But still IPEF has a meaning to keep the United States, with its increasing tendency toward economic isolationism, in the Indo-Pacific region. Therefore, it is important for Japan as a middle power to act as an intermediary between ASEAN and the United States and to actively bring the two sides together.

Currently, it is difficult to expect the United States to return to the CPTPP because of its domestic political conditions. However, one of the motivations for the United States to actively promote the TPP in the first place was its strategic importance in containing China's digital protectionist measures. The CPTPP has that potential, so that Japan needs to persistently persuade the United States to return to the CPTPP. In addition, it will also take time to get China to abide by the CPTPP rules, but if China wants to be a part of CPTPP, it is essential to press China hard to participate in accordance with the provisions of the CPTPP. Middle power countries should form a force that can counter China, while they should make China understand that it may lose economic opportunities in the future if it does not join the CPTPP framework. With weakening US leadership, China's economic rise, and a power vacuum in the Indo-Pacific, Japan, which has one of the world's most advanced sets of rules for digital trade and is a co-convener of the Joint Statement Initiative on e-commerce, should take a leading position in the formation of multilateral and regional rules with other middle powers like Australia and Singapore that share the same position.

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South Korea's Renewable Energy Odyssey: A Failed Attempt at Carbon-Neutral Growth Without Nuclear Energy

Min Gyo Koo

1 Introduction

António Guterres, United Nations Secretary General, who termed the August 2021 report by the Intergovernmental Panel on Climate Change (IPCC) a "code red for humanity," warned that the original ambition of limiting global temperature rise to 1.5 °C was already "perilously close" and urged the international community to take "the most ambitious path."[1] This and other concerns about the slow progress in climate action belie the so-called energy trilemma: it is difficult, if not impossible, to simultaneously achieve energy security, energy justice, and environmental sustainability.[2] In an era of the COVID-19 pandemic, a war in Ukraine, and global supply chain challenges, assuring energy security is critical for geo-political and geo-economic purposes more than ever before. The rift between energy-rich and energy-poor makes the social welfare debate more complicated. Be it a national security or justice issue, environmental considerations must be included in a country's geo-political and geo-economic strategies.

In a competitive geo-economic and geo-energy landscape in the Indo-Pacific, a number of countries have pledged to achieve net-zero emissions by 2050, making themselves carbon-neutral in the next 30 years. The pressure is visible in the traditional energy sector including fossil fuels and nuclear energy. At the UN Climate Change Conference (COP26) held in Glasgow in October–November 2021, the

[1] Rokke (2021)

[2] World Energy Council (2016)

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contracting parties agreed on "phasing down"—if not phasing out—their coal use. Alternatively, renewables have emerged as a relief pitcher of the impossible trinity.

The question remains unanswered: how and to what extent should states invest? Can solar and wind power, for instance, end the divide between energy-rich and energy-poor countries? Global efforts to stimulate the renewable energy industry have caused unintended consequences: The gold rush toward renewables and the Titanic sinking of fossil fuels and nuclear energy with potentially significant implications for the Indo-Pacific region, where the United States and China are in a tug-of-war for influence on various fronts including technology, energy storage, advanced manufacturing, and the like.

South Korea stands out in this regard. As an energy-poor country, it has long relied on imported fossil fuels and, in recent decades, nuclear energy riddled with safety issues and opposition. In the Indo-Pacific region where the energy trilemma is making South Korea more sensitive and vulnerable to oil price shocks and disruptions in energy supply chains, the Moon Jae-in government chose to accelerate the renewable transition while sharply phasing out nuclear energy. South Korea's numerical target to reduce greenhouse gas emissions may not appear striking.[3] But its renewable transition is distinctive in its speed of change. The Moon administration aggressively pursued "zero nuclear" and "zero fossil fuel" initiatives. Most notably, the 3020 Renewable Energy Implementation Plan (hereafter the 3020 Implementation Plan) would boost renewables' share of the energy mix from 7 percent to 20 percent by 2030.[4]

The track record of South Korea's renewable transition have been mixed. On the one hand, it has rapidly enlarged the renewable energy industry in South Korea. On the other hand, many elements of its policy are subject to legal, political, and financial challenges. Aside from potentially thorny trade issues with its trading partners, generous but uncoordinated government subsidies have caused traditional pork barrel politics[5] at home.[6]

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[3] South Korea has signed the Paris Agreement of the United Nations Framework Convention on Climate Change (UNFCCC) and pledged to reduce emissions 37 percent below business-as-usual (BAU) levels by 2030. In March 2021, President Moon Jae-in announced his plan to further bolster South Korea's target of cutting emissions by more than 24 percent by 2030 from the 2017 level.

[4] Energy mix refers to a government's policy for balancing and diversifying the sources of energy. It typically involves setting goals for the percentage of energy to be produced from different sources, such as fossil fuels, renewable energy, and nuclear power, and implementing measures to achieve those goals in a reliable, affordable, and sustainable manner. As to South Korea, the Third Energy Basic Plan (2019–2040) set the renewable energy target even higher at up to 35 percent by 2040 while leaving the target of nuclear energy ambiguous. According to the *Carbon Neutrality Vision and Strategy for Industry and Energy* released in December 2021, renewables would take up about 70.8 percent of South Korea's power generation capacity by 2050 (The Ministry of Industry, Trade, and Energy 2021).

[5] Park and Koo (2018)

[6] The so-called green subsidies are not compatible with the World Trade Organization (WTO)'s Subsidies and Countervailing Measures (SCM) Agreement if they distort the market mechanism and cause unfair discrimination against foreign firms (Rubini 2012; Lewis 2014; Lee 2016a, b; Chung 2018; Park and Koo 2018).

The zero nuclear pledge has caused no less trouble. Public attitude toward nuclear power plants turned negative in the aftermath of the 2011 Fukushima nuclear power plant disaster in Japan. A series of corruption scandals within South Korea's exclusive nuclear industry network fueled the anti-nuclear movement and motivated some politicians to garner support from public resentment. Scrapping two new nuclear reactors was Moon's election pledge. He also promised to make South Korea a nuclear-free nation. Within the first few years of his presidency, public energy enterprises shifted toward renewables. His predecessors' hope that South Korea's nuclear program would help combat climate change and energy insecurity dwindled to nothing. The rushed closure of older reactors and the scrapping of plans for new ones inevitably caused document tampering by government officials that the Board of Audit and Inspection (BAI) found illegal. In a dramatic turn of events, the new Yoon Suk-yeol government has promised to reverse Moon's nuclear-free promises, reflecting the dire need to address energy trilemma challenges and meet geo-economic goals.

The remainder of this chapter unfolds in four sections. Section 2 reviews the evolution of South Korea's energy mix policy and explains why South Korea's energy policy has had a rollercoaster rise, especially over the past decade. Departing from its earlier focus on fossil fuels and nuclear energy, South Korea found a new enthusiasm for renewables under the Moon administration. This section notes that South Korea's abrupt transition toward renewables was ipso facto problematic, as the government's green subsidies can potentially cause not only trade disputes but also an unsustainable waste of natural and financial resources at home.

Section 3 analyzes political and legal issues resulting from the Moon government's renewable adventurism. To attain its self-claimed goal by 2030 and beyond, President Moon toyed with a series of policy tools including the reintroduction of the feed-in tariffs (FIT) program and the extension of the renewable portfolio standards (RPS) system. Many of these measures are potentially incompatible with WTO subsidy rules.[7]

Section 4 critically reviews the policy process of the Moon administration's nuclear phase-out scheme with a focus on the 2017 deliberative polling and the scandal surrounding the early closure of Wolsong 1 nuclear reactor that surfaced as a result of the 2020 BAI's audit report. Both events reveal the ideological bias embedded in the Moon administration's nuclear phase-out policy. This section also reviews the policy U-turn being made under the new Yoon administration.

Section 5 concludes that South Korea's new energy mix policy has been driven by plan-ideological rather than plan-rational political environments, making it further adrift in the wake of a carbon-neutral ambition elsewhere in the world. In the

[7] First introduced in 2002, the program attracted high expectations as South Korea's flagship renewable energy supply project. However, support for new projects abruptly ended at the end of 2011, as the government's Electric Power Industry Infrastructure Fund ran out much faster than expected. Aside from rent-seeking behaviors and lack of transparency, the negative impact of solar panels and wind turbines on the environment brought the program to an early retirement to be replaced by the RPS in 2012 (Koo 2013: 2).

Table 1 South Korea's energy consumption by sources

Final energy consumption [PJ]	2000	2005	2010	2015	2020
Total	5626	6291	7179	8096	8341
Coal, lignite, and peat	614	591	756	876	732
Oil	3339	3329	3422	3774	3841
Natural gas	455	668	857	857	879
Bioenergy and waste	134	228	344	619	794
Electricity	946	1286	1615	1781	1842
Heat	139	190	184	189	253

Source(s): Korea Energy Statistics Information System (www.kesis.net)

geo-economic context of a global campaign for clean energy and climate action, the direction of South Korea's energy policy is right, but it needs to be depoliticized and its speed readjusted. South Korea must realize that carbon-neutral growth would not be made possible without nuclear energy.

2 South Korea's Energy Mix Policy, Past and Present

As an energy-poor nation, South Korea has given the highest priority to energy security as a prerequisite of its government-led industrial policy. In a competitive and occasionally hostile geo-political and geo-economic landscape of the Northeast Asian corner of the Indo-Pacific, it is no wonder that the South Korean developmental state has closely aligned its energy supply and demand structure with its industrial agenda. During the developmental decades, South Korea's energy mix policy prioritized economic growth over the environment. The potential conflict between these two policy areas was effectively managed, if not completely controlled, by development-oriented technocrats and vote-hungry politicians.[8]

South Korea heavily relied on fossil fuel energy sources during the early period of its industrial take-off.[9] As shown in Table 1, the country's industrial and household consumption of energy remain captivated by fossil fuels, which account for more than 65 percent of final energy consumption in 2020 in Petajoule (PJ).[10] It is equally notable that the share of electricity in energy demand has increased from 16.8 percent to 22.1 percent over the past two decades.

Aside from fossil fuels, nuclear energy has played a significant role in electricity generation (see Table 2). South Korea's dependence on nuclear energy has continued to rise until recently since its first nuclear power reactor began operating in 1978. Under the first phase of South Korea's nuclear power program, the government signed contracts with foreign companies for the procurement of reactors, with

[8] Park and Koo (2018)

[9] Lolla and Graham (2021)

[10] One PJ is equal to 278 gigawatt-hours of electricity or 28 million liters of petrol.

Table 2 Electricity generation by sources

Electricity production (GWh)	2000	2005	2010	2015	2020
Total	290,126	389,344	499,356	552,572	570,142
Coal, lignite, and peat	111,395	148,791	219,276	236,586	214,119
Oil	34,581	25,992	18,935	12,518	7298
Natural gas	29,461	62,154	103,184	122,856	146,678
Bioenergy and waste	93	294	1107	3150	9711
Hydro	5610	5189	6472	5796	7151
Nuclear	108,964	146,779	148,596	164,762	160,184
Wind	17	130	817	1342	3152
Solar	5	15	772	3975	17,967
Other	0	0	197	1091	3425

Source: United Nations Statistical Division, OECD/IEA and IAEA RDS-1

Korean firms playing a little role. After numerous technical and non-technical turns but steep learning curves, South Korea gained the knowledge and expertise to independently manufacture the equipment and components for nuclear power plants by the mid-1990s and finally commissioned its first Korean Standard Nuclear Power (KSNP) Plant, Hanul-3, in 1998. The first decade of the new millennium witnessed a rapid increase in capacity and capability of nuclear power technology, declaring technological independence since 2012. In 2009, South Korea surprised the international nuclear community again by winning the UAE's $20 billion-worth four nuclear reactors deal.[11]

Only a few environmental activists doubted that nuclear energy is a zero-emission clean energy source. But the public attitude toward nuclear power plants dramatically changed in the aftermath of the 2011 Fukushima nuclear power plant disaster in Japan. As Japan's geographically closest neighbor, South Korea's deep concern was understandable. The Fukushima accident sparked a thorough and exhaustive investigation of South Korean nuclear power plants, which revealed a corruption network that had pocketed several million dollars of bribe payments in return for turning a blind eye to the parts that did not meet the quality standards of Korea Hydro & Nuclear Power (KHNP). The 2013 corruption scandal caused a widespread distrust in the safety of nuclear power plants, forcing three plants to temporarily stop operating. Along with environmental and anti-nuclear activists, opposition parties raised their strong voices against nuclear energy.[12] The then Park Geun-hye government (2013–2017) introduced a series of reforms to enhance transparency in procurements and to prevent collusive bidding and fraud. However, as the nuclear

[11] Kim (2019)

[12] Most notably, the Democratic Party, the then-largest opposition party, declared in its new party platform: "Ecological democracy is a new value we must pursue, and creating green jobs is our immediate task. From the perspective of sustainability and human peace, we aim for a zero-nuclear power generation in the long term, while strengthening measures for nuclear safety in the short term. We strive to develop renewable energy and take the lead in environmental preservation at the global level" (Nocut News 2014).

scandal matured and the public learned more about it, the suspicion of the public did not subside.[13]

In 2016, these concerns were further aggravated after a 5.8 magnitude earthquake hit Gyeongju, a southeastern city. The Shin Kori nuclear power plants were located less than 50 km away from the epicenter. In a desperate attempt to pacify the local residents, the KHNP claimed that the Shin Kori reactors were designed to withstand earthquakes of up to 6.9 on the Richter scale. But the voice of anti-nuclear activists became even louder: In theory, South Korea's maximum potential earthquake magnitude is 7.5, and many people became inclined to such an extreme scenario. To make matters worse, it was found that no proper geological investigation had been conducted on the very site of Shin Kori 5 and 6 when the government had issued a construction license. As will be discussed in Sect. 4, it offered the political background against which the Moon government rushed to a "deliberative polling" to decide whether to proceed with the construction of Shin Kori 5 and 6.[14]

Having experienced the two oil shocks in the 1970s, South Korea also realized the need for diversification of its energy portfolio and began to restructure its consumption patterns away from fossil fuels. However, renewables received low priority among other alternatives. Most notably, the energy mix policy remained closely tied to industrial policy goals. It was not until President Lee Myung-bak (2008–2013) came to office that renewable transition first attracted policy attention albeit rhetorically. With the "low carbon, green growth" campaign, the Lee administration set a grid party target by 2020 and a primary energy supply target of 11 percent for renewable energy by 2030. The government also introduced the Green Growth Framework in 2010 as a legal platform to support green industries and climate change businesses. Yet President Lee shifted away from his earlier focus on climate change itself to an emphasis on the industrial promotion of green manufacturing.[15]

President Park Geun-hye echoed her predecessor's energy policies. Despite her rhetorical achievements, President Park was equally mediocre in her performance in terms of renewable energy policy. As with its predecessors, the Park administration failed to achieve its renewable targets. Her government claimed that South Korea's renewable energy share reached 7 percent of the entire energy supply. However, it remained silent on the claim that nearly 50 percent of the so-called new-and-renewable energy was generated from biomass and waste burning with a mixture of dirty coals.[16]

In sharp contrast, President Moon emphasized renewable energy from day one of his presidential campaign through his inauguration in May 2017. Most notably, the 3020 Implementation Plan pledged to raise RPS generation targets, to revive the FIT program for small-scale suppliers, and to encourage the engagement of local

[13] Lee (2016a, b)

[14] Jang (2017)

[15] Koo (2013); Lee (2014); Ham (2018)

[16] Lee (2014); Lim and Jo (2017)

residents and cooperatives in the renewable energy transition using promotional[17] measures.[18] Yet the 3020 Implementation Plan was too ambitious to achieve from the very beginning. Linked to the zero nuclear policy, the Moon administration's renewable energy was allegedly safer and cleaner than any other alternatives. The plan included a proposal to reduce biomass and waste burning.[19] It aimed to provide an additional 48.7 GW of renewables, 97 percent of which would be supplied by solar and wind power by 2030. In 2017, the total amount of solar and wind power supply was 6.9 GW. To achieve the 2030 target, an additional investment of more than USD 80 billion would be required.[20]

3 A Nuclear-Free, Renewable Moonland

South Korea's renewable energy industry in general and its renewable energy management system more specifically are in their early stage, lagging behind advanced manufacturers and operators in the United States, Japan, the European Union, and China. In solar cells/modules and wind turbine markets, for instance, China dominates with an average share of global manufacturing capacity over 80 percent. Over the past decade, the costs of renewable power generation have decreased rapidly across the world due to steady improvements of technology, economies of scale, efficient supply chains, and successful operator experience. Nevertheless, the cost of electricity produced by renewables is higher than other sources in South Korea. South Korea has some competitive edge in the solar panel sector. But the volume of its export has dwindled since 2012 under fierce competition, especially from China.[21]

[17] MOTIE (2017)

[18] A subsidy takes a variety of different forms, including grants, loans, equity infusion, loan guarantees, tax credits, and goods or services, other than general infrastructure (WTO SCM Agreement Article 1.1). The 2030 Implementation Plan offered financial incentives to large-scale renewable energy projects, R&D funds, and industrial clusters for innovative renewable companies. More specifically, the government promised a RPS mechanism with weighted REC system and a Korean-style FIT model with generous government loans and tax incentives. These subsidies can be highly contentious under the WTO. South Korea's Moon administration was not alone here. The US Biden administration's Inflation Reduction Act of 2022 has been similarly accused of creating distortions as a result of the subsidies it offers. In its ruling on the Canada-Renewable Energy/Canada-FIT Program (WT/DS412·DS426/R), the WTO's Dispute Settlement Body has indicated that measures to promote renewable energy sectors are subject to prohibited subsidies, especially when government subsidies confer benefits in existing markets (Park and Koo 2018: 70–71).

[19] As of 2016, renewables consisted of solar (38 percent), wind (8 percent), biomass (16 percent), and waste (25 percent). The negative consequences of burning biomaterials and waste were evident (Panwar et al. 2011). The Moon administration attempted to change the composition to 57 percent solar, 28 percent wind, 5 percent biomass, and 6 percent waste by 2030 (Kwak 2018: 27).

[20] MOTIE (2017)

[21] Yoo (2015); Federation of Korean Industries 2016; Hyundai Research Institute 2018; International Renewable Energy Agency 2021)

It was no wonder that South Korea's renewable energy community asked for government support for renewable energy production in South Korea. With little recognition of global norms on government subsidies, policy experts echoed that R&D subsidies and tax reliefs would be required to create and cultivate a vibrant renewable energy sector. Accordingly, the central government's renewable energy budget increased by 20 percent in 2019 from the previous year, surpassing USD 1 billion for the first time.[22] According to IHS Markit, solar power took up the majority share in South Korea's renewables with 67 percent of installed capacity or 10.5 GW as of 2020, nearly doubled since 2017.[23]

Moon's commitment and dedication to renewables culminated in the announcement of a *Green New Deal* in July 2020. A total of USD 95 billion would be invested to create two million new jobs by 2025 with a particular emphasis on the so-called green transition, the examples of which include 230,000 energy-saving buildings, 1.13 million electric cars, more renewable energy projects, and unemployment insurance to sustain the livelihoods of workers during the economic crisis. In particular, USD 38 billion would be dedicated to boosting the installed capacity of renewables.[24]

Subsidizing renewables is subject to Pandora's box of trade disputes. The 3020 Implementation Plan illustrates this point. Generous loans, weighted RECs, the Korean-style FIT program, and specific support programs are inherently actionable subsidies to the extent that they can cause adverse effects on other countries. More seriously, the focus on local engagement can be seen as import substitution subsidies, which are prohibited by the SCM[25] Agreement.[26]

In order to encourage local engagement and participation, the Moon government adopted the Korean-style FIT model and promised support for rural residents who participate in solar power generation. In addition to obtaining public support and achieving ambitious deployment objectives, civil participation was essential in revitalizing local economies. For instance, the new FIT model required six major electricity generators to buy electricity produced by small renewable businesses and

[22] Kim (2016); Ann (2018); Asan Institute for Policy (2018); Jung (2018)

[23] During the same period, hydropower capacity increased by 1.6 percent, wind capacity by 25 percent, and biomass by 100 percent (https://ihsmarkit.com/research-analysis/south-korean-quest-for-solar-unimpeded-by-coronavirus-.html)

[24] Kirk (2020)

[25] Park and Koo (2018)

[26] Moon's renewable energy policy was closely tied to local and regional engagement policy. Compared to their traditional counterparts, renewable energy sources including wind, solar, and biomass require more land, and their environmental impact has been controversial both biologically and environmentally (Seager et al. 2009). For 1 GW of electricity to be generated by solar and wind power, 33 million m^2 and 165 million m^2 of land are required. In contrast, nuclear energy production requires 363,000 m^2 of land for the same amount of electricity (Asan Institute for Policy 2018). As a result, renewables have posed a significant challenge to local residents, deeply polarizing local neighborhoods over renewables installation.

cooperatives/agricultural associations at a price set under the existing RPS system. Those recipients would be guaranteed constant flows of revenues for 20 years.[27]

However, such a local participation program can be problematic as it can be claimed as disguised protectionism. It clearly has the characteristics of local contents requirement (LCR).[28] The Korean-style FIT model and REC reform package were intended to encourage local participation and engagement. In addition, to support social cooperatives without financial capabilities, the Ministry of Economy and Finance (MOEF) asked the Korean Credit Guarantee Fund, a public financial institution, to extend credit guarantees for promising SMEs, which allowed them to borrow up to 90 percent of the required funds for solar projects from commercial banks. There were allegations that for the remaining 10 percent the government influenced commercial banks to unconditionally grant loans. It became a political scandal as many of the recipients of favorable loans were allegedly political allies of the ruling progressive[29] party.[30]

One of the Moon administration's clean energy ambitions was the Saemanguem Renewable Energy Cluster. Having been launched in 1991, the land reclamation project on the Saemanguem tidal flats in North Cholla Province was completed in 2010 after a series of delays and postponements. The project has added about 300 km^2 of land area to the Korean peninsula with a 33.9 km-long seawall. The Moon administration planned to dedicate more than 10 percent of the area to a renewable energy cluster. The plan included wind and solar power generators as well as hydrogen and fuel cell energy systems. It also included a giant offshore wind farm.[31] President Moon promised in February 2021 that the total capacity of the

[27] Hahm (2017); MOTIE (2017); KNREC (2018)

[28] WTO SCM Agreement Article 1.1 stipulates: a subsidy is "deemed to exist if there is a financial contribution by a government or any public body within the territory of a Member" or if "there is any form of income or price support in the sense of Article 16 of GATT (Subsidies)" and "if a benefit is thereby conferred." If a subsidy is found to be "specific to an enterprise or industry or group of enterprises or industries" (Article 2.1) and cause "adverse effects to the interests of other Members" such as "(a) injury to the domestic industry of another Member; (b) nullification or impairment of benefits accruing directly or indirectly to other Members; (c) serious prejudice to the interest of another Member" (Article 5), it is considered "actionable." Prohibited subsidies (Articles 3 and 4) are exempted from the specificity test, but a positive decision on the existence of a subsidy is a prerequisite.

[29] Lee (2018)

[30] According to a government investigation report released in September 2022, more than $189 million of taxpayer money was wasted during the former Moon administration in the form of direct payments or loans to fraudulent or manipulated renewable projects at least in 12 municipalities. The amount accounted for more than 12 percent of the total fund mobilized to assist renewable energy projects in local provinces. The fraudulent and manipulated cases mostly involved solar projects, such as "loans extended to install fake agricultural facilities under the solar power facilities so as to abide by the law that farmland must be cultivated, contracts with unregistered solar power generation companies and exaggerated tax invoices for solar projects" (Nam 2022).

[31] https://sdco.or.kr/portal/eng/main/main.do

offshore wind farm would be equivalent to 6 nuclear power plants that can keep 12 million citizens alight and create 120,000 jobs.[32]

One of the major political challenges to achieving these goals was the opposition from local residents—mostly farmers and fishermen. To pacify the local community, the municipal government in 2018 passed rules that allowed residents to acquire a 30 percent stake in local renewable energy projects. That has provided a windfall profit for residents so far as the government is dedicated to purchasing the electricity produced by renewable sources at high prices.[33] With a climate and topography ill-suited for large-scale renewable power generation, there have been other technical challenges. Wind and solar power in South Korea currently cost nearly three times as much as nuclear power, among the highest in the world.[34] Critics argue that the economies of scale of solar panels and wind turbines make little sense, and the sizable cost burden will eventually shift to the taxpayer.

As a matter of fact, the South Korean government faced severe criticism for its previous FIT program, which had eventually given financial benefits to Chinese solar module producers rather than their Korean counterparts.[35]The Moon administration seemed committed to not repeating the same mistake, but there is little evidence that his renewable dreamland held up during the bumpy transition from fossil fuel and nuclear energy to renewables without beggaring taxpayers and foreigners.

4 Making Nuclear Power Unrenewable

As the world's sixth-largest nuclear energy producer, South Korea has 24 reactors in operation, which provide about 20 percent of its electricity, and five under construction. According to a plan released in 2020 for the period of 2020–2034 by the Moon administration, South Korea would have 17 operable units by 2034. The share of nuclear capacity for electricity generation would fall from 18.2 percent in 2020 to 10.1 percent in 2034, while the renewables capacity rises from 15.8 percent to 40.5 percent during the same period (Fig. 1).

Although Moon's efforts to promote the green and clean energy sector were praiseworthy, the speed at which it aimed to achieve an energy transition was problematic. It was feared that replacing nuclear energy with renewable energy would disrupt the stable supply of electricity and reasonably low electricity prices, which would in turn have a negative impact on South Korea's industrial capabilities (Table 3).[36]

32 Katona (2021)

33 Lee and Mathis (2021)

34 Lee and Kim (2020)

35 Koo (2013)

36 Kong and Lee (2017); Park (2017); Yoon (2017)

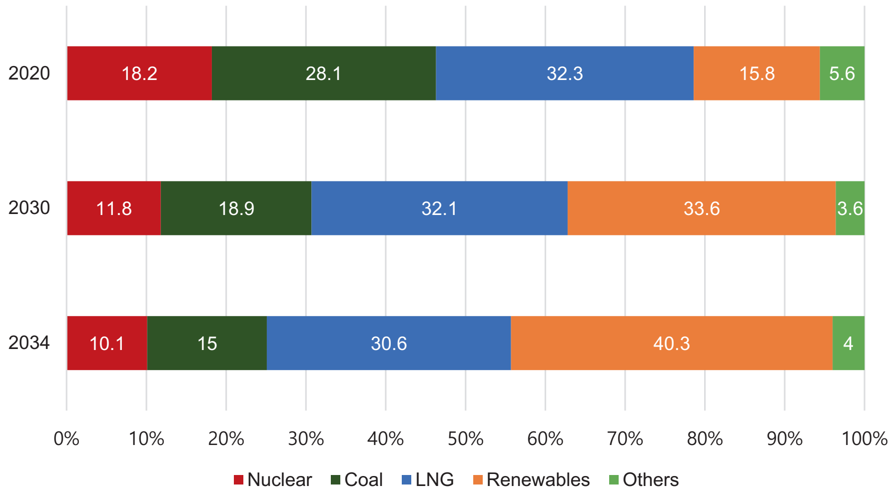

Fig. 1 Electricity Generation Targets for Selected Sources. (Source: The Ministry of Trade, Industry and Energy (2020), *ninth Basic Plan for Long-term Electricity*, https://www.korea.kr/news/pressReleaseView.do?newsId=156429427)

Table 3 Electricity generation targets by target date for selected sources

Sources\Year		2020	2022	2030	2034
Coal	30 out of 60 units (15.3GW) to be shut down, 7 new units (7.3GW) to be constructed	35.8GW	38.3GW	32.6GW	29.0GW
LNG	Transition of 24 units (12.7GW) out of 30 coal units to be shut down to LNG	41.3GW	43.3GW	55.5GW	59.1GW
Nuclear	4 units (5.6 GW) to be constructed, 11 old units (9.5 GW) to be prohibited from extending their lifespan	23.3GW	26.1GW	20.4GW	19.4GW
Renewables	Achieving the supply target of the third E-Basic (June 2019) and the Green New Deal Plan (July 2020) (based on rated capacity)	20.1GW	29.4GW	58.0GW	77.8GW

Source: The Ministry of Trade, Industry and Energy (2020), *ninth Basic Plan for Long-term Electricity*, https://www.korea.kr/news/pressReleaseView.do?newsId=156429427

Nuclear energy became a controversial issue, especially after the 2011 Fukushima accident. Public fear about nuclear energy programs and related health risks worsened thanks to a series of corruption scandals surrounding the nuclear industry network. President Moon was one of the politicians who were motivated to garner support from public resentment. During his presidential campaign in early 2017, he pledged to scrap two new nuclear reactor construction plans. He also promised to make South Korea a nuclear-free nation.[37]

Aside from financial concerns about the green transition plan, however, the sheer abruptness of the nuclear phase-out scheme was soon to be consumed by political controversy and bureaucratic scandals. In his early presidency, Moon chose the "deliberative polling" option to support and justify its decision to suspend a USD 7.5 billion project for two nuclear reactors—Shin Kori 5 and 6—amid the public's growing concerns about nuclear safety. In July 2017, an independent, ad hoc committee was established to manage public debate and conduct an opinion poll on whether to permanently abandon the two nuclear projects. After 3 months of deliberation, 59.2 percent of the 471 participants in the final survey responded in favor of resuming the construction work, while 40.5 percent supported abandoning the project. At the same time, the respondents suggested the government expand its investment in renewables (27.6 percent), while the majority (53.2 percent) supported Moon's nuclear phase-out policy, and the rest either the *status quo* (35.5 percent) or called for expansion[38] (9.7 percent).[39]

Such a paradoxical and eclectic survey result itself caused controversy over its legitimacy let alone its integrity. Neither side of the pros and cons felt the playing field was even. It was not even clear whether both sides were provided with enough information and made their decisions based not on the ideological bias but on scientific knowledge. Others believed that the time was too short for an in-depth deliberation and the selection process of topics was poorly organized. Very few participants turned out to have changed their original views and attitudes toward the nuclear issue after all.[40]

Despite growing criticism about the survey result, the Moon government was not deterred from pursuing its long-term plan for a nuclear phase-out. It announced that it would soon take necessary measures to resume the construction of the two reactors in response to the deliberative polling result but reaffirmed its commitment to shutting down nuclear reactors when they reach their naturally designed lifespan. In

[37] It is a public knowledge in South Korea that a doomsday film entitled "Pandora: We Knew This Day Would Come" influenced his nuclear-free fantasy. In the 2016 film directed by Park Jeong-woo, a magnitude 6.1 earthquake caused the explosion of an old nuclear power plant in a small village leading to a nation-wide chaos while evoking memories of the 2011 Fukushima meltdown. Reportedly, Moon shed a tear while publicly watching the movie in Busan, his political hometown, and told his supporters: "Even if the probability of a nuclear accident is only one in a million, if there is a possibility of an accident, we must prevent it. There are 3.4 million people living within a 30 km radius of the Kori region, where nuclear power is the most concentrated in the world. It will be a total disaster if any nuclear accident takes place in its neighborhood. For Busan citizens, it's like living with a bomb that will explode at your bedside. We should get rid of Pandora's box itself rather than hopelessly trying to leave it unopened" (Kim 2016; Kong and Lee 2017).

[38] Jang (2017); Kong and Lee (2017)

[39] A national Gallup poll conducted in September 2017 showed the public was evenly divided with about 40 percent in favor of nuclear constructions to continue and the same proportion wanting suspension (Kong and Lee 2017).

[40] Chung (2018, 2020)

a press conference in October 2017, the spokesperson of the Presidential Office confirmed that the president remained firm on building a nuclear energy-free nation, citing Moon to say: "Up until now, the lives and safety of the people have been put in the backseat when establishing and implementing energy policies, while environmental considerations have also been overlooked…To build a safe Republic of Korea and keep pace with the global trend, we...have to implement a great shift in our national energy policy that will reduce nuclear and coal-fired power plants, and implement and increase [the use of] clean, safe future energy."[41]

In December 2017, the Nuclear Safety and Security Commission (NSSC) approved the permanent shutdown of unit 1 at the Wolsong nuclear power plant, South Korea's second-oldest reactor dating back to 1983, which had been offline since May 2017. The nuclear power plant operator, KHNP, formally approved the shutdown of the unit in 2018 and permanently decommissioned it in 2019, 3 years earlier than scheduled. In 2012, operations at the reactor were suspended after it reached its 30-year lifespan, but the NSSC extended its lifespan by 10 years until 2022. NSSC's decision to revoke its earlier permission and KHNP's hasty implementation of its supervisory organization's decision were met with protests and criticism from the opposition parties and labor union of KHNP, which launched legal action against the NSSC and KHNP board members for abusing their authority and breaching[42] trust.[43]

As per the request from the National Assembly in September 2019, the Board of Audit and Inspection (BAI) started investigating an allegation that the KHNP had deliberately undervalued the economic viability of Wolsong 1 to hasten its earlier shutdown than originally planned. In October 2020, the BAI concluded that a June 2018 projection report commissioned by the KHNP unreasonably deflated sales figures and that KHNP employees noticed that such a manipulation would be problematic but remained silent because they believed it was VIP's—namely, President Moon's—intent to shut down the power plant sooner rather than later. BAI's report fell short of determining whether the reactor's early shutdown could be justified, as its audit focused only on the verification of the economic viability report on the Wolsong 1 reactor.[44]

At the time of writing in February 2023, the Ministry of Trade, Industry, and Energy (MOTIE) and the KHNP are still being investigated over the allegations of early closure of Wolsong 1. A former MOTIE Minister and several high-ranking government officials, who oversaw the KHNP, have been indicted for abuse of power and their alleged involvement in the destruction of over 400 government documents and other materials just before receiving an order to submit them from the BAI in late 2020, thereby hampering state auditors' investigation of the closure

[41] Yonhap News (2017)

[42] Nuclear Engineering International (2020)

[43] Aside from the shutdown of Wolsong 1, the construction of units 3 and 4 of the Shin Hanul nuclear power plant in Ulsan was postponed, and plans for other new nuclear power plants were also scrapped (Song and Lee 2022).

[44] Yonhap News (2020)

of Wolsong 1 reactor. The President of the KHNP has also been indicted on charges of breach of trust and obstruction of business. Their indictments reveal the systemic bias and collusion embedded in the Moon administration's nuclear phase-out policy.[45]

In the meantime, the combination of nuclear phase-out and electricity price controls under the Moon government is now creating a butterfly effect in the market. Most notably, Korea Electric Power Corporation (KEPCO) recorded an operating loss of over USD 600 million in the second quarter of 2021, turning to a loss for the first time in six quarters since the fourth quarter of 2019 (-USD 130 million). In the fourth quarter of 2021, its operating loss snowballed to over USD 4 billion. At the turn of 2022, the company suffered even larger losses such as USD 7 billion in the first quarter, USD 6 billion in the second, and USD 7 billion in the third. As of November 2022, KEPCO's annual losses are expected to reach over USD 25 billion.[46]

The Yoon government has no other options but to "normalize" electricity rates and other utility bills to tighten energy consumption and to ensure stable energy supplies by preventing public utility firms from going bankrupt. In an era of growing energy insecurity and growing energy costs, South Korea has felt the perverse effect of a shrinking trade surplus and energy-driven inflation at home. In September 2022, the Yoon government announced its plan to cut the energy consumption of public organizations by 10 percent. All central and provincial public organizations are required to adopt energy-saving measures, such as limiting indoor temperature and turning off exterior lighting. The government also asked private companies to implement their energy-saving targets and promised in return to extend tax incentives for the development of energy-saving technologies.[47]

In a dramatic turn of events, South Korea's nuclear energy policy has made a U-turn. Upon inauguration, President Yoon promised to "reinvigorate the nuclear-energy industry by reactivating suspended nuclear power plants and resuming building new ones." Acknowledging that an extensive revision to the energy mix is inevitable for South Korea to meet its climate targets, his administration is set to draft the Fourth Energy Basic Plan ahead of schedule to bring back nuclear power generation to the list of major energy sources. Under the new plan, the construction of Shin Hanul 3 and 4 plants will be resumed, and the retirement of aged nuclear power plants will be extended. Nuclear energy will be listed as part of climate-friendly "green" energy sources. Such a policy turn has been accelerated as the global energy crisis is deepening in the wake of the war in Ukraine and international sanctions against Russia.[48]

At the International Ministerial Conference on Nuclear Power in the twenty-first Century, organized by the International Atomic Energy Agency and held in

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[45] Yonhap News (2021); Korea JoongAng Daily (2022)

[46] Lee (2022a, b)

[47] Oh (2022)

[48] Choi (2022); Lee (2022a, b); Song and Lee (2022)

Washington, D.C. in October 2022, Oh Tae-seok, Deputy Minister of Science, Technology, and Innovation Office, confirmed South Korea's redirection of nuclear energy policy to the international audience: "The Korean government is promoting a policy to expand nuclear energy by actively utilizing nuclear power and harmonizing renewable energy rationally."[49] The statement is a self-reflection of South Korea's renewable energy odyssey and a confession that an attempt at carbon-neutral growth has failed without nuclear energy. Will this policy U-turn allow South Korea to navigate the geo-political and geo-economic storms caused by energy crisis or open the Pandora's box once again? A tentative answer to this question is carbon-neutral growth without nuclear energy will be costly and unsustainable in the long term.

5 Conclusion

From a geo-economic perspective, this chapter contributes to the growing literature on the new gold rush toward renewable energy and carbon neutrality by exploring South Korea's costly experimentation of finding a new way forward. In 2017, the former Moon administration set ambitious policy targets to expand renewable energy and develop related domestic industries. The 20 percent target for renewables' share by 2030 marked a clear departure from the conservative position of previous administrations. An updated net-zero target was set at 70.8 percent by 2050. Aside from the feasibility of such ambitious targets, the policy tools—including favorable loan terms, large-scale project-based aid, the RPS system with weighted REC, and the Korean-style FIT model—had elements of prohibited and actionable subsidies under the WTO SCM Agreement.

Intentionally or not, the former Moon administration ignored the fact that export subsidies and LCRs are prohibited under the global trade norms. Aside from the strict residential requirements for renewable energy projects, the preferential treatments extended to small businesses and social cooperatives potentially violate WTO rules. Other supporting measures taken by the Moon government were legally questionable as they were programmed to confer benefits to South Korean renewable energy firms only.

Of course, this does not mean that controversial measures taken by the South Korean government are all WTO-illegal. No one can say for sure until certain measures are challenged in the WTO dispute settlement procedure and the dispute settlement body renders its final decisions. More notably, "everyone's hands are dirty" to the extent that many countries do provide various supports for their domestic

[49] At the previous meeting held in Abu Dhabi, UAE in 2017, the Korean government voiced the exact opposite. Moon Mi-ok, the then-science and technology adviser at the presidential office, resonated President Moon's nuclear phase-out policy: "Over the next 60 years, we are pursuing an energy transition policy that will gradually reduce our dependence on nuclear power and increase the proportion of renewable energy" (Yoo 2022).

industries. Nevertheless, the South Korean case illustrates that, no matter how well intentioned, renewable policies can drift from their original "environmental" purpose as they respond to various political, social, and economic forces.

Renewable energy transition, therefore, requires careful balancing among different policy goals—that is, a trilemma among energy security, energy justice, and environmental sustainability. Abandoning nuclear energy is not a solution to the trilemma. The history of the energy mix policy has proven that the imagined conflict and dilemma between renewables and nuclear energy will eventually lead to distortion in allocating scarce financial and environmental resources. The point can be stressed further in an era of geo-political and geo-economics turbulence in the Indo-Pacific landscape.

There are fewer trade- and environment-restrictive methods to advance renewable energy. For instance, cutting subsidies for fossil fuels can lead to the increasing price competitiveness of renewable energy. Instead of rushing to short-term targets, the Moon administration should have contemplated the way in which solid infrastructure and framework can be established. Until then, there is no other choice but nuclear power.

A highly export-dependent country such as South Korea cannot simply ignore the goal of generating clean and cheap nuclear power in an era of rising fuel prices. Having listed nuclear energy as part of climate-friendly green energy sources, the Yoon administration has pledged to embrace nuclear energy as a main policy tool to accelerate South Korea's goal to zero out carbon emissions. Under the new plan, the pending construction of nuclear power plants will be resumed, and the retirement of aged ones will be extended. It is too early to tell whether this policy U-turn will mark the end of South Korea's trial-and-error experience in renewables or the beginning of a new odyssey. An important policy lesson can still be drawn: carbon-neutral growth without nuclear energy will be costly and unsustainable in the long term. Finally, South Korea's nuclear energy sector is now subject to ever more stringent transparency requirements and public accountability procedures. Many South Koreans hope that it would avoid the same mistakes and pitfalls from the previous decades.

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