

INTERDEPENDENCE THEORY, CHINA AND
AMERICAN SECURITY INTERESTS

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AMERICAN SECURITY INTERESTS

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DISSERTATION ABSTRACT
INTERDEPENDENCE THEORY, CHINA AND
AMERICAN SECURITY INTERESTS

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This research examines how the economic relationship between the United States and China impacts the potential for dyadic conflict. We employed Interdependence Theory to explain this relationship. Our purpose is to examine the strengths and weaknesses of Interdependence Theory as a framework for weighing the potential for conflict between the US and China.

We investigated the reforms Deng started in 1978 and examined how China has economically opened to the world, becoming one of the world's rising economic powers. The remainder of our methodology was designed around four tests. In the first test, we examined the US-China economic relationship unaided by Interdependence Theory methodology. We found that dyadic integration was very high and complex. Similar to

Oneal and Russett, we found that the two states have a very high level of economic integration, which translates into a significant reduction in the potential for conflict. The examination of actual dyadic conflicts suggests but does not prove that the level of conflict has been reduced as a result of Interdependence.

In our next test we examined an alternative interpretation of Interdependence Theory offered by Gelpi and Grieco. They posit that Interdependence's conflict-suppressing influence is diminished if either state is autocratic. This theory would have strong implications for the US-China dyad, but in the end, our research found this variant of the theory is not yet substantiated enough to consider reformulating the overall theory.

The last test was a consideration of Interdependence's value in explaining two dyadic events, China's entry in the World Trade Organization and the 1995-96 Taiwan Strait Crisis. Interdependence was useful for predicting future behavior, and in general the theory is a necessary, if not sufficient, tool for explaining the relationship between conflict and integration. Our policy recommendations supported maintaining economic engagement as a core element of US strategy, creating additional mechanisms to reduce trade friction, and promoting democracy in China in order to further reduce the potential for conflict. In general, our research supports the use of Interdependence theory as a means of both understanding economic relationships and formulating foreign policy.

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TABLE OF CONTENTS

ILLUSTRATIONS	x
CHAPTER	
1. INTRODUCTION	1
Research Questions	1
Background	3
Research Objectives	5
Organization of the Research	7
Expected Results	10
2. LITERATURE REVIEW	12
Introduction	12
Liberalism's Background	15
The Development of Current Interdependence Theory	18
The Basic IT Argument in the Third Wave	24
The Emerging Subvariants of IT	31
Interdependence Theory and China	38
3. METHODOLOGY	42
Introduction	42
Interdependence Theory Models	43
Challenges of Using IT	44
Four Tests for Analyzing Sino-US Interdependence	46
4. CHINA'S POLITICAL ECONOMY	51
Introduction	51
The Deng Era	53
The Current State of China's Political Economy	61
Test 1: A Broad Look at the Nature of US-Chinese Economic Interdependence	81
Results of Test 1: The Nature of US-Chinese Economic Interdependence	99
5. DATA AND ANALYSIS	102
Introduction	102

	Test 2: Sino-US Economic Interdependence using Oneal and Russett's Methods	103
	Test 3: The Impact of new Interdependence Subvariants on the Sino-US case	119
	Test 4: Sino-US Relations in Practice	129
	Results of Test 2-4: Data and Analysis	164
6.	IMPLICATIONS AND POLICY RECOMMENDATIONS	168
	Introduction	168
	Implications for US Policy Makers	169
	Chinese and American National Security Strategies	172
	Policy Recommendations	180
7.	CONCLUSIONS	193
	Introduction	193
	Readdressing the Purpose and Research Questions	193
	Comparing Expected Findings to Conclusions	199
	Topics for Future Research	201
	Conclusion	204
	BIBLIOGRAPHY	206

ILLUSTRATIONS

FIGURES

4.1. Gross Domestic Product	64
4.2. China's per capita GDP	65
4.3. China's real GDP growth, 1992-2004Q4	65
4.4. US trade balances with selected countries in billions of dollars in 2003	83
4.5. Growth in US trade with China, 1989-2003	83
4.6. Shares (percentages) of US imports by country and group, 1990 and 2004	84
5.1. US and China Economic Interdependence	107
5.2. Sino-US MIDs, 1949-1977	114
5.3. Sino-US MIDs, 1978-2001	115
5.4. Polity IV China Trend Data (Source: Marshall and Jagers 2003)	123
5.5. Polity IV country report 2003: China	124

TABLES

2.1 Control Variables in IT testing (1967-1999)	21
4.1 China's merchandise trade with the world in million of dollars, 1982-2003	63
4.2 US merchandise trade with China in billions of dollars, 1982-2003	82
4.3 US merchandise trade with China and China's merchandise trade with the US in billions of dollars, 1982-2003	86
4.4 China's merchandise trade balance with selected partners, 2003	87

4.5 US trade with the world and current account balance in billions of dollars, 1999-2003	89
4.6 US-China trade, 1999-2003	90
4.7 Top destinations for US students, 2003-4	93
4.8 US schools of higher learning, foreign students' countries of origin, 2003-4	93
5.1 US and China population and GDP	104
5.2 US trade with China, in US\$ millions	105
5.3 US and China Economic Interdependence	106
5.4 Sino-US Militarized Interstate Disputes	110
5.5 Sino-US Militarized Interstate Disputes (MIDs), 1978-2001	112
5.6 Sino-US Militarized Interstate Disputes (MIDs), 1949-2001	113

CHAPTER 1
INTRODUCTION
Research Questions

In the late 1980s, those with an interest in policy toward China began a major reconsideration of the US-China strategic relationship and the assumptions that formed the foundation of that relationship. As the USSR faded from the scene and China achieved strong economic growth, the split between those who sought to engage China in order to liberalize its society and those who sought to contain China's increasing power has widened. Those who seek to engage China largely won out over those who sought to contain China. This continuity in policy occurred across the span of several administrations, as both Republicans and Democrats have undertaken a strategy of engagement with China.

The policy of engagement is largely based upon or justified by Economic Interdependence Theory. **Interdependence Theory (IT) specifies that greater economic and social interconnection between states results in greater levels of cooperation and less interstate conflict.** The proponents of IT, such as John Oneal and Bruce Russett (1997), have a small but impressive body of empirical evidence to support their credible notion that trade reduces armed conflict in dyads. However, new research now suggests that Interdependence has different influences in specific cases. Recent research (Christopher Gelpi and Joseph Grieco 2003, forthcoming in 2006) indicates that

the conflict-suppressing effect of dyadic Interdependence is markedly lower if the dyad contains at least one autocratic member, such as China. IT may be true, but US-Sino economic relations may not fit the model at its most optimal level because of the characteristics of the two states themselves. These notions may help to explain the casual observation that there continues to be a high level of conflict between China and the United States, despite the recent growth in their economic relations. Using IT as the basis for our policy toward China is problematic, since IT does not provide clear evidence that it is having an effect on a specific potential conflict—the stated goal of an engagement policy toward China. Thus, US policy makers have sustained an engagement strategy upon an evolving theory with a state that has undergone dramatic changes in the past quarter century. This research attempts to reveal what we should expect from an application of Economic Interdependence Theory¹ to this specific case. We hope to amplify when IT is most useful for explaining the nature of the economic relationship between the US and China, when it fails to enlighten us about the relationship, and when we might turn to other international relations theories to explain the nature of interactions. In sum, we hope to see the power and limitations of IT as a tool for policy makers, so they can make decisions with their “eyes wide open.”

In this paper, we will explore the feasibility of IT as a basis for policy. Our purpose is to explore the strengths and weaknesses of Interdependence Theory as a framework for weighing the potential for conflict between the US and China. From these observations, we will develop recommendations for US policy makers.

Background

¹ In this study, we use Economic Interdependence Theory, Interdependence Theory and IT interchangeably.

Beginning in the late 1970s, Deng Xiaoping launched a series of reforms that have transformed China's economy and its relationship with other states. At the start of the reforms, Interdependence Theory was merely a hypothetical matter when applied to China, since the PRC was largely isolated from the world. However, expanding Sino-US trade suggests that IT may be critical for understanding China's future relations with the US. This is because China's economy has become more integrated with the global economic system and its players. At the same time, China's economic power has increased dramatically. Consequently for US policy makers, the matter of Interdependence and its relationship to interstate conflict have considerably more meaning than just two decades ago.

The US strategy of engaging China is based, in part, upon the notion that interacting with Beijing will lead China to join the ranks of advanced nations that live peaceably. Through several administrations, Washington has engaged China using all of its instruments of power: diplomatic, military and economic. As we shall see, the economic changes in the relationship have been very dramatic. This developing economic relationship has national security implications. While the impact of engagement is not universally agreed upon by US policy makers, the United States has gambled that economic integration will help China to develop democratic institutions and become more in tune with international organizations and the norms they represent. In the case of China, the economic component is intended as the vanguard for the other two legs (democracy and mutual membership in international organizations) of what John O Neal and Bruce Russett (1997) call the Kantian tripod. While one can posit other

theories and motivations to explain why the US has been driven to interact with China (e.g., Nixon “played the China card” in order to counterbalance the Soviet Union), engagement with China, with IT as a foundation, remains at the core of our relationship with China.

Proponents of IT hold that as two states voluntarily increase trade (specifically, merchandise trade), the potential for conflict declines. As a corollary, they posit that the fact that the two states might benefit unequally from this trade does not reduce the pacifying effect. In the IT formulation, Economic Interdependence, the independent variable, has an inverse relationship to conflict (militarized dispute), the dependent variable. Economic Interdependence is defined by dyadic merchandise trade. They (1984, 587) define conflict or militarized disputes as an international interaction involving threats, displays, or actual uses of military force that is “explicit, overt, not accidental, and government sanctioned.” Oneal and Russett start with data from the Correlates of War Project. IT is a developing theory, and these basic tenets of IT are the starting point for strains of the theory. As already noted, the strain posited by Grieco and Gelpi (2003) states that Interdependence is less likely to reduce conflict if either state is autocratic. It is these main tenets of IT that will form the basis of our theoretical investigation.

While IT has a compelling attraction to liberal democracies and indeed has consistently shaped US policy toward the emerging China, IT is fraught with several constraints and internal contradictions. First, despite the great credence given IT, it remains controversial. IT critics provide compelling historical examples and theoretical counter explanations to IT. Second, there are many variants of IT and many assumptions

that underlie these variants. This makes the application of IT to a particular case difficult. Third, the terms most important to IT, “merchandise trade” and “conflict” are notoriously imprecise, which complicates the operationalization of IT concepts. Fourth, because IT’s proofs are derived from using a broad spectrum of cases (using pooled data from paired states or dyads), its application may not fit a specific case. Fifth, IT does not address the relative weight it should be given in the context to other theories of international relations. In order to understand the utility of employing IT concepts in regard to China, these issues need to be clarified.

Research Objectives

This research has three objectives:

1. Determine the nature of the economic relationship between the United States and China, using the Interdependence Theory model
2. Develop an understanding of which aspects of IT (if any) apply to the China case, discerning which aspects best explain this unique situation and determining when IT provides a poor explanation of behavior in the relationship
3. Provide recommendations for policy makers on the effect of IT on Sino-US relations

Research Questions. To address these research objectives, we will focus on the following research questions, each of which will be addressed in separate chapters.

1. How and to what degree have the US and China become economically Interdependent?
2. How well does IT explain the nature of the relationship between the US and China?
3. Given a policy of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation?

The scope of this paper will be largely limited to the period after 1978, following the beginning of Deng's economic reforms. This research will NOT attempt to answer whether or not Interdependence Theory is proven by China as a historical example. In other words, this research is not a proof of IT, using China as a case study. Rather, we seek to find the utility and limitations of using the IT perspective. Many studies have been undertaken to demonstrate the general utility of IT and indeed of the broader concept of the Kantian tripod. This researcher is enthusiastic about the work of Interdependence Theory proponents. Yet, such notions must be weighed against the least flattering interpretations of the theory and then compared to alternate explanations. This research also does not seek to discredit or suggest replacing engagement as a strategy but rather seeks to augment this strategy by examining the implications of one of its major theoretical underpinnings.

Utility of this Research. Hans Morgenthau's (1978) noted that one of the great challenges facing policy makers is to distinguish between status quo states (those which

are satisfied with their place on the world stage) and revisionist states (those which seek to overturn the power structure in the international order). In the case of China, US policy is set upon a course of economically engaging China while remaining militarily prepared to contain China. This presents a challenge for US policy makers working on the proper way to engage China, since Beijing's behavior toward the US would be indistinguishable whether it is a status quo state or a revisionist state. Examining one of the theories that underlies engagement (Interdependence Theory) will help address the matter by providing insights into how such a policy actually impacts a state's behavior toward its partner in an economic dyad.

Organization of the Research

This research is organized into seven chapters, as outlined below.

Chapter 1. Introduction. This chapter provides an overview of the research objectives, presents the research questions and details the goals, scope, and significance of the work.

Chapter 2: Literature Review. The primary theoretical focus of this research will be on Interdependence Theory (IT). The main portion of this chapter will delve into the multi-faceted and often conflicting models of IT. We should expect to find that both supporters and opponents have well-developed and documented concepts and that many subvariants of IT have been proposed. We have already briefly introduced several proponents of Interdependence Theory. We identify the work of Oneal and Russett (1997) as being representative of the main empirical argument in support of IT. Our primary

subvariant for investigation will be from Gelpi and Grieco (2003), who find that the conflict-dampening effect of Interdependence is reduced if either state in a dyad is autocratic. Since IT is a subset of liberalism, and its critics come largely from the realists' camp, these ideas will also be touched upon.

Chapter 3: Methodology. This paper will take a policy analysis and implications approach, using the application of a general theory, Economic Interdependence, to a specific case, the US-China dyad. The following steps will be undertaken in this research:

1. An assessment of China's political-economic situation and its Economic Interdependence indicators with the United States (Chapter 4)
2. An interpretation of the independent variable, Interdependence, and the dependent variable, conflict, based upon data from the IMF and Correlates of War project, respectively (Chapter 5)
3. An assessment of how the basic and subvariant tenets of IT apply in the US-China case, with particular attention to the interaction between Interdependence, conflict and China's autocratic political system (Chapter 5)
4. An examination of two dyadic events (the 1996 Taiwan Strait crisis and China's entry into the World Trade Organization), comparing IT and realism in their utility for explaining US and Chinese actions (Chapter 5)
5. An overall assessment of the utility and limitations of IT in the US-Sino case (Chapter 6)
6. Recommendations for US policy makers (Chapter 6)

Chapter 4: China's Political Economy. In this chapter, we will examine the basic facts of both the Chinese political-economic situation and the state of Sino-US economic

relations. We examine Deng's economic reforms from the adoption of its development strategy to the current goals and challenges of this strategy. This background will help to describe the nature of the state and its economy that the US is attempting to shape via its policy of engagement. We then examine the recent history, depth and nature of the economic relationship in the dyad, using IT measures (trade) and other indicators not covered by IT. Our effort here will be to demonstrate the depth of Interdependence, using merchandise trade indicators and the breadth and scope of Interdependence using broader economic and non-economic variables. This effort seeks to answer the first research question: How interdependent have the US and China become?

Chapter 5: Data and Analysis. We examine IT and its main subvariants and determine which has the most relevance for the current relationship between the US and China. We will work with the theories of Oneal and Russett (1997) and Gelpi and Grieco (2003, forthcoming in 2006) as our primary focus. In addition, we will examine the applicability (if any) of the other subvariants identified in the Literature Review. We also compare how two theories (IT, which is a component of liberalism, and realism) would interpret two short cases: the 1996 Taiwan Strait and China's entry into the WTO. This chapter addresses the second research question: How well does IT explain the nature of the relationship between the US and China?

Chapter 6: Implications and Policy Recommendations. Here we delve into the policy implications for the United States. We investigate the implications which are driven by our Economic Interdependence with China. We offer policy recommendations that address the impact of IT. This addresses our third research question: Given a policy

of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation?

Chapter 7: Conclusions. In this chapter we take a step back to ensure the research has addressed the original research matters. We link the analysis and policy recommendations to the larger discussion about IT and policy toward China. Lastly, we explore opportunities for further research.

Expected Results

The result will be a specific application of IT toward China now and in the near future. While IT will have application for the China case, this researcher expects to see that IT does not apply in every aspect, largely because of the current political system in China. Specifically, while IT works over the long-term to reduce armed conflict, in the case of China, IT's subvariants suggest that the conflict-suppressing benefit from Economic Interdependence will have reduced effects because of China's lack of democracy. While Interdependence is the vanguard for the other legs of the Kantian tripod, Interdependence's relationship to conflict is conditioned upon the other legs of the tripod. Furthermore, we can expect that IT will prove to be a useful but incomplete model for explaining China's behavior in relation to specific cases. Lastly, while we expect to see a reduction in armed conflict over the long-term, non-military disputes will tend to increase. Engagement is an appropriate long-term strategy for the US, but policy makers need to be aware of the limitations and ramifications of the Interdependence Theory which underlies this strategy. While Interdependence may have a reward in the

form of a peace dividend, much of the effect of that prize will not come until China successfully reforms its political system.

CHAPTER 2

LITERATURE REVIEW

Introduction

Interdependence Theory has a long lineage going back to the very foundations of Western philosophy. Interdependence Theory, in fact, is a component of liberalism, arguably the dominant political philosophy in the world today. Despite the fact that liberal philosophy remains a foundation of foreign policy, many liberal concepts, including Interdependence Theory, remain controversial among academicians. A recent exchange among academicians about the concepts of IT and the related topic of Democratic Peace Theory shows the divide in academia. Oneal and Russett (1997) started the latest round in this debate with an ambitious defense of the links among Interdependence Theory, other Kantian peace theories, and reduced interstate conflict. Their article, *The Classical Liberals were Right*, was intended to silence any doubters with thoroughly vetted empirical evidence. But soon after, Benjamin Fordham and Thomas Walker (2002) presented a paper on *Democracy and Militarization: Were the Classical Liberals Right?*, calling into question Oneal and Russett's findings. Erik Gartzke's 1998 article, *Kant We All Just Get Along* tried to bring peace to the warring factions. Later, though, Gartzke (2003) himself piled on the assault with *The Classical Liberals were Lucky: A Few Thoughts about Interdependence and Peace*. Hyung Min

Kim and David L. Rousseau (2005) in their unpublished manuscript took a balanced approach with *The Classical Liberals were Half Right (or Half Wrong)*. Gartzke and Li (2003a) then attempted to solve the dispute over the interpretation of the Interdependence data, but they were taken on by Barbieri and Peters (2003) in an exchange of articles called *Measure for Measure* and *Measure for Mis-Measure*, respectively.² Gartzke and Li (2003b) had the final word in *All's Well that Ends Well*, although it was not clear that any party was satisfied. With apologies to Shakespeare and all whimsy aside, there is a point: IT remains an ongoing and unresolved academic matter despite the prominence of IT in our national security philosophy.

Modern Interdependence Theory is probably best represented by the works of John Oneal and Bruce Russett (referred to as OR hereafter). In the coming pages we will see how they masterfully advanced the core notion that Interdependence reduces conflict between the members of a dyad. Much of the theoretical work in this research will revolve around their model. But, as noted above, IT is developing, so we will explore several ideas that build upon (or deconstruct) OR's concepts. Chief among these new ideas (or subvariants of IT) is the work of Christopher Gelpi and Joseph Grieco (2003, forthcoming in 2006) who are referred to as GG hereafter. As we noted in Chapter 1, GG attempt to show that Interdependence between dyads involving at least one autocratic member, such as the US-China case, has a markedly lower level of reduced conflict when

² An earlier and related argument over Democratic Peace Theory in MIT's *International Security* between Christopher Layne ("Kant or Cant: The Myth of the Democratic Peace") and Bruce Russett ("The Democratic Peace: 'And Yet It Moves'") has essentially been settled in favor of the Democratic Peace Theory argument.

compared to the Oneal and Russett model. This argument is significant for several reasons:

1. GG show that their idea has a large and measurable impact on IT effects.
2. This subvariant directly addresses IT, while the other subvariants we examine are more tangential and are tied to the other two legs of the Kantian tripod.
3. GG use Oneal and Russett's data and methodology, and OR have not directly disputed their findings.
4. This concept directly relates to subject of this research, since China's fragile and non-democratic political system is central to the Sino-US security relationship.

We begin this chapter by exploring liberalism, the philosophy underpinning IT. We will look at the three waves of recent IT development, followed by an inspection of its conceptual mechanisms and IT's core arguments and research models. We then take a brief look at IT critics. Next, we look at the most important subvariants of IT, which have emerged in recent years, emphasizing the work of Gelpi and Grieco. We will make a critical examination of the challenges of attempting to work with IT as a theoretical construct. Lastly, we look at some of the literature that specifically addresses Economic Interdependence Theory as applied to the Sino-American situation. This will conclude the analysis of the theoretical question being examined.

Liberalism's Background

Liberalism, as a core foundational concept, has many variants and strains, several of which are now in direct contrast with one another. However, all have the same basic foundational tenets in the form of classical liberalism. Amy Sturgis (1994), writing for The LockeSmith Institute, identifies four items as being at the core of classical liberalism:

1. An ethical emphasis on the individual as a rights-bearer prior to the existence of any state, community, or society
2. The support of the right of property carried to its economic conclusion, a free-market system
3. The desire for a limited constitutional government to protect individuals' rights from others and from its own expansion
4. The universal (global and ahistorical) applicability of these above convictions
(Amy Sturgis 1994)

Thus, Sturgis breaks down the liberal concept as involving: the individual, a free market system, limited constitutional Government, and universality. Sturgis explains that liberal ideas have evolved from antecedents in Western thought. The Greeks conceived of a social contract; the Roman's had Cicero's version of natural law; and Renaissance philosophers cultivated economic and political thought that reflected earlier Christian thinking; and Protestantism placed the individual into a new relationship with his God, his physical environment and his government.

For Sturgis (1994), all these strands came together in the person of John Locke (1632-1704). As the founding father of classical liberalism, Locke articulated an integrated vision of these emerging concepts, thereby laying the framework upon which others would expound the many variants of liberal thought. Sturgis sees Locke's contribution as coming from his respect for law, his view of humanity as essentially good, his notion that the consent of the governed is a prerequisite for legitimate government, and his belief that the right to personal property is the heart of economic prosperity and political freedom.

If John Locke is the father of classical liberalism, Immanuel Kant (1724-1804) is the father of the peace variant of liberalism. His masterpiece, *Perpetual Peace*, published in 1795 lays out his view that representative government leads to governance that is more responsive to a broader segment of the population. In Kant's view, such societies seek economic goods through mutually beneficial trade and are less likely to pursue war, since such conflict has little benefit for the broader population.

The importance of the economic factor of liberalism was expounded through the ideas of Adam Smith and Thomas Paine. The Manchester School and, in more recent years, Norman Angell in *The Great Illusion* (1910) argued that the modern era had made the concept of gaining resources through war obsolete. In other words, industrial societies would no longer conduct wars of conquest. World War I quickly made a mockery of Angell's notion although the broader concept of the inverse relationship between economics and conflict survived. While these thinkers and others built upon Kant's ideas, his main propositions remain the common starting point for researchers in modern thinking on liberalism, including Economic Interdependence Theory. For the

purposes of this paper, we will consider the Kantian tripod as described by John Oneal and Bruce Russett (OR).³ They (Oneal and Russett 1997, 1999b; Russett and Oneal, 2001) see the three parts of the Kantian vision as consisting of: Democratic Peace Theory, Economic Interdependence, and Joint Intergovernmental Organizations (IGOs) membership.

Oneal and Russett (1997) view the first leg of the tripod, Democracy, as an expression of the Democratic Peace Theory which states that democracies rarely, if ever, fight each other although they do tend to fight non-democracies at a high rate (Rummel 1995). Here they contend that Democratic Peace is proven. While this conclusion may be too strong, since the theory is still disputed by realists and others, Democratic Peace Theory has the strongest empirical support of the Kantian tripod and is generally considered to have the most direct impact on conflict. As Michael Doyle (1983) observed, the concept that democracies do not fight each other is "the closest thing we have to a law in international politics." In contrast, Kant's International Governmental Organizations leg of the tripod is considered to be the weakest of the three. This theory posits that dyads which belong to the same international organizations are less likely to become engaged in military conflict. This leg is by far the least researched of the trio of theories, and its validity remains an open question. Indeed, the few empirical studies on this leg tend to show the weakest correlation to conflict. The last leg of the Kantian tripod is IT, the theoretical proposition which we will examine in more detail.

³ Oneal and Russett are the preeminent proponents of Kantian peace theories. Their interpretation of Kant has come under criticism for articulating ideas Kant did not hold and ignoring those he did. Suffice it to say that Kant is to liberalism what Clausewitz is to warfare and St. Paul is to Christianity – great founts of wisdom who can be interpreted to support any variant of the subject matter. Despite this controversy over the Oneal and Russett read of Kant, we will follow the lead of other IT researchers who have used Oneal and Russett's take on Kant as a convenient starting point.

Democratic Peace Theory, as noted, is a widely accepted concept in International Relations. While not an irrefutable truth, the evidence is very strong. Applying Democratic Peace to evaluating the relationship between the US and China poses several problems. First, if Democratic Peace Theory is true, then there can be little new understanding gained from this concept by applying it to another case. Second, there is no democracy in China today, so the theory is not yet in play as restraint on conflict. While nascent democratic trends have been observed in China, no scholar would claim that this would allow us to test the theory. Similarly, the IGOs leg of the tripod lacks a strong history of research and is considered to be the weakest of the three Kantian legs in reducing conflict between states. So we focus on Economic Interdependence theory (IT), in part, because there is reason to believe there is growing Interdependence between the US and China and, in part, because considerable research has been done in developing the foundations of IT. In fact, many who support engagement with China see Economic Interdependence as a catalyst to introduce democratic ideals and institutions into China. As we shall see, there is strong reason to believe that the three legs of Kantian tripod work together, and Interdependence could be the vanguard into China for all three.

The Development of Current Interdependence Theory

Using the Kantian tripod, we have distilled IT from its liberal background and affixed it to a specific strain of peace theory. Now we will trace the relatively recent development of Interdependence Theory. Keshk, Pollins and Reuveny (2004) see modern Interdependence Theory as developing in three waves. The first wave is

reflected in the work of Solomon Polachek (1980), who began from the premise that “trade brings peace.” These researchers used the dyad as their unit of analysis and offered evidence that increased merchandise trade ties reduce the likelihood of conflict.

The second wave produced the most ardent supporters and critics of IT. These included realists, such as Katherine Barbieri (1996, 2002, 2003), who believed that under some circumstances trade *promotes* dyadic conflict. This second wave also produced John O Neal and Bruce Russett (1997), who we have noted provided empirical support for the “trade brings peace” camp. The second wave saw the undertaking of numerous empirical studies that often used the same databases to produce results which contradicted each other.⁴

The third wave of IT thinking is melding the competing and contrasting theories and evidence by attempting to “delineate the boundary conditions and contingencies that temper and limit the liberal claim” (Keshk, Pollins and Reuveny 2004, 6). The latest developments in this third wave will be covered below.

Conceptual Foundations of Modern Interdependence Thought. The three waves reflect some basic concepts and theoretical mechanisms about how Economic Interdependence influences relations between states and the potential for conflict. One of the earliest concepts to explain the IT impact on conflict came from Eugene Staley (1939). He further advanced the proposition that international trade would replace the need for land conquest to satisfy economic needs. Others, such as Michael Doyle (1997), argued that increased economic relations would create a kind of international community, promoting communications between individuals and companies and other subnational

⁴ The most comprehensive review of the second wave can be found in Susan M. McMillan (1997).

actors. Subnational economic actors (interest groups) are also seen as becoming proponents of the foreign trade upon which their fortunes depend, so they pressure their home government to seek peaceful solutions to disputes. At the systemic level, IT creates an international economic order, which requires standards of behavior to enter and remain in the market and which values stability in the system. These concepts, which exist across several levels of analysis, lack specificity and are therefore difficult to prove. Others (Polachek 1980) argue that states as a whole realize a gain from trade, and thus the government attempts to maintain such trade, since societal goods are a function of government. Lastly, IT, like the other two legs of the Kantian tripod, can be explained through a normative understanding; that is, trade builds common values. These shared values include the maintenance of international order through reduced conflict.

IT Research Models. Barbieri and Schneider (1999, 395) examined the leading writers on IT, both proponents and critics, from 1967 to 1999. They show how theory-testing evolved, eventually using as many as eight control variables. They also demonstrate the development of the data from dyads at war over short periods (10 years) to all dyads covering up to 115 year periods.⁵ The control variables used in these analyses are listed in table 2.1.

⁵ ONeal and Russett (1997) set a standard followed by many other researchers. They began by measuring militarized interstate disputes (MIDs) between “major power” dyads during the 1950-1985 time frame. Their source database is the Correlates of War Project, originally at the University of Michigan and now at Pennsylvania State University.

Table 2.1 Control Variables in IT testing (1967-1999)

Alliance Ties	Contiguity	Concentration of Power	Defense Expenditures
Economic Growth Rates	Economic Openness	Geographical Proximity	Hegemony
Socio-economic and Demographics	Political Change	Price Elasticity	Political Relevance
Politically Relevant Dyads	Regime Type	Relative Power	Temporal Dependence

The Critics of IT. Barbieri and Schneider's (1999) review of IT studies demonstrate how much work both proponents and critics of IT have done in recent years in this field. The number and variety of the control variables suggest the complexity of collecting useful data. As we note below, other international relations theories (particularly realism) continue to resist the IT concept, despite the current progress being made to find common accord among those in the IT community.

Albert Hirschman ([1945] 1980) believed that trade can include winners and losers. Realists would call this a shift in the balance of power—the key catalyst for conflict in the realist vision (Mearsheimer 2001). Realists focus on the inequities of relative gains, while liberals focus on the mutual benefit of absolute gains—even if they do not accrue equally to both parties. Similarly, the costs or decreased benefits from ending a trading relationship are not necessarily similar for two countries, thus impacting the balance of power. Others argued that trade itself can become a cause for disputes and thus increases the opportunity for armed conflict.

Many of the empirical efforts in the 1990s to demonstrate that trade causes conflict have been rejected by the academic community. This was due in large part to the negative evaluations of the measuring methods used by IT opponents and by the continued, if uneven, success IT proponents have had in expanding their empirical evidence. Despite IT proponents' best efforts to prove the value of IT, they have not fully been able to dismiss the theoretical argument of realist and others that trade provides uneven benefits for the parties in a dyad. As noted earlier, Hirschman ([1945] 1980) posited that trade is perceived as having different gains for the two parties involved. Invariably, one party gains more than the other, so one theoretically has the upper hand in the relationship. This is true directly through trading activity itself and may also occur in the cost of severing and replacing the source of the goods. This is essentially a realist argument (Waltz 1979). Somewhat ironically, neo-Marxist and dependency theorists, coming from very different philosophical foundations, sound similar themes in their arguments about exploitation of the weaker power. Others, such as realist Barbieri (1996), take a more global view and argue that symmetrical trade decreases the opportunities for conflict, while asymmetrical trade increases the chance for violent conflict. Robert Keohane and Joseph Nye in *Power and Interdependence: World Politics in Transition* (1977) were more supportive of the general concept of IT, yet also found the potential for conflict in asymmetrical trade.

Gartzke and Li (2003a, 554) suggested that Interdependence is too complex to truly measure. Indeed, one of the main dividing points between IT researchers is the method they use to observe Interdependence between states. Mansfield and Pollins (2003), building upon the work of Keohane and Nye's 1997 book *Power and*

Interdependence: World Politics in Transition, identify three measures of Interdependence – Dependency, Openness and Gain. *Dependency* or *Vulnerability* focuses on a variety of measures of bilateral trade relations.⁶ This is usually expressed as the total of merchandise trade between two states as a percentage of each state's national income as measured by GDP (Oneal and Russett 1997, 275). As we shall see, this is the measure OR identified as their primary measure of Economic Interdependence. *Openness* is meant to measure the level of exposure an economy has to all of its trading relationships. It is usually expressed as a ratio of merchandise trade to overall economic output. Openness is the most commonly used measure of a nation's integration into the global economy rather than to another state. *Gain* is a measure of the benefits a state receives from trade. It is understandably difficult to measure, and it is not used often. Proponents tend to rely on measures that support their facts, so liberals use openness and absolute gains, while realists use vulnerability and relative gain (Mansfield and Pollins 2003, 12-13). In this research we will focus on dependency (vulnerability), which addresses dyadic relationships rather than openness which measures an individual state's level of engagement with the global economy.

The Current State of Interdependence Theory. As IT entered its third wave, we can identify the four major views of IT:

1. Those who believe Economic Interdependence reduces conflict (e.g., Oneal and Russett 1997)

⁶ Oneal and Russett and other IT advocates prefer the term dependency, since they see a positive aspect of the relationship, while realists prefer the term vulnerability, since it reflects the imbalance in the relationship.

2. Those who believe Economic Interdependence increases conflict (e.g., Barbieri 1996)
3. Those who believe that Economic Interdependence has no significant impact on conflict (e.g., Gariorowski 1986)
4. Those who believe Economic Interdependence can reduce conflict but only in certain situations of polity (e.g., Gelpi and Grieco 2003, forthcoming in 2006)

The outstanding work for IT in its third wave is to define the characteristics of those majority and minority cases (Mousseau, Hegre and Oneal 2003, 279-280). For this research, we will attempt to determine inter alia if the Sino-American dyad is a case in the majority situation (where Interdependence reduces conflict) or a case in the minority (where Interdependence increases or has no impact on the potential for conflict).

The Basic IT Argument in the Third Wave

Returning to the work of Oneal and Russett, we can construct a basic outline of Interdependence Theory as it now stands. From there, we can describe some of the subvariants of IT that remain actively debated in the third wave. OR's work is a valid representation of IT, because they are the baseline from which critics and proponents have begun their explorations, they have corrected their early shortcomings and expanded their databases, and they have incorporated the arguments and methods of critics in their later research (Oneal and Russett 1997, 1999a, 1999b; Russett and Oneal 2001; Oneal 2003; Oneal, Russett and Berbaum 2003).

OR's Research Design. Oneal and Russett's basic approach is to conduct "pooled cross-sectional time-series regression analysis of data regarding pairs of states (dyads) observed annually" (1999b, 3-11). As we have already noted, they concentrated on all three legs of the Kantian tripod, so they employ several independent variables (which have remained fairly consistent over their years of studies) and then test the three legs (Economic Interdependence, Democratic Peace Theory, and Joint Intergovernmental Organizations [IGO] Membership) against the dependent variable of conflict.

The following twelve factors have played a major role in their statistical analyses as dependent, independent, or control variables:

- a. Conflict. This measure of militarized interstate disputes (MIDs) is the dependent variable. OR define conflict (or more accurately MIDs) as "international interaction involving threats, displays, or actual use of force; it must be explicit, overt, not accidental, and government sanctioned" (Oneal and Russett 1997, 273). OR used data from the Correlates of War Project (Singer 1995; Jones et al 1996) capturing two types of conflict – the onset of military conflict and those conflicts which resulted in actual combat fatalities – to differentiate between the two ends on the conflict scale.
- b. Dependency (or Vulnerability). This independent variable serves as OR's primary measure of Interdependence. OR base their Interdependence measures on a calculation of merchandise trade and Gross Domestic Product. They began using trade statistics from the IMF's *Direction of Trade* (IMF 1997) data and the *Penn World Tables* (Summers et al, 1995) for GDP numbers but have since updated and filled in the gaps in data with work by K.

S. Gleditsch (2000). OR use purchasing power parity to measure GDP. As in the case of democracy below, OR assume that the less constrained state (or less trade dependent state) is the “weak link in the chain of peace” and has the greater influence in determining whether conflict arises, since it faces lower costs if conflict diminishes or stops trade. OR account for both the less and more dependent states in their regression model. In the end, OR found that the less dependent state has the only statistically significant influence in determining the potential for conflict—within the model’s strict controls—and when the initiator of the conflict is undetermined. Dependency (or Vulnerability) is measured as:

Country A Imports and Exports with Country B / Country A GDP.

- c. Trend in a Dyad’s Interdependence. Building on a concept posited by William Domke (1988), OR also tested whether change in the level of Interdependence in a dyad over a limited period influenced conflict. They studied three-year periods among dyads to see the impact on conflict levels, expecting to find that a trend of increasing Interdependence correlates with decreasing conflict. This is a simple trend measure of Dependency (**item b**).

The measure is:

Increase/Decrease of Change for the More Dependent State over three years.

- d. Openness. This is a secondary measure of the independent variable Economic Interdependence noted in **item b** above. William Domke (1988) found that states with higher levels of trade are less like to initiate conflict with other

states. This is essentially a monadic measure of Interdependence with the global economy. OR note that openness is “only modestly correlated ($r = 0.33$) since trade can be shifted from one country to another” (Russett and Oneal, 2001, 147). Again, this is a general rather than a dyadic measure of integration. Openness is measured as a state’s total trade over its total GDP or: Country A Total Trade / Total GDP.

- e. Democracy. This is the second of the three Kantian legs that serve as independent variables. Using the *Polity III* (Jaggers and Gurr 1996) data set, OR devised a state’s composite score by subtracting the Autocratic Score from the Democratic Score for each state in the dyad. The less democratic of the two states is assumed to have the broader freedom of action in the relationship, since democracies are more constrained in the use of force than autocracies. However, OR account for both the less and more democratic states in their regression model.
- f. Political Change. OR again use Jaggers and Gurr’s (1996) *Polity III* data set to determine if changing from one regime type to another increases the short-term risk for conflict (as indicated by Mansfield and Snyder 2002a, 2002b, 2005). OR used a country’s composite score to determine regime type (by subtracting the Autocratic score [-10 to zero scale] from the Democratic score [zero to 10 scale]) and then traced progress from one type to the other over three year intervals (and longer intervals in the most recent studies).
- g. Joint IGO Membership. This is the third of the three Kantian legs that serve as independent variables. Using the *Yearbook of International Organizations*

(Union of International Associations 2000), OR employ a count of joint membership in relationship to the average membership rates for all states.

- h. Capability Ratio. OR attempted to take into account realist arguments that conflict is a result of balance of power gains and losses. The capability ratio attempts to control for power balancing, and the measurement is done by “using the logarithm of the ratio of the stronger state’s military capabilities to those of the weaker in each dyad” (Oneal 2003, 191).
- i. Alliance. Membership in the same security alliance, entente, or neutrality pact reduces the likelihood of conflict. OR assess this dichotomous relationship with a 1 if the states are so linked and a 0 if they are not.
- j. Contiguity and Distance. OR attempted to account for the argument that states which are physically close are more likely to engage in conflict by developing a measure for proximity of national capitals and contiguity. Major powers, as defined by the Correlates of War Project (Singer 1995; Jones et al 1996), are less constrained by contiguity, so OR include a binary variable for major power status in this measure.
- k. Economic Growth. OR wished to control for the possibility that states with growing economies avoided conflict while states with weak or declining economies might have incentives to initiate conflict. They did this by calculating the “lower rate of economic growth in the dyad of real GDP per capita, average over 3 years” (Oneal and Russett 1997, 277).
- l. Expectations of Future Levels of Interdependence. OR tested Dale Copeland’s (1966) theory that expectations of future levels of

Interdependence will determine whether states initiate conflict (see below).

Using their 2003 regression model, OR tested three cases (rising, fall and steady Interdependence).

OR's Findings. Oneal and Russett found that the Kantian tripod is linked to peace. Independently, Democracy, Economic Interdependence, and Joint IGO Membership all reduce conflict. The tripod legs work together, so the cumulative total of the three effects is less than achieved by simply adding the parts. In Oneal's most recent summation of their joint research, Oneal tested the OR findings using six separate models, including models of their critics (Oneal 2003, 196; 200). He found that increasing the measure for each leg of the tripod by a single standard deviation decreased the level of conflict significantly. For the IT measure (**item b** above) risk of conflict was reduced by between 20 and 71 percent, depending upon the model and type of conflict (onset or onset with fatalities) employed. Similarly, openness (**item d** above) reduced conflict in a range from 17 to 32 percent, depending upon the model and conflict definition used.

Oneal's 2003 work includes only data on conflict and Interdependence. In a slightly earlier version, in the book *Triangulating Peace* (Russett and Oneal 2001), OR found that increasing each of the following variables by a single standard deviation decreased the level of conflict by these respective levels: Interdependence 44%; Openness 27%; Democracy 36% and Joint IGO Membership 27%. The combined impact of the three factors in the tripods is 71% (Russett and Oneal 2001, 146, 171).

Other independent variables produced somewhat more ambiguous results. For example, OR originally found that a positive trend in a Dyad's Interdependence (**item c** above) correlated with less conflict, while declining Interdependence correlated with

increased conflict (Oneal and Russett 1997, 281). They reported later, however, that there was no significant relationship here (Russett and Oneal 2001, 150). The findings on the variable Economic Growth (**item k** above) followed the same pattern. OR originally found evidence that it reduced conflict but later concluded it had no impact (Oneal and Russett 1997, 281; Russett and Oneal 2001, 153). OR did not find that an imbalance in trade dependence (asymmetrical trade) leads to more conflict.

According to their findings, OR found that Political Change (**item f** above) *did not* correlate with a short-term increase in the potential for conflict as suggested by Mansfield and Snyder (2002b). In fact in 2003, Oneal, Russett, and Berbaum found that movement from autocracy to democracy has a very rapid impact of *reducing* the potential for conflict (Oneal, Russett, and Berbaum 2003). Finally, OR (**item l** above) found that their model did not support Copeland's (1966) theory that conflict is determined by expectations of future levels of trade.

OR's research also generally supported the expected findings for their control variables. Thus, they found that contiguity and having a major power in the dyad increased conflict. They found somewhat contradictory evidence on whether alliances are correlated with increased or decreased conflict. Also, keeping with realists' expectations, they found that having one state with a preponderance of power (Capability Ratio, **item h** above) rather than a relative balance led to reduced conflict in dyads.

The Emerging Subvariants of IT

Keshk, Pollins and Reuveny's (2004) third wave of IT has not produced a unified theory although several theorists have begun to parse out the nature of IT in specific situations. These IT subvariants are important for three reasons. First, they work to bring together the empirical research studies (and to a lesser degree the theoretical constructs) that have divided IT. They accomplish this by explaining the conflicting results researchers have seen in their studies. Second, the subvariants provide a level of specificity to Interdependence, allowing IT to provide a general theory of international relations while describing the circumstances in particular cases. Third, the subvariants explore the seams between the three legs of the Kantian tripod. This demonstrates the interaction between and strengths of the three legs. These subvariants are examined over the next several pages and will be used in evaluating the state of Interdependence between the United States and China. In this section we consider five such subvariants:

Interdependence and Level of Democracy. Gelpi and Grieco (2003, forthcoming in 2006) demonstrated the interaction between the two strongest legs of the Kantian tripod—Democracy and Economic Interdependence. Gelpi and Grieco (2003, 44-57) show that IT works for democracies but can increase conflict between authoritarian states. They also provide evidence that Interdependence has a greater impact in the present era. Building on the work of Kant and Bueno de Mesquita, they first tie democracy to IT. They posit that leaders of democracies are beholden to successful policies in order to maintain power and that the best way to achieve economically successful policies is to pursue open trade. This is in contrast to autocrats whose policies need not benefit the

general population and whose power may be threatened by openings to international trade. Gelpi and Grieco believe this explains why IT has the greatest impact on lowering conflict between democracies, reduced influence on mixed traders (democracy and autocratic) states and (in contrast to OR and in support of Barbieri) actually increases the potential for conflict between two autocratic states. In a democratic-democratic dyad, the researchers found that increasing trade from a base of 0 to .9 percent of GDP of the less dependent state decreased the potential for conflict by 67 percent (Gelpi and Grieco 2003, 44-57). In a democratic-autocratic dyad, similar increases in trade reduced the potential for conflict by only 12 percent.

In their model, Gelpi and Grieco start with the variables, data and methods provided by OR. They also add an interaction measure to assess their hypothesis that “the impact of Interdependence depends on the presence of democracy” (Gelpi and Grieco 2003, 50). Their 2006 study questioned OR’s notion that only the less dependent state’s action are statistically significant. To GG this meant, that the less dependent state was always the conflict initiator, a position not supported by the Correlates of War database. So, GG’s 2006 work included an interaction variable tied to democracy level, dependency level and whether the state was the initiator or recipient of the conflict. In this case, Gelpi and Grieco again found that democracy and dependency were tied together, and autocratic states were not constrained to initiate conflict with states with which they were tied to by high levels of Interdependence.

Interdependence and Transition to Democracy. The next item cannot be considered as a pure subvariant of IT, since it arguably belongs to the Democratic Peace Theory. However, this subvariant is important. It contradicts findings by OR and is, like

the GG subvariant, tied to one characteristic, the potential for political change, that is important for our case. Previous studies have treated democracy as a static variable, usually by typifying dyad members as a particular regime type, e.g., democratic or autocratic. Several researchers, most notably Mansfield and Snyder (1995, 1996, 2005), have demonstrated that the transition from authoritarian to democratic regime type increased the potential for conflict. Specifically, they found that autocratic states that made an incomplete transition to democracy were more likely to become involved in interstate militarized conflict than other states. This is due to the fact that old elites are threatened by the coming transition and find they need to move before the weak democratic institutions can resist. This leads to logrolling (self-preserving horse-trading between threatened interest groups), risky adventurism in the hopes of achieving short-term goals for the threatened elite group, and hypernationalism as a means of retaining legitimacy. In a dyad with one of more members in the state of incomplete democracy, the impact of Economic Interdependence on the potential for conflict is dampened.

Mansfield and Snyder (2002b) start with the same data that OR use, but use different *Polity III* (Jagers and Gurr 1996) data set determinants for defining regime transition. They attempt to break out the category of states that make a quick and complete transition to democracy (e.g., Spain) to those that make an incomplete transition to democracy (e.g., Russia). Whereas OR look at *Polity III* data to develop a single measure of whether a state was democratic or autocratic, Mansfield and Snyder look at four specific measures in the data set. These measures are:

- a. A composite index of regime type (-10 to 10 scale)
- b. The extent of the constraints placed on the chief executive (1 to 7 scale)

- c. The openness of executive recruitment (1 to 4 scale)
- d. The competitiveness of political participation (1 to 5 scale)

Using these four measures plus the other control variables used by OR, Mansfield and Snyder tested regime transition (during five year periods) and its impact on conflict (2002b). They found:

certain types of democratic transitions markedly increase the risk of such disputes within dyads, even when economic and political relations between states are taken into account. Particularly prone to violence are dyads in which either state undergoes an incomplete democratic transition: that is, a shift from an autocratic to a partially democratic (or anocratic) regime that stalls prior to the establishment of consolidated democratic institutions. (Mansfield and Snyder 2002b, 529)

Mansfield and Snyder (2002b, 537-538) found that the potential for conflict increases by 50 percent between the members of a dyad when at least one member is in a state of incomplete transition to democracy. They are particularly concerned with the potential for states to make incomplete transitions to democracy. OR, looking at the somewhat different variable of generic political change, found no indication that such change correlates with increased violence.

Interdependence and Preferential Trade Agreements. OR's third leg of the Kantian tripod is International Organizations, which include a wide variety of social, political, security and economic bodies. Recent studies have focused on the power of Preferential Trade Agreements (PTAs), which deal with a specific type of international

organization, thus refining OR's initial theory. PTAs deal with trade, the core essential of increasing Economic Interdependence, so PTA studies have often been classified within IT research, while the broader definition of International Organization has constituted its own, albeit limited, body of research. For the purposes of this research, we will treat PTAs as a subvariant of IT. Mansfield and Pevehouse (2000) demonstrate that membership in Preferential Trade Agreements reduces the likelihood of war between two states. They define PTAs as free areas, customs unions and common markets, noting that almost every member of the World Trade Organization (which is not a PTA) also has membership in one of fifty PTAs now in existence. Starting with OR's data on Joint IGO Membership, Mansfield and Pevehouse found that states that are not in a PTA are one-third to one-half more likely to become involved in a military conflict than those states in a PTA. Furthermore, they found that PTA membership has a compounding effect on trade and conflict. For example, an increase in trade between two states reduces conflict, but a similar increase in trade between states that are PTA members has an even greater impact on conflict. This they explain by the fact that PTAs act as a venue for working out all bilateral issues, including trade. In addition, other regional partners become active in potential disputes in order to prevent disruption in regional trade (Mansfield and Pevehouse 2000; Mansfield 2003). In their later work, the researchers found that their studies did not support OR's evidence that generalized increased joint IGO membership reduced conflict. For Mansfield and Pevehouse, it is PTA membership that makes the difference regarding IGOs and conflict. Joint membership in other IGOs, including global, economic organizations like the WTO, does not reduce conflict.

IT and Trade Expectations. As noted above, Dale Copeland (1966) developed a theory that attempted to address both liberal and realist views about trade and conflict.

As he noted

Interdependence can foster peace, as liberals argue, but this will only be so when states expect that trade levels will be high into the foreseeable future. If highly interdependent states expect that trade will be severely restricted—that is, if their expectations for future trade are low...the most highly dependent states will be the ones most likely to initiate war... In short, high interdependence can be either peace-inducing or war-inducing, depending on the expectations of future trade.

(Copeland 1966, 7)

Copeland goes on to provide a rich theoretical construct and two historical case studies (Germany prior to both World Wars), but he does not provide an empirical test of his theory. As noted above, OR developed their own method for testing this concept, and found no evidence to support Copeland. Still, the academic discussion on this issue remains open.

Interdependence and Development. Another subvariant we could examine comes from Havard Hegre (2000). Hegre holds that IT works best in countries with developed economies. Hegre builds upon the work of Richard Rosecrance (1981,1986), who examined why states chose peaceful trade policies over wars of conquest to meet their resource requirements. Rosecrance held that developed states are dependent on trade to meet their resource needs and that the material and political costs of conducting war are greater in developed states. Using a gravity model, Hegre found that economic

development influences the degree that Interdependence reduces conflict. Using GDP per capita and energy consumption per capita as indicators of development, he concluded that: the greater the development level, the greater the IT impact. In the case that one of the two traders was not developed, the dyad was considered to be not developed, and thus the conflict reduction impact of IT was diminished. While, Hegre apparently contradicts his own research in Mousseau, Hegre and Oneal (2003), other researchers (Lemke 2002) continue to hold onto the concept that development and IT are linked. Still, of the subvariants we have discussed, the empirical evidence is weakest here. For these reasons, our consideration of this subvariant will end here, pending additional determinations of its validity.

Relevance of IT's Subvariants to This Research. Below we summarize the subvariants we will consider in this research. GG's theory will be addressed in length in our data examination and analysis, while the others will be only be addressed as corollaries to our main effort.

1. Interdependence and Level of Democracy. Gelpi and Grieco's modification of OR's model lies at the core of our research. This is due to the fact their ideas directly examines the relative weight Interdependence produces in a given relationship. GG use OR's own data and methods to link IT to a dyad involving both democratic and autocratic states. Furthermore, GG's focus on political systems is at the heart of the matter between the US and China and thus at the heart of this research.
2. Interdependence and Transition to Democracy. Mansfield and Snyder posit (and Oneal and Russett dispute) that states in transition to democracy are more

prone to violence, which suggests (but does not directly demonstrate) that Interdependence might lead to more conflict between US and China.

Mansfield and Snyder's weakness is that they do not directly link Interdependence and conflict.

3. Interdependence and Preferential Trade Agreements. Mansfield and Pevehouse show that PTAs reduce conflict more so than other common membership in international organizations.
4. Interdependence and Trade Expectations. Dale Copeland holds that Interdependence's influence can be weakened by either partner's expectations that trade might change. Copeland's theoretical construct lacks a proof.
5. Interdependence and Development. Harvard Hegre's concept linking trade, develop and conflict will not be considered again for the reasons given above.

Interdependence Theory and China

Clearly, the amount of research on IT is significant. Yet the amount of research on case studies and the application of IT is extremely limited. This is true in part because IT's validity is only now being accepted. Another reason may be the challenge of trying to apply the theory to current, rather than historical cases (Ripsman and Blanchard 2003). Consequently, there is very little literature which approaches China's relationship with the US using IT. This is true despite the great volume of ink spilt in recent years on China's economic development and its role as a growing regional and global power. One can also find a great many works which focus on China as an emerging regional and

global threat to US interests. Many of these works consider the pros and cons of the policy of engagement, which is based upon on IT. Again, most of these works do not make the direct connection to the reliability of IT as a predictor of potential conflict between the US and China.

Most of the research that looks at US policy at China starts with engagement as the strategy. This is useful for understanding the policy in a generic sense but fails to consider the meaning of the IT that underlies the policy. Of those researchers who consider engagement from an IT perspective, the 1998 assessment from Paul Papayoanou and Scott Kastner is the most useful for our purposes (Papayoanou and Kastner 1998). Their purpose is to determine whether those elements within China that support Economic Interdependence have the power to prevail in policy decisions against those who do not value China's current economic policies. The researchers draw on historical examples prior to World War I (Tsarist Russia and Wilhelmine Germany) where nondemocratic powers had important international economic interests but chose divergent paths on whether to sustain those relations or abandon them in pursuit of more conflictual policies. These lessons are then applied to China and the US.

Papayoanou and Kastner (1998, 8) believe we can weigh the future intent of China's leaders to pursue armed conflict by seeking to "understand whether the institutions of the nondemocracy are likely to permit internationalist economic concerns to wield significant influence in the policy process." The researchers consider pro-Interdependence forces in China to have a considerable advantage over those who have reason to feel threatened by such policies. The former forces are judged to be widely spread throughout the different levels of government and to work in fast growing

industries. Those who might be threatened by such policies (state owned enterprise, heavy industry and those agencies invested in the centralized planning system) have either been co-opted by subsidies or found other benefits in the economic growth of the last quarter century.

One of the most useful works on the current state of IT was recently edited by Edward Mansfield and Brian Pollins. *Economic Interdependence and International Conflict: New Perspectives on an Enduring Debate* (Mansfield and Pollins 2003) includes chapters from many of the leading writers in this field, both proponents and critics. Two chapters briefly examine the place of IT in regard to Sino-US relations. As for the impact of IT, Bruce Russett (2003, 168-171) notes that trade remains the strong suit for decreasing the potential for decreasing conflict with China, because the International Organizations component of the tripod is weak, and the future of democracy in China remains an open question. He also concludes that economic engagement with China is a policy without an attractive alternative. It would be difficult to persuade the world to impose sanctions on China, and the unilateral variety would surely fail, since other states would fill the void (Russett 2003, 169).

Michael Mastanduno (2003, 175-177), like Russett, begins his chapter from the premise that IT will tend to reduce conflict with China. However, he places IT in context, starting (as we did in Chapter 1) from Hans Morgenthau's (1978) observation that policy makers must distinguish between status quo and revisionist states. A state which seeks to replace the dominant power, in this case the US, could very well behave in exactly the same fashion as a status quo state or a state that could be persuaded to accept the status quo. Failure to understand this dynamic would mean that a revisionist power could

acquire the capability to further its goals – all in the name of economic engagement (Mansfield and Pollins 2003, 180-185). This is meant to be a cautionary tale for those who develop policy for China. Mastanduno makes the policy maker realize that IT holds three risks. The first risk is that Interdependence Theory may be incorrect or inapplicable in a specific case. The second risk is that a policy of active engagement may or may not actually lead to Economic Interdependence with the target state. Finally, a policy of IT includes the risk that the target state will be disingenuous about the very basis of its relationship with the other state, i.e., is it a revisionist state or not? Russett and Mastanduno get pretty far away from the narrow focus of Interdependence Theory, but they do remind us that the use of economic engagement is a state strategy, and informing state policy is the ultimate goal of this research.

Other than OR's short examination of the Sino-US relationship, which we discuss in Chapter 5, no other research sheds much light on the topic of this dissertation – the influence of IT on the potential conflict between the US and China – although many works discuss the matter in broader terms as noted above. Having delved into the nature of the theoretical foundation of the US policy toward China, it is now time to turn toward the context in which we will apply IT – China and its economic relationship with the United States.

CHAPTER 3

METHODOLOGY

Introduction

If our analyses are to be relevant to policy makers, we must be as sure as science allows that the Kantian influences cause a reduction in interstate conflict. (Oneal, Russett and Berbaum 2003, 374)

The above quote from Oneal, Russett and Berbaum (2003) reveals the ambition of IT – to make it a useful tool for the policy maker. This research pursues a similar goal of providing practical assistance to policy makers. Previous IT studies have been either theoretical constructs or empirical proofs from many pooled cases, with very little on application to particular cases. This research attempts to take that next step by applying IT in a specific case (the US-China dyad). We do this by creating four simple “tests” of IT in this dyad. These tests, which will be conducted in Chapters 4 and 5, represent the bulk of the effort of this research. These four tests represent an approach to the research question which recognizes the complexity of the theoretical construct of IT and the intricacy of the economic relationship within the dyad.

This chapter explains our methodology in three parts. First, we will re-introduce the research model used by the Interdependence theorists that we examined in Chapter 2. We then examine the challenges of using Interdependence Theory. Lastly, we develop

the four tests that will be the main mechanisms used to address our research questions and explore the strengths and weaknesses of IT.

Interdependence Theory Models

Returning to Chapter 2, we drew three major propositions that will be examined in the main effort of our study:

1. Economic Interdependence reduces conflict (Oneal and Russett's definition of IT).
2. Economic Interdependence in most cases reduces conflict, but Interdependence can increase conflict in some cases (our interpretation of the current state of IT in the third wave).
3. The conflict-suppressing effect of dyadic Interdependence is markedly lower or non-existent if the dyad contains at least one autocratic member (Gelpi and Grieco's concept) which we judge best addresses the importance of IT in regards to the US and China relationship.

We also acknowledge three minor propositions (subvariants) from our literature review:

- a. States in transition to democracy are more prone to violence, which suggests that Interdependence might lead to more conflict between the US and China (Mansfield and Snyder 2002b).

- b. Preferential Trade Agreements reduce conflict more so than other common membership in international organizations (Mansfield and Pevehouse 2000).
- c. Interdependence's influence can be weakened by either partner's expectations that trade might change (Copeland 1966).

These positions involve research models that attempt to measure the variables we discussed in Chapter 2. These models and methods are key to understanding the nature of Interdependence Theory, so we explored them in depth in the previous chapter. The quantitative methods OR developed for measuring Interdependence variables are central to it, but these methods do not represent the methodology of this qualitative research effort. We instead focus our efforts on four tests of IT in relationship to our dyad.

Challenges of Using IT

Chapter 2 investigated the arguments among academicians in recent years on the validity and meaning of Economic Interdependence. These varieties of opinion regarding IT are not the only challenges for employing IT. To better understanding the complexity of using IT, we will investigate these three categories of challenges: definitions, methods and data.

Definitional Challenges. The single greatest problem with IT is that the empirical research never truly attempts to measure Economic Interdependence. Rather, merchandise trade is identified as a stand-in for Interdependence. While this captures the main portion of the concept, such activities as services exchanges, foreign direct

investment and capital flows are not accounted for in these studies.⁷ The definition of conflict is also not a constant with most studies focusing on militarized disputes and neglecting other, non-violent conflict, which can also be very important.

Methodological Challenges. In our Literature Review, we covered the variety of research models used by the different camps within IT. We note that many of the empirical studies have used pooled data. While this is useful for ensuring that all types of relationships are covered, it also means that very different types of relationships are being observed and measured. So, trade between China and the US is covered, as well as trade between Laos and Barbados. Consequently, pooling the data removes the chance to examine the impact of relevant dyads. This has hampered efforts to break out the distinctions between different types of dyadic relationships. Most researchers have also acknowledged that peace increases trade or the “trade follows the flag” proposition. In other words, this is a case of simultaneity; the factors of violence and peace interact. Some work has been done on this matter, yet most researchers tend to ignore this interaction. This is not a fatal blow to any single study, since the interaction is clearly weighted in favor of IT (Keshk, Pollins, Reuveny 2004; Mousseau, Hegre and Oneal 2003, 279).

Data Challenges. Trade statistics have long been considered troublesome to work with, since many believe that they do not accurately portray the nature of the relationship. They may not capture the meaning of the real flow of goods and services; they are manipulated for self-serving reasons by some governments; statistics may be available at

⁷ The work on defining a complex measure for Interdependence is already underway. Gartzke, Li and Boehmer (2001) attempted to broaden the definition of Interdependence by including the effects of international trade flows, monetary relations, and the cross-border movement of capital.

the national level but not for specific dyads; and illicit trade is underreported. In addition, many studies rely on IMF statistics, but communist Bloc countries did not belong to the IMF, so data are missing. This is particularly important for studies involving China, which has had a poor record of providing reliable statistics on its economic performance. The record has improved since Beijing initiated economic reforms, yet its figures are still considered as somewhat tainted.

Four Tests for Analyzing Sino-US Interdependence

Our research examines the impact of Interdependence upon Sino-US relations. As such, this is essentially a case study approach that does not employ traditional case study methodology. Still, we do apply our research to a specific case, the US-China Dyad, so case study methods do inform us. Robert K. Yin (1994) defines case study methodology as, “an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident” (Yin 1994, 13). In some ways, Yin was speaking to the type of endeavor we are undertaking. This case builds upon and uses measures from empirical studies; we look at the contemporary situation of the US and China, focusing on data rather than theory; and the analysis derives from a theoretical basis which is struggling to further define its relationship to the observable world. Unfortunately, our application of IT to the Sino-American context stands the case study approach on its head, moving from a large number of observations to a single case rather than the reverse.

Another way to consider our development of methodology is whether to use qualitative or quantitative tools. Clearly, OR and others have used quantitative measures to develop IT, but our purpose is a practical application; and different goals require different methods. Robert Stake (1995, 37) noted that “Quantitative researchers have pressed for explanation and control; qualitative researchers have pressed for understanding the complex interrelationships among all that exists.” OR and other researchers have worked hard to prove IT’s validity by controlling variables; our goal is not to control such variables but to understand the complexity of the Sino-US economic relationship. Consequently, our research approach is a qualitative examination of theory as applied to a specific case.

Research Questions. In this research we undertake the investigation of three research questions, first identified in Chapter 1:

1. How and to what degree have the US and China become economically Interdependent?
2. How well does IT explain the nature of the relationship between the US and China?
3. Given a policy of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation?

We will analyze Economic Interdependence Theory in the US-China case using four tests: Broadly defined Interdependence (test 1), data examination (test 2), Gelpi and Grieco’s autocracy subvariant (test 3), and examining two dyadic events which pit the IT

perspective against realism (test 4). This qualitative approach creates attempts to address the research questions by applying IT to the dyad, using four different perspectives.

1. Broadly defined Interdependence. We examine the Chinese political economy and the nature of Sino-American economic relationship in broad terms, unconstrained by the very narrow definitions imposed by attempts to quantify Interdependence using trade. The purpose here is to describe the complexity, depth and challenges of the variables involved. This sets the scene for the remaining steps and draws us back into the complexity of the variable, Economic Interdependence, which is the theoretical basis of our research.
2. Data examination. This is an interpretation of the relationship between the independent variable, Interdependence, and the dependent variable, conflict, based upon data from the IMF and Correlates of War project, respectively. This step looks at the hard data from the Oneal and Russell methodology in the China-US case. This will be by necessity a short examination, since the data are very thin. Similarly, our goal is limited, since we are not attempting to prove or disprove the validity of IT. The examination of one dyad over such a short period may prove anecdotal evidence of the nature of IT, but there are too few data points to attempt a proof. Rather, we merely hope to understand the nature of the two variables in the context of the situation and as they changed over a short, but volatile period in the history of the dyad.
3. Gelpi and Grieco's autocracy subvariant. This step is an assessment of how GG's subvariant of IT applies in the US-China case, with specific attention to the interaction between Interdependence, conflict and China's autocratic

political system. GG's work sheds light on the nature of Interdependence in specific cases. We examine the importance of GG's interpretation of the relationship in light of OR's projections. Our purpose here is to advance the third wave of IT thought and determine when and to what extent IT influences the potential for conflict in specific situations.

4. Examining two dyadic events. Here we undertake an examination of two dyadic events (China's entry into the World Trade Organization and the 1995-1996 Taiwan Strait crisis), comparing IT and realism in their utility for explaining US and Chinese actions. Our purpose here is two fold. First, we attempt to demonstrate that IT is a model of international relations, and as a model, has bounded potential for explaining reality. Second, we hope to place IT in context with the theory, realism, which stands in sharpest contrast to liberalism and its components, including IT. These two dyadic events are not intended to demonstrate the totality of our argument about IT and China, but they have instead the more limited ambition of demonstrating the capabilities and limitations of IT in the light of other competing international relations theories. We have selected these particular events for the purposes laid out below:

- a. China's entry in the WTO. This event represents one of the most powerful symbols that both Beijing and Washington may value economic cooperation over mundane power considerations. It demonstrates that IT has an impact on the US decision-making process. Realism, on the other hand, would suggest that trade leads to vulnerability and increased conflict.

- b. The 1995-1996 Taiwan Strait Crisis. This incident demonstrates how and why power considerations and not economic ties might drive decision-making in Beijing and Washington. This event is also one of the Militarized Interstates Disputes (conflicts) in the Correlates of War database. It is, in fact, the most serious such incident during the period of Interdependence. It also involves the single issue, Taiwan's status, that could most likely lead to military conflict between the US and China.

These four tests represent an approach to the research question which recognizes the complexity of the economic relationship between the US and China. While our approach does not include rigorous number crunching, such efforts are not applicable to our study, for OR and other theorists have already done the quantitative research linking trade to conflict. Rather, the four tests provide the reader several prisms through which to view the strengths and weaknesses of Interdependence in this dyad.

The findings from these tests will lead into Chapter 6: Implications and Policy Recommendations. Here we investigate the policy implications for the United States as it faces greater Economic Interdependence with China. We offer policy recommendations that are provided for US policy makers to best optimize the situation. We conclude by determining whether we have addressed the original research question and by examining opportunities for further research.

CHAPTER 4
CHINA'S POLITICAL ECONOMY
Introduction

Economic Interdependence Theory attempts to prove that the risk of conflict between the members of a dyad decreases as economic integration between the members increases. As we witnessed in Chapter 2, the proof for this theory (as represented by Oneal and Russett) is represented by measuring conflict and merchandise trade between the members of the dyad. Clearly, use of merchandise trade limits the nature of the actual economic relationship within the dyad. Indeed, much of IT is bounded by the need to create a proof. These boundaries are somewhat artificial, and they tend to restrict our understanding of the true nature of the economic relationship between the United States and China. If we are to understand the phenomenon of US-China Economic Interdependence, we need to take a step back from the limited definition of Interdependence Theory. In this chapter then, we examine the broad indicators of the level, depth, trends and functions of the US-China economic bond in order to develop a deeper understanding of the relationship. We also briefly examine trade statistics, but we will refrain from investigating the specifics of Oneal and Russett's Interdependence data until the next chapter. Before we undertake that investigation, we also need to spend some time studying the development of China's political economy, since, as a member of

the dyad, its political and economic situation has greatly changed (and promises to continue evolving) during the period covered in this study.

This chapter is in four sections. First, the chapter looks into the economic reforms begun under the Deng regime and continues with the development strategy of succeeding administrations. Second, we will look at Beijing's current economic strategy and how it has undertaken a policy leading to integration into the global economy. Third, we investigate how the US and China have engaged each other and how the economic relationship has developed in the dyad. We accomplish this by using measures outside the Interdependence methodology, including non-merchandise trade measures. We examine the energy sector as a specific case to demonstrate the intricacy of the economic bond. In the fourth section, we summarize the findings of our broad look at Sino-American Economic Interdependence.

These final two sections address the first research question: How and to what degree have the US and China become economically Interdependent? These sections also represent the first of the four tests of IT as applied to the US-China situation which we described in Chapter 3. By looking at the relationship without the narrow constraints of IT, we can show the complexity, depth and challenges of the variables involved. We show that a broader look at the relationship will both bolster and undercut the IT argument. The other three tests (data examination, assessing Gelpi and Grieco's autocracy subvariant, and the two case studies) will be discussed in Chapter 5.

The Deng Era

Deng Xiaoping's life (1904-1997) spanned the tragic events of China in the Twentieth Century, stretching from crippled empire to still-born democracy under Sun Yat-sen to civil war to world war to communist revolution to economic rebirth. While Deng was a witness to these events, he was also a key player in several of them and the architect of its present path. Deng's approach to the political economy of China was colored by his experiences under Mao Zedong and the Chinese Communist Party's (CCP) earlier experiments to transform China. We begin to explain the Deng era by examining the role of the CCP and its charismatic leader, Mao Zedong.

The rise of the CCP was rather quick, with the first Congress held only in 1921. The CCP's success came about due to decades of urban political agitation, the failure of the democratic model, the rise of nationalism against first the West and then the Japanese, and the aid of outside sources, particularly the USSR. Following its quick rise to prominence on the national stage, the Communists movement was to suffer the ups and downs of similar movements elsewhere. Much of the CCP's tribulations sprang from Moscow's constant urging to work with the Nationalists forces against the Japanese and to start armed insurrection. The 1927 split with this policy led to the beginning of the Red Army and Mao's strategy of moving from the cities into the rural areas to build a broad base of support and to move slowly toward the use of armed attacks. After Nationalist attacks forced the Long March, the CCP declared war on the Japanese, and the CCP and Nationalists entered into a second (anti-Japanese) alliance in 1936. During this time, Mao emerged as the clear political and ideological leader of the Communist

movement. The Red Army gained more and more land during the war with Japan, and, with Soviet aid, was finally able to beat the Nationalists in 1949 (Pye 1991, 153-73).

Once the civil war was over, Mao and the CCP were able to assert control over the country fairly quickly for several reasons. One, they were used to governing, since they had ruled large chunks of China for a decade or more. Two, the PLA was an effective instrument of control and in fact became a model for reorganizing society. Three, the beginning of the Korean War in 1950 was a rallying point about which all Chinese nationalists could collect. Four, Soviet aid was generous. Five, the CCP itself proved a sometimes unstable but always assertive role in reshaping China with the work unit or *danwei* replacing the Confucian family as the common unit of society (Pye 1991, 174-90).

The CCP came to be dominated if not fully controlled by a charismatic leader, Mao Zedong, who would control China for the next quarter century. One of America's great "China hands," Lucian Pye, paints Mao as a figure of often contradictory impulses, and sees him less as the monolithic power that common history suggests. He may have been the Great Helmsman, the very model of a cult of personality, but to his peers, such as Zhou Enlai and Liu Shaoqi, he was merely the most powerful among a small cadre of very powerful men. Still, one cannot deny the influence of Maoism both in China and as a symbol to other developing countries, guerrillas, and revolutionary groups even to this day. It was Mao's fascination with ideas over materialism and zeal over bureaucracy that drove the great movements (both productive and destructive) of China under Communism. Mao's ideology no doubt was the major factor that drove apart Beijing and Moscow, helping to split the Communist Bloc (Pye 1991, 220-54).

The portrayal of Mao as a talented if flawed man is not too far removed from the version of Mao first described by Edgar Snow in his seminal works *Red Star over China* and *The Long Revolution*. A very different portrayal of Mao and his impact on the nature of the Chinese Revolution has been posited by Jung Chang and Jon Halliday in *Mao: The Unknown Story* (2005). They portray the Great Helmsman as a Stalin-like thug, whose enduring personality cult has continued to hide the true nature of the Twentieth Century's greatest villain. Chang and Halliday's well-researched, consistently polemic opus claims that Mao's disregard for the lives of his citizens left millions dead from war, starvation and manufactured revolutionary excess (Chang and Halliday 2005, 289-90, 357-78). Mao's greatest feats, including his championing of the peasants and the Long March, are pure mythology meant to mask his personal cowardice, lust for global dominance and betrayal of every friend and ally he had through the years (Chang and Halliday 2005, 91-96, 128-36, 159-65, 184-86, 221-29, 259-60, 301-05, 622-23). While only idealists have failed to see the misery under Mao's rule, Chang and Halliday place the era's constant purges and social turmoil fully on the shoulders of a sociopathic and narcissistic Mao (Chang and Halliday 2005, 12-15, 238-50, 268-69, 514-16).

The implications of this new take on Mao Zedong are significant in three ways. First, it posits that the PRC's history would have been very different and probably a great deal brighter without Mao. Second, it suggests that Deng's pragmatic reforms were even more remarkable in light of the evil that prevailed under Mao. Third, it further calls into question the legitimacy of the current regime which continues to hold up Mao as the wise and caring founder of modern China. It remains unclear if Chang and Halliday's rewriting the story of Mao is a single incident or the opening salvo of a battle that will

finally destroy the Mao myth. Then again, in the thirty years since his death, Mao's legacy continues to fade as the Chinese race toward a new destiny.

During the height of his power, Mao hoped to change the nature of man and his political and economic motivations. He sought to toss out Confucian ideas, the moral and religious code of China, and replace them with a uniquely Chinese form of Marxist-Leninist ideology. Later, beginning in 1953, Mao pushed the first of his economic reforms through Five Year Plans. Following the example of the USSR, he hoped to improve the agricultural sector in order to create a catalyst for modernization (MacFarquhar, Cheek and Wu 1989, 4). In order to harvest the revolutionary zeal of the peasants in the pursuit of industrial goals, Mao dreamed up the Great Leap forward at the beginning of the second Five Year Plan in 1958. The Great Leap Forward, of course, has come to be seen as the very symbol of poor economic planning. By 1960 the country was in a desperate famine and millions were to starve to death (Cheng 1989, 117-18). The Great Leap Forward was only surpassed in its excesses (and economic damage) by the last of Mao's sociopolitical movements, the Great Proletariat Cultural Revolution that ravaged China from 1966 to 1976.

Such was the legacy that introduced China to the Deng reforms. Deng himself was one of the most prominent victims of the Cultural Revolution, having been relieved as Party Secretary early in the movement. He was "re-educated" and returned to prominence in 1973 and soon became a strong backer of Premier Zhou Enlai and the moderate camp. After a second purging, the death of Zhou and the fall of the radical Gang of Four, Deng began his long tenure as Mao's successor. Deng, having politically risen from the dead following his humiliation during the Cultural Revolution, worked to

promote pragmatism over ideology, technology over zeal, and modernization over orthodoxy. That is to say, he put economic reforms on the front burner and political development on the back (Pye 1991, 320-35).

Deng promoted a policy called the Four Modernizations, a plan first revealed in 1973. It emphasized improving these four sectors: Agriculture, Industry, Science and Technology and National Defense. The concept was adopted in 1977 while Deng was coming to power (deCrespigny 1992, 284), and the entire package of gradual reforms was officially unveiled at a National Party Congress in December 1978. This long birth is indicative of the difficult negotiations to bring the polity together to support a marked departure for both the CCP and the PRC. Deng chose the agricultural sector as the first target of his economic reforms. Mao's attempts to reform the agricultural sector had left farming in shambles. In 1985, China was still an agricultural society at this time with 63 percent of the labor force working on farms (Worden, Savada and Dolan 1998, 231).

Deng's policies sought to stimulate agricultural production by replacing the rigid hierarchical system with local controls and providing market mechanisms to encourage private production (Worden, Savada and Dolan 1998, 275-78). These initial reforms had a dramatic effect. Agricultural production increased by 49 percent between 1979 and 1984 (US Congress, Joint Economic Committee 1986, 327-38). In 1985, 17 percent of the labor force worked in industry, and they produced 46 percent of national income (Worden, Savada and Dolan 1998, 234). Industry was dominated by state-owned, heavy manufacturing for the domestic market (Worden, Savada and Dolan 1998, 235). The reforms sought to reduce the command controls and turn over more authority to factory managers. Managers were expected to produce profits and could use monetary measures

to motivate workers (Naughton 1986, 608). The profit remissions program of the command system was replaced with a sliding tax, based upon the size of the company (Naughton 1986, 612). Some controls over working with foreign companies were lifted in order to allow for greater exports of light manufacturing and the import of machinery and equipment (Worden, Savada and Dolan 1998, 223-25). The resulting changes were quick to materialize. Before Deng, merchandise trade had rarely reached 10 percent of national income; by 1986 it was already 35 percent and climbing (Worden, Savada and Dolan 1998, 226).

Science and technology development had long been emphasized in the PRC, following the Soviet model, and China had built many research institutions. However, Deng and other leaders perceived that these institutions were inefficient in using their talents to promote China's growth. The 1980s reforms forced the institutions to seek commercial partners for their products by reducing state funding. Incentives were also created to allow research centers to provide monetary incentives to individuals, and a patent system was created to codify the recognition of benefits for work (Worden, Savada and Dolan 1998, 398). A sophisticated system was developed to import advanced technology and equipment from developed countries (Simon 1996, 264).

China's military at the beginning of the Deng era was shaped by its long history as an under-resourced, politically active people's mass militia. National defense in the Deng era revolved around three initiatives to begin the process of creating a military fit for a major power. First, Deng sought to remove the military from the political process and assert civilian control over the apparatus. Second, Deng sought to professionalize the military by improving training and education and by updating its doctrine and

organization. Finally, Deng wanted to create an industrial relationship which allowed the military to have a modern force independent of foreign sponsorship (Worden, Savada and Dolan 1998, 553-54).

Political Reform. Deng's bold economic reform plan was counterbalanced by a status quo reform of the political system. He proposed four basic principles of political control to assuage more conservative-minded CCP leaders and to chart a course that ensured that economic reforms did not lead to a collapse of the socio-political system. He sought continued adherence to the Party as the core loyalty of the state. The first principle ensured that the CCP would remain the central authority over the government and no competing political organizations would be tolerated (Deng 1980, 97). The second principle committed the CCP to continue its pursuit of socialism. Referring to the status of the CCP, a 1982 law declared that it would remain, "the vanguard of the Chinese working class, the reliable representative of the interests of the people of all nationalities, and the core leading the cause of socialism in China" (Domes 1985, 101). The third principle committed Chinese society as a whole to working toward a socialist, egalitarian goal. The fourth principle tied the political process to an evolution of Marxist-Leninist-Maoist thought (K. Chang 1990, 92-93). Thus, the CCP was the core and only political authority, and the CCP and society in general were committed to socialism as defined by Marxist-Leninist-Maoist philosophy.

Deng's final equation between the economic and political reforms was not balanced. The CCP and the government were committed to the political goal of maintaining control over the political system in China. On the other hand, the true

measure of success has become whether or not the government is able to build and sustain economic growth and development.

China's Development Model. The reform period was marked by periods of advancement of new ideas and retrenchment as more conservative forces pushed back as they saw their privileges and institutions being pushed aside. By 1988, Deng and company had a ten-year run of sustained economic growth and were prepared to make another major shift in strategy. They moved beyond the creation of internal market mechanisms and took on aspects of the export-focused strategy of the Asian Tigers (Taiwan, South Korea, Singapore and Hong Kong). The linchpin of this strategy was to concentrate on using foreign capital and expertise to engage in labor-intensive industries, employing China's inexpensive labor force (Clark and Jung 2004, 139-41).

In ten years, Beijing moved from an insular, command economy to a mixed economy with growing foreign trade promoted through a state development model. Clark and Jung (2002, 18) identified two basic concepts behind the developmental state model. "First, that most developing nations are at such a disadvantage in the world economy that market forces themselves preclude significant industrial growth. Second, that the state, in at least some of these nations, possesses the power to overcome the barriers facing late developers." Thus, China sought to emulate the Asian Tigers, but used a state development strategy that included a surprising amount of reliance on foreign investment and external influence.

Of course, the Chinese have not worked in a vacuum; Soviet Bloc command economies also moved to rapidly reform in the 1990s, and China learned from their experiences. The Soviet Bloc states suffered a variety of economic setbacks and to some

degree moved to overcome these missteps. The Chinese have observed these reforms, but they have opted not to follow the types of successful experiments used in Poland and the Czech Republic. The Chinese are fully aware of the Japan model, where strong ministries (such as MITI, the Ministry of International Trade and Industry) orchestrated a planned national development with individual firms. Indeed, some believe the Japanese model never worked as designed, for rather than picking key industries to develop, MITI and its imitators merely conformed to market forces already in play (Steinfeld 1998, 54-55). Besides, the context is very different in present day China. Japan in the 1960s and 1970s and Taiwan in 1970s and 1980s had economies in which the sharp bureaucrats, such as those in Japan's Ministry of Trade and Industry, worked together with the market. As Edward Steinfeld notes, in China, the state with its massive bureaucracy *is the problem*, and there is only a limited market with which to interact (Steinfeld 1998, 54-55).

The Current State of China's Political Economy

China's current economic development strategy has continued to evolve since the end of the Deng era. Deng's successor (Jiang Zemin) has himself been succeeded by Hu Jintao. The PRC, now in its fourth generation of leadership, has retained a remarkably stable development policy despite the changing leadership. The government continues to improve its agricultural sector although the rural population is no longer benefiting much from economic reforms. Industry continues to rely upon cheap labor, but the sophistication of manufacturing industries continues its progress. Science and technology continue to advance the level of China's economic output and of the talents of

its workforce. China's military budget and equipment purchases are ever-expanding. In addition, Beijing has remade its relationships with its neighbors and is seeking a new role as a regional and global player.

Export Strategy and Economic Growth. One of the great attributes of China's development is that it has continued to evolve and advance, even as it has moved from Deng to his successor's successor, Hu. Currently, China's development strategy resembles, ironically enough, the strategy of Taiwan. Beijing sets the rules of the game and controls access to the market, but for the most part, private companies and the market drive production (Clark and Jung 2004, 139). Much of this activity is being undertaken with Taiwanese capital and Taiwanese business expertise. China, of course, again encompasses Hong Kong, the Asian Tiger which most clearly used a *laissez-faire* approach to development. Modern China sustains both a hybrid state development strategy and a *laissez-faire* strategy. As in both the Taiwan and Hong Kong examples, China places a heavy emphasis on exports to both increase revenue and to provide the tools to create a continuous process of economic technological advancement.

The early successes in Deng's reforms came in the agricultural sector, relying upon the domestic market. However, its long-term economic development model included opening the country to outside economic forces. China's recent economic growth has been matched by its incredible growth as a merchandise trader, with a goal to increase exports. As indicated by the Chinese government's statistics in table 4.1, the values of its exports increased 20 times from 1982 to 2003. Furthermore, during the past two decades, China's growth in exports and imports has been greater than the world average (Rumbaugh and Blancher 2004, 3).

Table 4.1 China's merchandise trade with the world in billion of dollars, 1982-2003

Year	China's Trade w/ the World (Chinese Data)			World Trade w/ China (Partner Data)		
	China Exports	China Imports	China Balance	World Exports	World Imports	World Balance
1982	22	19	30	16	23	-7
1983	22	21	.1	18	23	-5
1984	25	26	-1.1	25	27	-2
1985	27	42	-15	38	31	7
1986	31	43	-12	36	35	1
1987	39	43	-4	39	47	-7
1988	48	55	-8	52	60	-8
1989	53	60	-6	52	73	-21
1990	63	54	9	49	89	-40
1991	72	64	8	62	112	-51
1992	85	82	4	82	137	-54
1993	92	103	-12	108	157	-49
1994	121	116	5	121	192	-71
1995	149	132	17	146	234	-87
1996	151	139	12	156	254	-98
1997	183	142	41	165	286	-121
1998	184	140	43	153	289	-136
1999	195	166	29	163	322	-159
2000	249	226	24	212	398	-186
2001	266	243	23	221	413	-191
2002	326	295	30	271	484	-213
2003	438	413	25	422	601	-179

Of course, an increase in exports is not proof of an advancing economy, so we need to examine other indicators. Gross Domestic Product is the most commonly used gauge of an economy's success. As seen in fig. 4.1, official Chinese statistics show that as the country moved from the second generation of leadership to the fourth, it continued to have extremely strong growth. Of course, China did have a steady population growth

during this period, but the per capita GDP rate also increased rapidly, as noted in fig. 4.2. In addition, the most recent GDP growth rates from the Chinese government show continued rapid increases in production (fig. 4.3). While Beijing's official figures tend to be higher than external assessors, China remained a success story well after the initial gains made during the Deng regime. Independent western observers also track high GDP rates. Nicholas Lardy reports that from 1978 to 1995, China's economy grew at an average of approximately 8.3 per annum (Lardy 2002, 12).

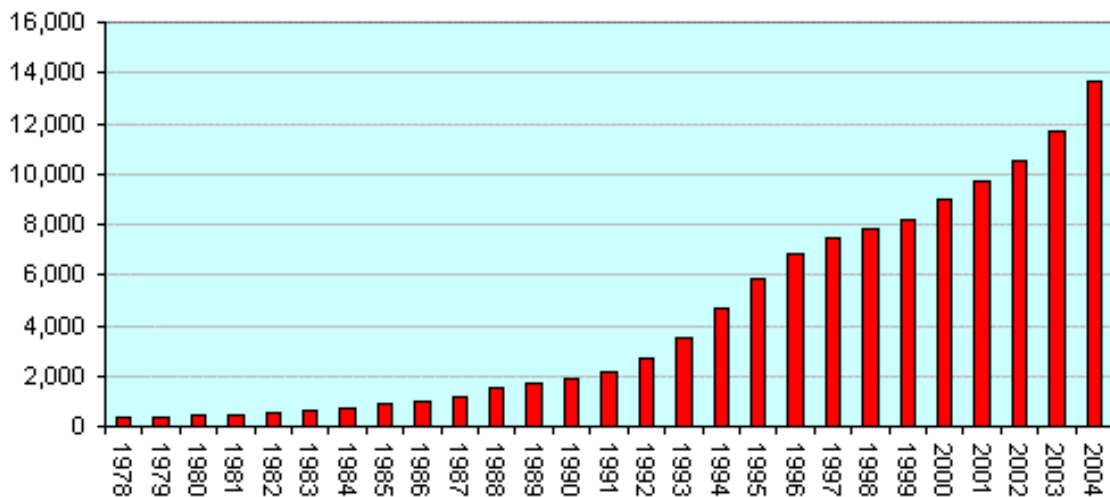


Fig. 4.1. Gross Domestic Product (Source: National Bureau of Statistics, China Statistical Yearbook 2004; National Bureau of Statistics plan report)

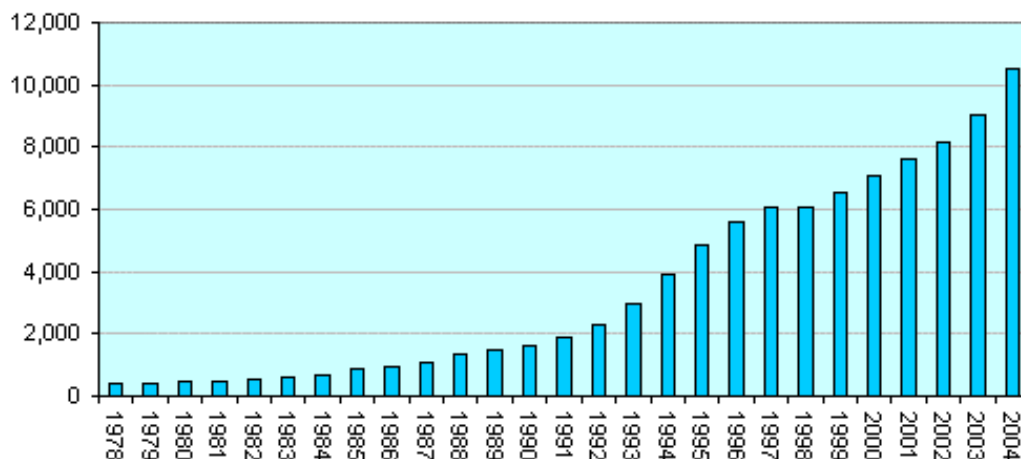


Fig. 4.2. China's per capita GDP (Source: National Bureau of Statistics, China Statistical Yearbook 2004; National Bureau of Statistics plan report)

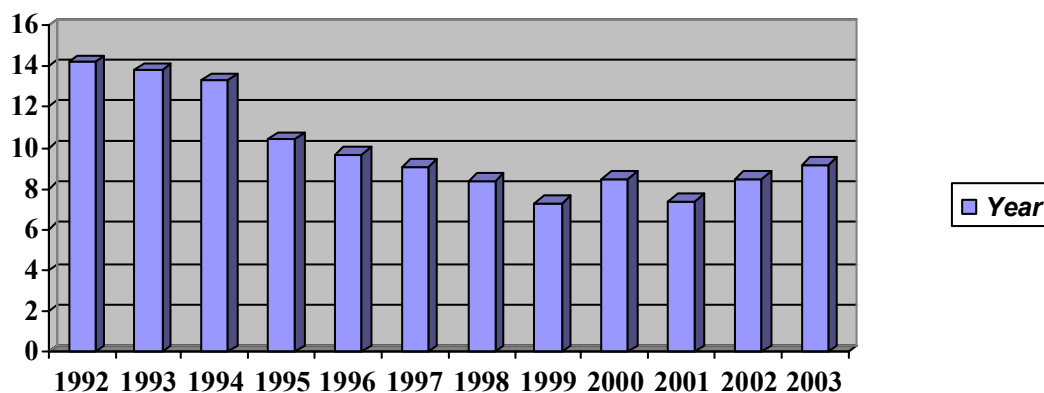


Fig. 4.3. China's percentage real GDP growth rates, 1992-2003 (Source: China Statistical Yearbook 2003; National Bureau of Statistics of China)

Economic Challenges. Despite China's great strides in recent years, Beijing faces several challenges on the economic front. Economic growth has not been without its stresses to society, including unemployment, mass migration in search of jobs, declining rural fortunes, environmental degradation, and loss of centralized control of the process.

In the realm of these economic issues, the greatest threat to the Chinese miracle is the status of its state-owned enterprises.

State-owned enterprises (SOEs) are a legacy of the command economy in that they are big by design, they dominate in heavy industry, and they are still controlled by the state rather than private corporations. We might ask ourselves why the issue of these SOEs matters in a China that has enjoyed often double-digit growth rates for decades. An optimist would speculate that natural forces will drive creation of additional market institutions that will fix the market for SOEs. However, these SOEs comprise China's capital-intensive heavy industries. Penetration of this industry by non-SOEs is simply not in the cards in the near term. The centrality of SOEs within the Chinese economy has shrunk considerably since the beginning of reforms; in the 1970s, SOEs produced 80 percent of manufactured goods (Lardy 2002, 15). Large-scale SOEs now provide 35 percent of outputs of the economy (Steinfeld 1998, 13). At the same time, SOEs still control 80 percent of all working capital in the manufacturing sector (Lardy 2002, 15). Most importantly for the state, SOEs provide the central government most of its internal revenue, 71 percent in 1995 (Steinfeld 1998, 17). In 1995, 83 percent of all outstanding bank loans were with SOEs, suggesting that both the SOEs and the banking system are in jeopardy (Steinfeld 1998, 13).

Another level of analysis comparing SOEs to other sectors of the economy would leave one with the realization that the reforms of the 1980s and 1990s have allowed the Chinese to pick the low-hanging fruit, but the remaining harvest will require much greater effort. While Beijing has undertaken a risky and largely successful effort to reform much of its economy, it has long deferred the toughest of challenges, reforming

SOEs. Beijing focuses on its successes rather than these “dinosaurs,” because the cost of delayed reforms is immense and growing ever larger. Many argue that these SOEs are the clearest hurdle to China’s continued economic success. The root problems stem from the lack of institutional mechanisms to create corporate governance through explicit private property rights (clear and unique ownership), limited commercial capital markets, a weak regulatory regime, and poor accounting standards.

The SOE issue is tied to the status of property rights in China, which is a particularly appropriate topic today, considering the fact that China now guarantees a limited right to own private property. Yet, these first steps in protecting private property rights will not solve the underlying motivations of SOE managers. MIT Professor Edward Steinfeld believes that behavioral change by managers will not come about merely by granting them more freedoms; rather, they will come about by providing clear penalties from failure to change behavior (Steinfeld 1998, 54-55). In the past, SOEs have failed to respond to the market even after being given the freedom from command planning. Creating private property rights is ineffective if the institutional structure, including government regulation, is not there to facilitate market forces. Steinfeld believes that at the heart of problem is the relationship between the SOEs and the various governmental organizations. In the current environment, the state organs continue to have informal control of the firms, pressuring them to make profits (which return to the state) and forcing banks to make soft loans to SOEs. The SOE leader is then compelled to increase profits, usually by borrowing and sleight of hand (Steinfeld 1998, 54-55).

Many SOEs were created under the old planned system and survived in the current system despite the withdrawal of subsidies. These companies now work to create

profit rather than simple output. Indeed, balance sheets suggest great success at increasing profits at many of these companies; unfortunately, these “profits” are often created by imaginative accounting and increasing liabilities, which ultimately causes severe liquidity problems (Steinfeld 1998, 84-85). Half-measure reforms are part of the problem. The limited autonomy given managers has resulted in destructive behavior; the effort to create incentives to enhance the company’s assets failed. The lack of governance and ownership allows firms to deal in triangular debt schemes, in which SOEs trade amongst themselves on credit but fail to perform on their loans. Thus they have “profit” but may be collecting cash on only a fraction of their sales.

Our travels through the troubled SOEs logically lead us to the front doors of China’s stressed banking system. As seen elsewhere, China is both a nation of “world-class savers” (about 40 percent of wage earnings) and poorly-performing loans to SOEs (G. Chang 2001, 123, 124-28). Non-performing loans in 1999 were 70 percent of the total, a truly worrisome number if compared to Western standards, and four banks hold about 70 percent of deposits and make about 70 percent of loans (G. Chang 2001, 127). These banks are rapidly modernizing, but they remain in jeopardy, because they are forced by the government to continue giving loans to the already debt-ridden SOEs. To some, this is evidence that the system is about to collapse. Much research points to the SOEs and the banks as the most problematic area of the Chinese government. The Chinese government, short of revenue, raids these banks in order to perpetuate the employment of SOE workers, who make up about 40 percent of urban workers. The monies also allow the SOEs to continue providing the considerable social services and retirement pensions it gives to millions of Chinese.

The sorry state of the SOEs and the banking system are of great concern, but their condition has not tarnished the general perception in the USA that China's economy is on an inexorable upward trajectory. Peiter Bottelier (2000, 63-78) posits that the economy has inherent strengths that give it unusual stability, particularly against external machinations. China has incredible foreign exchange reserves. This fact, together with low external debt and large current account surpluses, suggests little chance of external short-term debt problems. In fact, the greatest external threat may be the continued recession in Japan. Similarly, the limited convertibility of the *renminbi* means China's cannot be manipulated in the way the Thai *baht* was at the dawn of the Asian Flu crisis. Bottelier identifies other factors that demonstrate a good economy, such as a trend in good harvests, the more-or-less successful integration of Hong Kong, continued strong growth, and a clear commitment to reform (Bottelier 2000, 63-78).

Current Political State. As we noted earlier, China has seen both political and economic reform. Gone are the days when Red Guards ruled the streets and gone are the predominance of the five-year economic plans. But China's economic reforms are incomplete, as witnessed by the gravity of the challenge caused by the state-owned enterprises. In the same way, the devils of China's political past remain active today. The strategy of the political reform outlined above was little more than a fig leaf over the CCP cadre's desire to remain in control of China. Socialism remained the goal, but status quo political distribution and social order were the operational objectives. The unsettled nature of China's political landscape leads to speculation about two potential futures: Will China democratize and will it remain stable in the near term? Both questions are critical for understanding the future of China's Economic Interdependence.

Some are optimistic in their outlook for China's political future. Eric Heginbotham and George Gilboy, in their article "China's Coming Transformation," posit that China's leaders will seek political liberalization as a solution to the challenges they face (Heginbotham and Gilboy 2002, 107-08). They believe such liberalization will include much social turmoil and warn that the greatest threat to reform is a belligerent tone by the US. The move to political liberalization will come as a result of the changing nature of the state-to-society relationship. Farmers, consumers, environmentalists, minorities, religious groups and laborers are all pressing their interests (Heginbotham and Gilboy 2002, 107-08). Why should the elite allow such change? They recognize that repression is less viable, for the use of force hampers economic development. The fourth generation of leaders, many from the pragmatist wing of the CCP, will find accommodation the best solution.

David Shambaugh of George Washington University examined the change permeating the CCP leadership and also comes away with a fairly upbeat assessment (Shambaugh 2000, 26-39). Shambaugh, writing before President Hu Jintao and the fourth generation of leaders began to take the reigns of power in 2002, noted the smooth transition to Jiang Zemin (and Li and Zhu) following the death of Deng and their subsequent consolidation of power at the 15th Party Congress. While short of constitutional due process, these events demonstrate regularity in the system. More importantly, the voice of radicals has faded in the upper reaches of government (there are no more Long Marchers), and the CCP leadership is decidedly more technocratic, educated, and global in their outlook than their predecessors.

The political leaders also have some disadvantages, the most important of which are narrow bases of personal political power on which to rest their aggressive agendas. Bruce Dickson notes even greater problems among the lower levels of the political class (Dickson 2000, 52). While the new party cadre is younger, better educated, and savvier at business than their predecessors, most have very little affinity with either the rural or urban working classes, a strength of the early CCP. With its drive to recruit entrepreneurs, the CCP has decided its needs real skills rather than simple loyalty to the Party doctrine. While this strategy has some benefits, this new cadre is not well prepared to deal with the potential rise of discontent from those left out of the economic miracle. Dickson believes that at the least, the CCP risks becoming irrelevant, which bodes ill for short-term stability, if not long-term progress (Dickson 2000, 50-54).

Shambaugh concludes that China is in a state of “stable unrest” with many nodes of instability, creating an environment that is more unstable than any other period since the Cultural Revolution. On the other hand other issues, such as a relatively stable central government, strong control of the security services by the political elite, and an improving lifestyle, are stabilizing influences that for the present will allow the CCP and central government to withstand challenges from within or outside of the party-government (Shambaugh 2000, x).

Others see Chinese society as heading to collapse. Gordon Chang in *The Coming Collapse of China* sees China as a paper dragon, “in long-term decline and even on the verge of collapse” (G. Chang 2001, xvi). Chang believes China is a “lake of gasoline,” awaiting only a match to set it off (G. Chang 2001, 44). The core problem is the CCP and its intolerance for competing centers of power. While Deng Xiaoping made some

important reforms, the current crop of CCP leaders have brought the revolution only half way and are not in consensus about the next steps. The reforms have left important issues unaddressed, and the Party consequently is too weakened to make the needed changes. Chang argues that is not in the nature of the Party to reduce its own influence; hence, it can not make real reform. This is one of many contradictions in this argument, since the Party has already voluntarily made reforms on the economic side, which have weakened its control. Chang avers that another powerful leader, another Deng, might be able to make true reform (G. Chang 2001, 15). However, China has grown beyond charismatic leadership into a more complex system which may lead China to the day when institutions, laws, and societal norms and not revolutionaries will determine China's fate.

The pessimists view of the dexterity of the Chinese political system points to the rising dissent of groups like the Falun Gong, workers, and ethnic minorities. Such protests can be seen as either a sign of potential growing pluralism or growing instability. Chang and others charge the CCP is targeting entrepreneurs, because they are creating inequities in income. Other evidence suggests that the CCP is providing considerable latitude to the new rich, even recruiting entrepreneurs into the Party. For example, the process of allowing businessman into the CCP was formalized in 2002 (*BBC News* 2002). Is the CCP unaware that constraining the new rich would jeopardize the Party's only claim to legitimacy? Certainly, the inefficient government and corrupt Party do throw up barriers to entrepreneurs, but there is little evidence to believe they would jeopardize their strategy of using economic prosperity as their main reason for maintaining political control.

China's International Relations. In contrast to the static nature of the internal political structure, China has transformed its relationship with other states and intergovernmental organizations. In this sense, their new policy looks much like their economic policy—more engaged in the existing international order. In their book, *China Joins the World: Progress and Prospects*, Elizabeth Economy and Michel Oksenberg argued that in international politics China pursues several tactics. Beijing will try to: retain flexibility in foreign policy and avoid alliances, seek rent directly or indirectly as the price for its participation in regimes, place, “the burden of maintaining good relations on the other side,” mobilize developing countries, take advantage of regime ambiguities, act as the aggrieved member, and frustrate attempts at transparency (Economy and Oksenberg 1999, 25). China has also become more assertive, more effective and a better negotiator in recent years. This is true in part because after decades of remaining outside the game, Beijing is finally learning the rules of the game. China has standardized its internal decision making process and developed a more pragmatic, consultative tone (Economy and Oksenberg 1999, 25-27).

China's relationship to international institutions has been transformed in the past thirty years. Samuel Kim of Columbia University investigated China's increasing involvement with the United Nations and other intergovernmental organizations. Kim points to UN Resolution 2758, passed in 1971 as one starting point of the change in Chinese attitudes toward IGOs; UN Resolution 2758 transferred recognition from Taiwan to the PRC, giving Beijing a permanent UN Security Council seat. The second turning point would be Deng's succession to leadership. China's attitude toward the UN has gone through several stages from hopeful engagement in the early Mao years to vitriolic

condemnation in the 1960s to its current approach of opportunistic “unilateral self-help” (Kim 1999, 80). In this perspective, China is seen as a cautious, conservative, status quo power in its behavior in the United Nations. Essentially, China is seeking to use the organization to further its own agenda. Nonetheless, the turn in China’s attitude toward the UN and international governmental organizations has been remarkable. From 1977 to 1996, China’s membership in intergovernmental organizations jumped from 21 to 51, and its membership in international non-governmental organizations (NGOs) climbed from 71 to 1,079 (Kim 1999, 46). These IGOs and NGOs are, of course, the same organizations that Oneal and Russett identify as one leg of the Kantian tripod.

Michael Swaine and Ian Johnston see China as a free-rider in the world system (Swaine and Johnston 1999, 118). They note that China has demonstrated three attributes in its behavior (Swaine and Johnston 1999, 104-06). One, it is willing to engage in more regimes that require some level of compliance. Two, Beijing can change its mind on participation in specific regimes, as evidenced in the about-face entry in the Comprehensive Test Ban Treaty in 1996 (Swaine and Johnston 1999, 106). Three, China is motivated by its image, particularly among Third World states. China has not moved forward equally in all aspects of its engagement with intergovernmental organizations. According to Andrew Nathan (1999a, 156-58), China has been less willing to participate in human rights regimes. Human rights represent a special case, because unlike other matters of tensions with the West (such as, weapons proliferation), there is little doubt that China violates international standards. Rather than joining human rights IGOs, China has resisted Western definitions of human rights and values, claimed state sovereignty, made quid pro quo concessions, and played international politics with the

matter. Despite China's reluctance to join up, Beijing continues to adopt slowly the very standards that underpin these organizations. Beijing's interaction with arms control regimes is an issue of the highest priority for US policy makers. Beijing is uninterested in either surrendering its prerogatives regarding its own weapons systems and sales of such technologies, and it is similarly disinterested in the broader goals of creating global norms on such weapons. Rather, Beijing enters such regimes with the purpose of increasing its own security (or freedom of action) and is willing to act against the stated goals of the organizations it joins. For the latest developments on China's foreign policy and the concept of "China's peaceful rise," see the Chinese and American National Security Strategies section of Chapter 6.

Military and Security Issues. In its annual report on China to Congress, the Office of the Secretary of Defense (OSD) at the Pentagon laid out the official US government view of China's military power. "The PLA is transforming itself from a mass army designed to fight a protracted war of attrition within its own territory to a smaller, modern, professional force capable of fighting high-intensity, local wars of short duration against high-tech adversaries" (OSD 2005, 16). According to China's numbers, its military budget for 2005 was US\$29.9 billion, a 12.6 percent increase over 2004 and a 100 percent increase since 2000 (OSD 2005, 21). The Pentagon puts the figure at \$90 billion, which would make China's military spending third to only that of the United States and Russia (OSD 2005, 21-22). Ted Galen Carpenter and Justin Logan of the Cato Institute found the Pentagon's figures for China's military to be highly exaggerated and instead point to a RAND Corporation report that places the figure at between \$31 and \$38 billion (Carpenter and Logan 2005). By comparison, President Bush requested \$401.7 billion

for defense spending in 2005, a year in which war costs in Iraq and Afghanistan required additional expenditures over the president's request and the Congress's final budget (The White House).

China's rapidly expanding budget has been used to order a host of advanced military equipment, with Russia providing the bulk of these orders. The People's Liberation Air Force is procuring third and fourth generation Russian-made, precision-strike fighters and command and control aircraft, while the Navy is adding the guided missile cruisers and advanced submarines that will give China a blue water navy for the first time in its modern history (OSD 2005, 4-5; Goldstein 2005, 56-62). While China claims a "no first use" policy for its nuclear forces, it is improving the number and quality of its strategic forces (OSD 2005, 28). China has about 40 ICBMs in its minimum deterrence nuclear force, which it is updating with road-mobile and sea-based ICMBs (OSD 2005, 28).

The army on the other hand, is downsizing again to about 2.3 million members, leaving it as the world's largest army (OSD 2005, 4-5). This reduction in force is not indicative of a reduced robustness, but rather of an effort to professionalize it in order to carry out the more complex operations of a modern army (OSD 2005, 5). Returning to David Shambaugh's work (2000, 26-39), he observed that the Chinese military leadership is also more likely to include experienced commanders rather than political commissars as in the past. However, there are downsides in the makeup of the new leadership. These new military leaders have very limited experience with the world outside China and, in contrast with the past, they do not have established relationships with the political leaders or even each other.

In revamping its military's doctrine and force structure, China has looked to the one nation that has been at the center of the use of force on the world stage the past two decades, the United States. China has closely examined America's recent war experiences from Operation DESERT STORM in 1991 to Operation IRAQI FREEDOM in the present to learn vicariously about the nature of modern warfare (OSD 2005, 17-19). From these observations, the Chinese anticipate the strategy and organization needed to fight their most powerful potential rival and learn which capabilities will best serve its generic security needs. This examination of America's military lessons learned is essential for the PLA, since its most recent military experience is decades old and based upon a discarded doctrine.

The Pentagon report posits that China does not, "face a direct threat from another nation" (OSD 2005, 13). Beijing's military build up is, "focused on preventing Taiwan independence or trying to compel Taiwan to negotiate a settlement on Beijing's terms" (OSD 2005, *preface*). The corollary to this goal is that China seeks to prevent third parties, particularly the US, from aiding Taiwan, and Beijing trains to this second goal. Beijing's military posture reflects these priorities, since its best military assets are heavily concentrated across the Taiwan Strait from its erstwhile province (OSD 2005, 3). China has 650-730 missiles, 700 aircraft and two-thirds of its fleet opposite Taiwan and maintains a two-to-one advantage in the region in ground troops (OSD 2005, 4, 43). The Pentagon notes that "the cross-Strait balance of power is shifting toward Beijing as a result of...improvements in the PLA's military capabilities" and the fact that "Taiwan defense spending has declined in real terms over the past decade" (OSD 2005, 37). In

contrast to China's buying spree, a \$15 billion offer of military equipment sales made in 2001 by the United States remains stalled in Taiwan's parliament (OSD 2005, 37).

In 2005, China passed an anti-secession law, which reaffirms China's belief that it has the right to use force to prevent Taiwan from declaring independence (OSD 2005, 38). China would use force in the following circumstances, "a formal declaration of independence of Taiwan, foreign intervention in Taiwan's internal affairs, indefinite delays in the resumption of cross-strait dialogue, Taiwan's acquisition of nuclear weapons, and internal unrest on Taiwan" (OSD 2005, 39). Currently China is also deterred from taking action against Taiwan, because it lacks an overwhelming military advantage and fears the consequences of international retaliation on its economic development (OSD 2005, 42).

But China is not solely focused on military instruments to use in the Taiwan case. Military equipment acquisitions and organizational and doctrinal changes suggest that China is looking to other interests in the region (OSD 2005, 12-13). Furthermore, the rise of India, the ongoing preoccupation with Japan's potential military power, and concerns about keeping sea lanes for China's imports and exports also drive Beijing's security measures. In such an emerging environment, the Pentagon speculates that China, whether by design or circumstance, might take a military path due to: uncontrollable nationalism, economic collapse, inexperience as a great power actor, internal unrest, territorial disputes, and an over-empowered military (OSD 2005, 8-9). Furthermore, military conflict might arise because of the rapidly changing military balance. Other states might underestimate China's prowess, while Beijing might overestimate its new

capabilities (OSD 2005, 26). These arguments point to the conundrum faced by China's dual economic and military rise.

American security experts are divided by China's surging military prowess. Journalists Richard Bernstein and Ross Munro in their book *The Coming Conflict with America* paint an alarming portrait of the intentions and growing capabilities of China. They claim that since the death of Deng Xiaoping, China's leaders have taken a course that runs counter to US interests. China is driven by nationalism, a desire to redress past wrongs, and a plan to replace the US as the Asian hegemon (2002, 2). Specifically, they see China as attempting to prevent US containment and weaken ties to South Korea and Japan. They claim that Beijing's apparent actions in recent years to conform to international norms and work with the US are really just a cynical "tactical gesture" (2003, 3). The authors point to close cooperation with Russia and aid to Central Asian republics as evidence of China's intentions. They are alarmed at China's rapid military build up, which is true but less startling when one considers the primitive level upon which the PLA is modernizing.

CSIS researchers Kurt Campbell and Derek Mitchell examine the importance of the Taiwan issue in US-Chinese relations. They believe that divergent views between Beijing and Taipei, the need for ongoing intelligence collection (witness the EP-3 incident of 2001), and the changing nature of the military balance, make the Taiwan Strait the most likely place for the US to find itself in a major war. Taiwan's democratization makes foreign policy matters more open to domestic machinations (as seen in recent statements leading up to the March 2004 presidential election). With the

fall from power of the Kuomintang, the rearmament of Taiwan, and the lack of official negotiations, the authors anticipate greater possibilities for open hostilities.

Robert Ross of Boston College takes a very different tack on China, seeing it as a conservative, status quo power (2002, 15-26). He believes that engagement with China will maximize the possibility that China will adopt policies that coincide with US interests and that confrontation will result in a self-fulfilling prophesy. Ross takes on the notion that China is using its growing potential to exert influence in Southeast Asia and the South China Sea. Ross points out that under the Nixon Doctrine, China was intended to supplant the USSR as the dominant power in this region. In other words, by US design, China is already the status quo dominant power there (2002, 16). This came about after the collapse of the Soviet Union. As far as the South China Sea, China will lack power project capability in that region until 2020 and has not pursued a policy of using force in the dispute areas (2002, 20). As for the Pentagon, it sees China as downplaying its current power while readying its forces for future use. The Pentagon's strategy for dealing with China's rising military power is covered in the China and American National Security Strategies section of Chapter 6.

Findings on China's Economic, Political and Military Status. From our review of the status of China, we can draw the following conclusions:

1. China has reformed its economy from a command economy to a state development/laissez faire model.
2. China has transformed its economy from an agricultural society to a new industrializing society that is quickly advancing in size and sophistication.

3. China has adopted capitalist practices, embraced international organizations and practices, and by joining the WTO has made a commitment to continued reform.
4. Significant areas of the Chinese economy remain unreformed, notably the state-owned enterprises.
5. The Chinese political system remains largely unreformed although Beijing has provided a level of stability not seen in the decades prior to the Deng reforms. Still, it is not clear whether China can maintain the status quo without experiencing civil unrest.
6. China has transformed its political relationship with the outside world by rapidly increasing its engagement with intergovernmental organizations.
7. In the 1990s, Beijing began a significant improvement of its military forces, increasing its capability against Taiwan and those that would aid it in a conflict. This buildup has heightened concern in the US and regional capitals about China's intentions.

Test 1: A Broad Look at the Nature of US-Chinese Economic Interdependence

In the preceding pages, we have discussed China's current political and economic situation and how it came to be. In this section of this chapter, we seek to answer directly the research question: *How and to what degree have the US and China become economically Interdependent?* To accomplish this, we perform Test 1, looking at the true nature of the US-China relationship by going beyond the bonds of IT. While this

researcher holds that IT is as useful concept for viewing international relations, IT is a model and thus suffers from the constraints of narrow definitions and restricting methodology. We begin by examining the merchandise trade statistics IT employs and then delve into service trade, capital flows, student exchanges, and finally the cooperation and competition involved in energy issues.

China's growth as a trading nation has brought it into a much closer economic relationship with the United States. According to US Commerce Department data between 1982 and 2003, China's exports to the US expanded by 60 times (table 4.2). The hallmark of this trading relationship is the increasingly large trade deficits the US has developed with China. In 2003, the US trade deficit with China was \$124 billion--twice that of America's next largest partner, Japan (fig. 4.4). The trade gap has widened at an increasing rate since 1989 (Scott 2005, 5), as demonstrated in fig. 4.5.

Table 4.2 US merchandise trade with China in millions of dollars, 1982-2003
(Source: US Department of Commerce)

Year	US Exports	US Imports	US Balance
1982	2,912	2,502	410
1983	2,173	2,477	-304
1984	3,004	3,381	-377
1985	3,856	4,224	-368
1986	3,106	5,241	-2,135
1987	3,497	6,910	-3,413
1988	5,017	9,261	-4,244
1989	5,807	12,901	-7,094
1990	4,807	16,296	-11,489
1991	6,287	20,305	-14,018
1992	7,470	27,413	-19,943
1993	8,767	31,183	-22,416

1994	9,287	41,362	-32,075
1995	11,749	48,521	-36,772
1996	11,978	54,409	-42,431
1997	12,805	65,832	-53,027
1998	14,258	75,109	-60,851
1999	13,118	81,786	-68,668
2000	16,253	100,063	-83,810
2001	19,234	102,280	-83,046
2002	22,053	125,167	-103,115
2003	26,806	151,620	-124,814

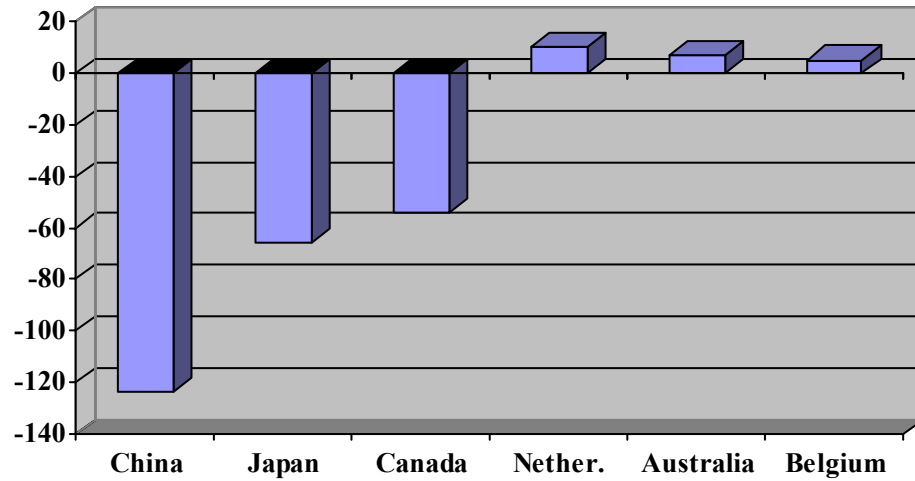


Fig. 4.4. US trade balances with selected countries in 2003 (Source: US Department of Commerce)

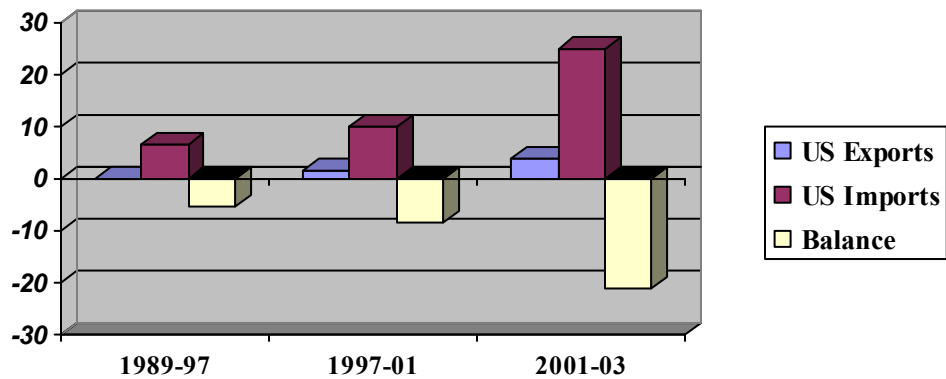


Fig. 4.5. Growth in US trade with China, 1989-2003 (Source: USITC 2004)

As shown in fig. 4.6, China's share of the US import market grew several-fold during the 1990s, while the share of other industrial states in Asia fell.

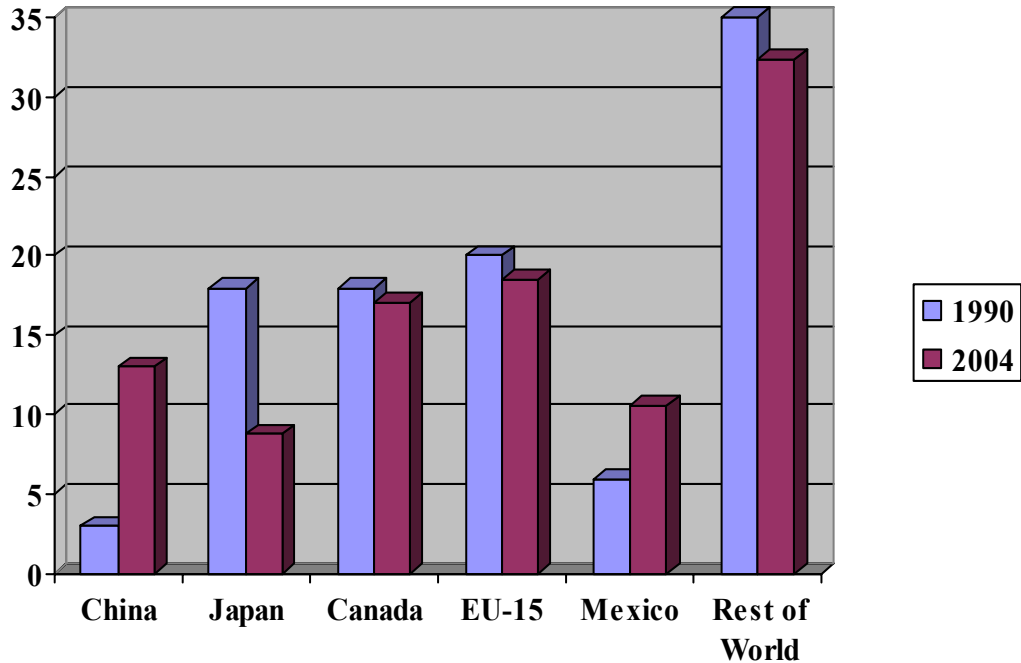


Fig. 4.6. Shares (percentages) of US imports by country and group, 1990 and 2004 (Source: Congressional Research Service)

The twin facts of China's fantastic economic growth and the ballooning US trade deficit with China drive much of the discussion of the nature of the economic relationship between the two countries. However, this two-part vision is extremely limited and fails to capture the intricacy of the relationship. Morgan Stanley economist Joseph P. Quinlan demonstrates that a simplistic understanding of the US-Chinese economic relationship can only lead to a poor grasp of how these two economies are tied together. He notes that the US trade deficit with China was \$US80 billion in 1999, the highest deficit with any country (Quinlan 2002, 91). The 2003 figure is \$120+ billion (table 4.3). These figures do not tell the full story, since many of the goods sold from China to the US are made by

affiliates of US companies, and much of the profit returns to the US. Nor does this capture the fact that much of the remaining deficit is arguably the result of products from third countries sold to the US indirectly through China, in order to capitalize on cheap labor. The corollary is that US imports from Taiwan, Japan, and South Korea are down, since we are buying from their affiliates operating within China rather than directly from the home countries (fig. 4.6). This inflates the trade imbalance and increases the perception that jobs and industries are fleeing the US for China. In reality, some of these industries (e.g., footwear production) fled the US to other Asian states years ago and have now migrated to China. In fact, during the 1990s, as much as 75 percent of China's exports to the US were simply redirection of exports from other developing countries (Hufbauer and Wong 2004, fn 1).

Lastly, US manufacturers prefer to sell to the Chinese from their affiliates within China, also to save on costs. Thus, while there is no direct international exchange in inter-affiliate trade, some profit is still returned to a US company, and the US in effect captures part of China's domestic market. This internal trade also reduces the amount of potential US trade to China companies. Rather than seeing the trade deficit as a failure of US economic prowess, one might view it as US manufacturers preferring to maximize American core competencies via direct investment rather than trade.

Table 4.3 also demonstrates that China and the US measure merchandise trade differently. Beijing's numbers would indicate that the US deficit in 2003 was less than half that suggested by American data. A good part of this discrepancy is due to how the two partners calculate trade statistics through Hong Kong. The US uses a "free-along ship" method to count entrepot trade (trade in which goods are imported and re-exported

without duties) between Hong Kong and China, while Beijing uses freight on board (Hufbauer and Yee 2004, 3-4). Thus, the US counts partially finished products exported to Hong Kong for additional assembly (value added) as both coming from China proper and worth the value when the finished product is re-exported from Hong Kong to the US.

Table 4.3 US merchandise trade with China and China's merchandise trade with the US in billions of dollars, 1982-2003

Year	US Trade w/ China (US Data)			China's Trade w/ the US (Chinese Data)		
	China Exports	China Imports	China Balance	World Exports	World Imports	World Balance
1982	3	3	.4	2	4	-3
1983	2	2	-.3	2	3	-1
1984	3	3	-.4	2	4	-1
1985	4	4	-.4	2	5	-3
1986	3	5	-2	3	5	-2
1987	3	7	-3	3	5	-2
1988	5	9	-4	3	7	-3
1989	6	13	-7	4	8	-3
1990	5	16	-11	5	7	-1
1991	6	20	-14	6	8	-2
1992	7	28	-20	9	9	-.3
1993	9	31	-22	17	11	6
1994	9	41	-32	21	14	7
1995	12	49	-37	25	16	9
1996	12	54	-42	27	16	11
1997	13	66	-53	33	16	16
1998	14	75	-61	38	17	21
1999	13	82	-69	42	20	22
2000	16	100	-84	52	22	30
2001	20	102	-83	54	26	28
2002	22	126	-103	70	27	43
2003	27	151	-124	93	34	59

Table 4.4 indicates that in 2003 China ran only a modest trade surplus of \$26 billion. While it had a positive flow of \$56 billion to the US and \$19 billion to the European Union, Beijing had trade deficits with Asian states. And China became the world's third largest *importer* of goods in 2003 (Hufbauer and Wong 2004, 2). In the same year, China's trade surplus only amounted to 2.5 percent of its GDP (Hufbauer and Wong 2004, 3). China then is not a simply a universal exporting juggernaut. Following its development model, it exports finished and semi-finished goods, but also imports the goods and equipment to make manufactured products and to improve the quality of its infrastructure. China is also relatively open to foreign trade and investment, a fact which has been codified by its accession in the World Trade Organization. Hufbauer and Wong (2004, 2-3) found, using two measures of openness, that China was more open to trade than both the US and Japan. Using the trade-to-GDP ratio, they found that China came in at 56 percent in 2002, while the US and Japan both came in at 22 percent. Using foreign direct investment (FDI)-to-GDP ratios, China was at 35 percent, Japan at 2 percent and the US 13 percent in 2002.

Table 4.4 China's merchandise trade balance with selected partners in billions of dollars, 2003

Country/Region	Exports	Imports	Trade Balance
Latin America	12	15	-3
European Union	72	53	19
East Asia (ex. Japan)	138	151	-13
ASEAN	31	47	-16

Middle East	16	15	1
Africa	10	8	2
Japan	59	74	-15
United States	92	34	59
Total	438	413	26

Hufbauer and Wong (2004, 3) also compared the trade differences between the US and China to that of Japan in past years. In 2000, when the US trade deficit with Japan peaked, that deficit represented 0.9 percent of US GDP. In contrast, the US trade deficit with China was 1.1 percent in 2003. In 2003, the US trade imbalance was greater with China than it had been at its peak with Japan. Current account balances of Japan and China provide an insight into both countries trade relationship with the rest of the world. From 1984–1991, Japan ran a current account surplus which equaled an average of 2.8 percent of its GDP. From 1994-2003, China’s global current account surplus averaged 2.0 percent of GDP, and in 2003, its current account surplus was an equally large part of its GDP (Hufbauer and Wong 2004, fn 15). In this sense, assuming China has reached its peak of current account surpluses with the world, its surpluses represented a smaller part of its economy than it did for Japan.

The US, on the other hand, runs a trade deficit with the world. In 2003, the US ran a \$600 merchandise trade deficit with the world, with China accounting for less than a quarter of that deficit (table 4.5). US global exports fell from \$697 billion in 2000 to \$625 billion in 2003 (Hufbauer and Wong 2004, fn 10). Notably, the US has run a

surplus in service trade for a number of years, reducing its overall trade deficit by almost \$60 billion in 2003 (table 4.5).

Table 4.5 US trade with the world and current account balance in billions of dollars, 1999-2003 (Sources: USITC Dataweb, US Dept. of Commerce, BEA statistics)

Year	Total Merchandise Trade		Total Services Trade		Goods & Services Balance	Current Account Balance
	US Imports	US Exports	US Imports	US Exports		
1999	1,017	642	181	265	-291	-291
2000	1,205	712	205	283	-414	-411
2001	1,133	666	202	275	-393	-394
2002	1,155	630	205	279	-451	-481
2003	1,250	651	246	305	-539	-542

Non-merchandise trade issues. IT does not consider many aspects of economic exchange in its methodology for measuring the relationship between two states. Among the important exchanges which are not included is trade in services, an important issue between the US and China because of the disparity between their levels of development and wage scales. In the case of the US and China, this trade goes in favor of the United States. Although the surplus is small, this does tend to suggest that IT misses the opportunity to measure a significant type of Economic Interdependence, since services often involve interpersonal exchanges and the sharing of business practices and knowledge. Furthermore, if table 4.6 is correct, the US level of services trade with China should be expected to grow as the relationship matures. This is certainly a hope of the US businesses that supported China's entry into the World Trade Organization.

Table 4.6 US-China trade, 1999-2003 (Sources: USITC Dataweb, US Dept. of Commerce, BEA statistics)

Year	Total Merchandise Trade		Total Services Trade		Goods & Services Balance
	US Imports	US Exports	US Imports	US Exports	
1999	82	13	3	4	-68
2000	100	15	3	5	-82
2001	102	18	4	6	-82
2002	125	21	4	6	-102
2003	152	27	5	7	-123

One of the more compelling non-trade indicators of Economic Interdependence is capital flows, an issue that Oneal and Russett have not accounted for in their methodology. We noted in Chapter 3 that Gartzke, Li and Boehmer (2001, 391-93) have attempted to broaden the definition of Interdependence by including the effects of cross-border movement of capital. They found that Interdependence in capital markets reduces conflict in a dyad (391). Given the relative levels of development of the US and Chinese economies, it is not too surprising to see that investment flows largely in one direction. FDI in the US totaled \$1.5 trillion in 2004; only \$490 million of that total was held by Chinese firms (Samuelson 2005). In contrast, US firms have thirty times that amount (\$15 billion) invested in China (Samuelson 2005). The corollary to the huge trade surplus that the China has with the US is the tremendous investment (and asset ownership) the US has in China. However, capital flows have another component. The US borrows heavily from the global capital market to finance its budget deficits. By 2005, China held

\$243.2 billion in US public debt, up from only \$60.3 in 2000. In contrast, the largest holder of US public debt, Japan, held \$680.2 billion in 2005 (Tanner 2005, 4).

IT fails to take into account the impact of these capital flows. Oneal and Russett do not consider how private US companies become invested in the future of China's political and economic stability via its FDI. Nor does it consider how Chinese companies and the government rely upon this FDI to continue to expand the Chinese economy. Furthermore, Chinese sponsorship of US public debt puts US national lawmakers and policy makers at the mercy of Beijing. In this case, IT appears to undercut its own premise, since in this instance, capital flows have increased dramatically in recent years, along with merchandise trade flows. IT does identify private and public actors as the mechanism through which conflict is tamped down. According to the theory, such actors are invested in continued economic exchange and work to ensure the status quo is maintained. We have identified the economic activity and the actors and their motivations, but IT does not account for activity outside of merchandise trade.

There are other, albeit more esoteric, indicators of Economic Interdependence. Population exchanges between the two countries are largely motivated by the search for economic advantage. In this case, the US and China are part of an international labor market much in the same way that they are part of a global commodities market. Another measure concerns the number of students studying in each other's countries. From a level in 1972 in which only a handful of Chinese students were studying in the US and almost no US students were studying in China the trend has been reversed. On the side of US students studying in China there were 7,437 US students in China in the 2003-04 school year (*Chronicle of Higher Education* 2005; table 4.7). This was the ninth most

popular country for US students, far behind first placed United Kingdom at 32,237 students. It is important to note that this was a ninety percent increase over the previous year, representing the highest year-to-year increase of any nation (*Chronicle of Higher Education* 2005; table 4.8). On the other hand, only India sent more students to the US than China, which had 62,523 students in the US at that time (*Chronicle of Higher Education* 2005; table 4.8). An additional 7,180 students in the US came from Hong Kong.

The implications are several. Chinese students are learning about the US although American students are not learning about China. Returning Chinese students bring back US values and practices in business and sciences. Clearly, there is a cultural aspect to this, particularly as defined by liberals, since Chinese students who study in the US are exposed to liberal ideas and return to China (if they do) and can act as change agents. Chinese students remaining in the US provide their expertise to the American economy, while the PRC relies on returnees to improve its industrial base. *The Economist* (2005) reports that foreign students add \$13 billion annually to the US economy. Also, the US benefits since it experiences job creation in university positions. Liberals (and IT supporters) would probably say this is increasing Interdependence, but IT does not account for this. Perhaps merchandise trade is a good barometer of these economic and pseudo-economic ties and thus captures the effect, but this matter has not been explored.

Table 4.7 Top destinations for US students, 2003-4 (Source: Institute of International Education; *Chronicle of Higher Education*)

Destination Country	Number of Students
1. Britain	32,237
2. Italy	21,922
3. Spain	20,080
4. France	13,718
5. Australia	11,418
6. Mexico	9,293
7. Germany	5,985
8. Ireland	5,198
9. China	4,737
10. Costa Rica	4,510
11. Japan	3,707
12. Austria	2,444
13. New Zealand	2,369
14. Cuba	2,148
15. Chile	2,135

Table 4.8 US schools of higher learning, foreign students' countries of origin, 2003-4 (Source: Institute of International Education; *Chronicle of Higher Education*)

Origin Country	Number of Students
1. India	80,466
2. China	62,523
3. South Korea	53,358
4. Japan	42,215
5. Canada	28,140

6. Taiwan	25,914
7. Mexico	13,063
8. Turkey	12,474
9. Thailand	8,637
10. Indonesia	7,760
11. Germany	8,640
12. Britain	8,236
13. Brazil	7,244
14. Colombia	7,334
15. Kenya	6,728
16. Hong Kong	7,180
17. Pakistan	6,296
18. France	6,555
19. Malaysia	6,142
20. Nigeria	6,335

Cooperation and Competition in the Energy Sector. China's economic growth has many direct and indirect influences upon the Sino-US relationship. Many of these results are economic in nature but are not reflected in the trade data used by Interdependence theorists. One sector in which China has experienced dramatic changes is energy. We will now look at how China's energy strategy has evolved and how competition over energy sources is changing the nature of economic relations with the United States.

With the world's third largest reserves of coal (after the US and Russia) and the world's largest coal extracting industry, China seemingly has a secure source of energy and even an exportable commodity (Moseley 1998, 67-68). On the other hand, coal has a host of drawbacks, including an exceptionally inefficient production plant (some 80,000

mines of varying sizes), an inadequate transportation system, and a mismatch between the location of the best coal and the power generating plants (Moseley 1998, 66-69).

China's petroleum industry has been a success story, at least until recently. In the 1960s and 1970s, China oil industry grew at double digits, and China became one of the world's leading producers (and a minor exporter). But those oilfields have been winding down their output, and new fields in Central Asia and the South China Sea have barely kept production at pace, and in 1993 China became a net importer of petroleum (Caruso 2005, Slide 11). Even at lower rates of growth, China should expect to see its oil imports increase, particularly as more cars crowd the streets. Another important alternate resource, natural gas, has largely been ignored until recently. However, China found that partnering with western expertise produced fairly quick results in the huge natural gas fields off Hainan Island in the South China Sea. Here again, China's needs will probably outpace its production (Moseley 1998, 84).

China has perhaps the most abundant hydroelectric assets in the world, and hydropower accounted for seventeen percent of total electrical production in 1996 (Moseley 1998, 87). China is moving aggressively to exploit this asset. At the same time, many would say such projects as the Three Gorges Dam are too aggressive and uneconomical and environmentally unsound. Other renewable energy resources (geothermal, biomass) are indeed pursued but not at a level that would affect national energy needs (Moseley 1998, 112).

The greatest obstacle for improving China's energy situation is its underdeveloped infrastructure. While China's economy (particularly among coastal provinces) has been expanding rapidly the last two decades, its infrastructure (particularly

in provinces that provide raw materials) has not kept apace. Transportation's failings have already been noted; 42 percent of all rail lines are dedicated to coal transportation (Moseley 1998, 114). Road construction is also out of step with need. With more and larger cars on the road, this shortfall is leading to road congestion and reduced energy efficiency. Port facilities for exporting coal and importing oil are being built at a great speed but not quickly enough. In addition, the nation's electrical power grid and oil pipeline systems are also lacking, due to the long geographical distances between extraction sites and conversion to electricity.

Another obstacle is the artificial price of energy inside China, even after decades of market pricing reforms. As an example of the consequence of this policy, natural gas prices provide a disincentive for investment, particularly from foreign sources, which have been instrumental in many energy projects. And in a familiar refrain, the central government uses these low prices, to subsidize poorly performing state owned enterprises (Moseley 1998, 122). In recent years, China worked to reform energy pricing, largely in preparation for WTO entry. However, by making security a higher priority than market mechanisms or technical feasibility, China has at times chosen an inefficient and ineffective overall energy policy.

China faces growing energy needs, an ever-larger share of which will come from imported petroleum. Industry will require more resources, but much of the demand will come from empowered consumers, who will buy and drive more autos and have access to more heating and cooling systems. In 2003, Chinese automobile production reached 4.44 million units, a 36.6 percent rise over 2002, making it the fourth largest car producer in the world (Zhu Min 2004). The number of cars in China grew from 10 million in 1990 to

23.8 million in 2003 (*FOURIN China Auto Weekly* 2005). The number of vehicles in China is projected to grow to 120 million in 2020, according to PRC estimates (Dorian 2005, slide 11). In 2003, China surpassed Japan as the second largest oil consumer after the United States, and it accounted for about a third of recent increase in global demand (Wonacott 2003). Oil consumption increased to 6.4 million barrels/day in 2004; oil imports increased by 34 percent that year (Dorian 2005, slide 4-11). In comparison, the United States, the world's largest consumer, used 20.4 million barrels/day in 2004 (US Department of Energy 2005). The International Energy Agency forecasts that imports will double by 2010, and China will import 10 million barrels/day by 2030, matching the current US import rate (Wonacott 2003).

China has turned for its increased oil needs to Middle East states, which provide most of the oil for Japan and Western Europe. Gulf states are already cooperating with China, and several Gulf oil companies have invested in Chinese oil exploration (Dorian 2005, slide 11). This raises US security concerns, because of China's clear willingness to deal with Iran. As Beijing's interests, relations and dependencies in the region grow, it might hamper US freedom of action in the area. Of course, recent events trend in the opposite direction. While US actions in the Gulf have been seen as unilateral; in fact, other states have benefited from a very stable and cheap flow of oil. China may not be interested in seeing the US flex its muscles, but it has the same goal, a steady flow of oil from the Persian Gulf. China is also working with Central Asian nations and Russia for energy supplies and the pipelines to bring oil and gas east (Dorian 2005, slide 9, 11; Wonacott 2003). Lastly, China has been working with other states to create joint ventures and buy up overseas reserves in Central Asia, South America and Sudan (Dorian

2005, slide 9, 11). China is paying a premium for its energy security, bidding 30 percent more than the next higher bidder for rights to the Uzen oilfield in Central Asia and twice as much as its competitors for tracts in Venezuela (Moseley 1998, 141).

There are many other areas besides energy where the US and China and other growing economies will compete. China's hunger for resources is great; in 2003, it used half of the cement, 36 percent of the steel and 30 percent of coal produced in the world (Hufbauer and Wong 2004, fn 5). Furthermore, China is not the only expanding economy which is forcing competition in the oil markets. India, which relies on imports for 70 percent of its petroleum, is expected to see demand double from 2005 to 2030 (Sengupta 2005). These two factors, the competition for energy and other resources and the rise of other economies, will complicate the US-China economic relationship in years to come.

Competition is not the only hallmark of China's changing energy sector. China has learned to depend on foreign assistance, financial and technological, to develop its future energy assets. Foreign investment in petroleum increased 20 fold in the 1980s, and foreign investment provided as much as half of all funding for energy projects (Johnson 1999, 273). Additionally, US technology and investment are important for overcoming the crippling effects of the poor infrastructure noted above that prevents China from getting the optimal use of its energy sector. On the downside, future foreign involvement may decrease because of Beijing's concerns about dependency and the inability to overcome inefficiencies in the Chinese system.

The energy situation between the US and China has two main distinctions. First, we do not know its future, other than to say it will probably change and not for the better.

Second, it is of critical importance to the relationship despite the fact that virtually no trade of the commodity itself exists between the members of this dyad. In other words, IT tells us little about how the energy issue will impact relations and conflict between the US and China. While IT predicts that cooperation in the form of trade may reduce conflict, IT tells us nothing about how competition in the economic sector may increase the potential conflict. This requires an understanding of comparative advantages one might gain from using game theory or realist concepts. For example, is there an increased risk of conflict because the US has a comparative advantage due to its superior technology to exploit energy assets? Or, does the trade in such technology reduce the potential for conflict?

Results of Test 1: The Nature of US-Chinese Economic Interdependence

Test 1 is intended to review what an observer would see of the US-Chinese economic relationship unaided and unencumbered by Interdependence Theory. In this case, we found that the relationship is both complex and compelling. While IT may provide a framework of how these economies intertwine, we developed a deeper understanding by looking at other factors than merchandise trade. From our examination of the nature of the US-China economic relationship, we take away the following findings:

1. From our brief tour of the trade figures, we can see that US Economic Interdependence with China, as measured by trade, has increased significantly

since 1978. China is now the United States' third largest trading partner (Hufbauer and Wong 2004, 3).

- a. China has a high level of openness in trade and investment in comparison to the United States.
 - b. By comparing China to Japan, a significant partner with the US, we see that Chinese trade deficits with the US and the world are not unprecedented.
 - c. In services trade, the US actually enjoys a trade surplus with China.
 - d. The US's huge trade deficit with China is partly due to re-exporting via China.
 - e. Increased capital flows since the Deng Reforms have provided advantages for both states. China receives FDI to expand its industry, while the US gains investment in a growing market. Also, the US receives funding for its public debt, while China enjoys the benefit of guaranteed returns on loans to the world's largest economy.
2. China and the US have become economically integrated in ways exceeding the "merchandise trade only" measurements of IT.
 3. In our examination of the energy sector, we were reminded that economic relations are not solely about trade. Multiple concepts are needed to explain the economic relationship. This tends to undercut the utility of IT. This issue will be explored in a more in-depth in our case studies in the following chapter.

4. Interdependence Theory fails to account for all the ways in which the United States and China are economically intertwined. Merchandise trade is important, but so are services trade and capital flows. IT's failure to capture these exchanges may mean the impact of Interdependence on conflict is underrepresented by current IT methodology.

Summary. In this chapter, we have examined how China has reformed its economy from a command economy to a state development/laissez faire model. By adapting capitalist practices, embracing international organizations and standards, and joining the WTO, China has made a commitment to continued reform. The resulting increased trade with the US and other states has transformed China's economy. The observations in the preceding pages in some ways support IT and in other ways expose its limitations. In the next chapter we will look at the actual data as applied to the Sino-American case and explore the implications of this evidence.

CHAPTER 5

DATA AND ANALYSIS

Introduction

In Chapter 4, we begin our analysis of the Sino-American economic relationship by stepping back from the methodology that drives Interdependence Theory. In this chapter we directly reengage IT, returning again to the measurement methods of John Oneal and Bruce Russett, who have developed the most compelling IT over the past decade. We will determine what relevance IT and its main subvariants have for the current relationship between the US and China by conducting Tests 2 to 4 of our research approach. Test 2 will examine the data in the case using only the Oneal and Russett method. Test 3 will focus on the applicability of Gelpi and Grieco's work on the relationship of polity type to the impact of Interdependence on conflict in a dyad. Taken together, Tests 2 to 3 capture the full gamut of Interdependence Theory ways by which the US-Chinese relationship might be examined. Test 4 attempts to examine IT against the backdrop of actual events by exploring two dyadic events: China's entry into the WTO and the 1995-6 Taiwan Strait Crisis. This final test will also examine how two theories (IT, which is a component of liberalism, and realism) would interpret these events, thus comparing the utility of IT versus another contending theory of international relations. The final section of this chapter will be a summary of these three tests. In this

fashion, we will address the second research question: How does IT explain the nature of the relationship between the US and China? We begin the chapter with the second test of our four tests by examining the raw data using the Oneal and Russett model.

Test 2: Sino-US Economic Interdependence using Oneal and Russett's Methods

Oneal and Russett use the independent variable, dependency, as their primary measure of Interdependence. We recall that dependency is defined as the total of merchandise trade between two states as a percentage of each state's national income as measured by GDP. For Country A, its dependency with Country B would be expressed as: Country A's Imports and Exports with Country B / Country A's GDP. In their 2003 work, OR continued to rely upon the *Penn World Tables* and IMF's *Direction of Trade* figures as their main sources on GDP and dyadic trade, respectively, and they employ the Correlates of War database for measurement of Militarized Interstate Disputes (MIDs) (Oneal, Russett and Berbaum 2003, 376-77). We use a recent version of the *Penn World Tables*, version 6.1, to provide GDP figures from 1978 to 2000, and we resource the *Direction of Trade Statistics Yearbook* for the same period (Heston et al, 2002; IMF 1983, 1990, 1997 and 2004).

The *Penn World Tables* data, using purchasing parity power, shows that from 1978 to 2000, US GDP grew from \$2.2 trillion to \$9.8 trillion, while China's GDP grew from \$432 billion to \$4.8 trillion (table 5.1).

Table 5.1 US and China population and GDP (Source: *Penn World Tables* from Heston et al 2002)

	US			China		
	Pop.	GDP/C	GDP	Pop.	GDP/C	GDP
	(in millions)	(in thousands)	(in millions)	(in millions)	(in thousands)	(in millions)
1978	223	10218.8	2278790.2	956	452.51	432599.6
1979	225	11303.6	2543301.0	969	541.42	524636.0
1980	228	12170.3	2774835.2	981	617.36	605630.2
1981	230	13497.4	3104392.8	994	709.24	704984.6
1982	232	13902.9	3225468.2	1009	819.25	826623.3
1983	234	14944.6	3497038.7	1023	905.02	925835.5
1984	236	16483.5	3890106.0	1037	1046.72	1085448.6
1985	239	17504.8	4183647.2	1051	1133.44	1191245.4
1986	241	18330.8	4417730.0	1067	1231.74	1314266.6
1987	243	19349.2	4701858.0	1084	1344.61	1457557.2
1988	245	20656.1	5060739.6	1102	1419.55	1564344.1
1989	247	21988.6	5431191.6	1119	1400.5	1567159.5
1990	250	23005	5751237.5	1135	1568.28	1779997.8
1991	253	23471.1	5938180.7	1151	1788.93	2059058.4
1992	255	24517.7	6252018.6	1165	2031.61	2366825.7
1993	258	25504.5	6580171.3	1178	2306.04	2716515.1
1994	261	26834.1	7003705.3	1191	2551.97	3039396.3
1995	263	27894.9	7336364.0	1203	2759.92	3320183.8
1996	266	29193.9	7765580.1	1215	2972.61	3611721.2
1997	268	30797.8	8253821.1	1227	3141.07	3854092.9
1998	271	32230.2	8734381.5	1239	3317.79	4110741.8
1999	273	33725.8	9207135.2	1250	3483.39	4354237.5
2000	275	35618.7	9795134.3	1259	3843.67	4839180.5

From IMF *Direction of Trade* figures, we are reminded that total bilateral trade (using US statistics) from 1978 to 2000 grew from \$405 million to \$122 billion (table 52). As noted in Chapter 4, US trade figures do not match Chinese trade figures, and neither correlates exactly with IMF numbers. We use the IMF figures to remain consistent with OR's methodology.

Table 5.2 US trade with China, in US\$ millions
(Source: IMF 1983, 1990, 1997 and 2004.)

	Exports	Imports	Total Trade
1978	48	357	405
1979	57	656	713
1980	162	1164	1326
1981	258	2062	2320
1982	106	2502	2608
1983	66	2477	2543
1984	3004	3381	6385
1985	3856	4224	8080
1986	3106	5241	8347
1987	3497	6910	10407
1988	5017	9261	14278
1989	5807	12901	18708
1990	4807	16296	21103
1991	6287	20305	26592
1992	7470	27412	34882
1993	8767	31183	39950
1994	9287	41362	50649
1995	11748	48521	60269
1996	11978	54409	66387
1997	12805	65832	78637
1998	14258	75109	89367
1999	12944	86481	99425
2000	15964	106215	122179

To calculate dependency (Country A's Imports and Exports with Country B / Country A's GDP), we employ the figures from tables 5.1 and 5.2; the calculations are presented in table 5.3, and the data is graphed in fig. 5.1. The results are a dramatic representation of the increase in trade (and Interdependence) between the two states. In

this case, we find our numbers are very close to OR's (see below). The US is the less constrained state, with 1.25 percent of its GDP represented by bilateral trade in 2000. In contrast, China's trade dependency is twice as high at 2.5 percent of its GDP. OR assume that the less constrained state (or less trade dependent state) is the "weak link in the chain of peace" and has the greater influence in determining whether conflict arises. OR do account for both the less and more dependent states in their regression model, but in the end, OR found that the less dependent state had the only statistically significant influence in determining the potential for conflict in cases where the initiator is unknown. Ironically, then it is the United States, according to Oneal and Russett, which will most determine the potential for conflict in the Sino-American dyad although China will also feel the impact of Interdependence.

Table 5.3 US and China Economic Interdependence (Source: calculated from *Penn World Tables/IMF*)

	US IT		China IT
1978	0.000178		0.000936
1979	0.00028		0.001359
1980	0.000478		0.002189
1981	0.000747		0.003291
1982	0.000809		0.003155
1983	0.000727		0.002747
1984	0.001641		0.005882
1985	0.001931		0.006783
1986	0.001889		0.006351
1987	0.002213		0.007140
1988	0.002821		0.009127
1989	0.003445		0.011938
1990	0.003669		0.011856
1991	0.004478		0.012915
1992	0.005579		0.014738

1993	0.006071		0.014706
1994	0.007232		0.016664
1995	0.008215		0.018152
1996	0.008549		0.018381
1997	0.009527		0.020404
1998	0.010232		0.021740
1999	0.010799		0.022834
2000	0.012473		0.025248

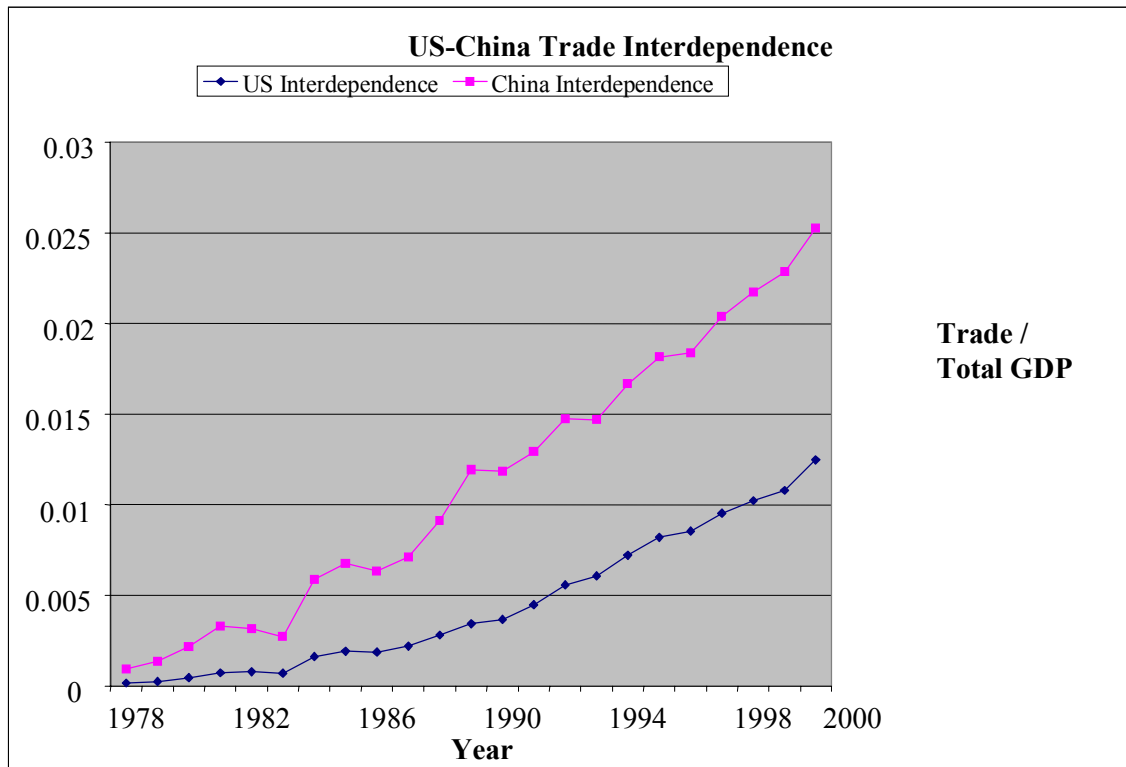


Fig. 5.1. US and China Economic Interdependence (Source: calculated from *Penn World Tables/IMF*)

Oneal and Russett are aware that the US-Chinese case represents a uniquely important test of IT. They (with Michael Berbaum) discussed the case in a single paragraph (with footnote) of their 2003 article. Here, OR investigated the, “importance

of the Kantian variables ... illustrated by considering contemporary relations between the United States and China” (Oneal, Russett and Berbaum 2003, 383). Looking at the period from the mid-1960s to 2002 (roughly the period we are studying), OR found that the US and China went from having virtually no trade to a very significant level of Economic Interdependence. US-China trade (both imports and exports) accounted for 1.20 percent of US GDP in 2002. This puts US-China Interdependence in the 90th percentile of trading states. Based upon their examination of hundreds of dyads from the mid-1800s to the present, OR submit this represents a 27 percent decrease in the potential for conflict compared to when the states had almost no trade. Calculating the impact of all three legs of the tripod (Interdependence, Democracy and Joint IGO Membership), OR believe that the potential for conflict has been reduced by 58 percent for the dyad. This translates to the probability of a military dispute with at least one fatality falling from 1.9 percent to 0.8 percent.⁸ Oneal and Russett’s decade of research on IT has led them to quantify that the increase in Economic Interdependence alone has reduced the chance for conflict by more than a quarter. As we have noted, this assertion does not go unchallenged by critics.

Analysis of Sino-US conflict data. Despite providing statistical evidence that bilateral trade reduces conflict, Oneal and Russett and other theorists cannot predict that in a specific case of bilateral Interdependence the result will be a 27 percent reduction of the risk of military conflict between the members of that dyad. Aggregated data can only suggest aggregated future outcomes, so one can merely say that past experiences in

⁸ (OR also cover China’s integration in a Kantian world in their 2001 book, but they look at the matter in a systemic sense rather than at the dyadic level. See Russett and Oneal 2001, 282-305.)

these circumstances of Interdependence, the aggregate level of conflict declined 27 percent. In some specific cases in the past, the IT impact may have more or less than 27 percent or may have lead to increased conflict. Similarly, one cannot use the China case to prove or disprove IT, since IT suppositions are based upon aggregated findings of thousands of dyads over many decades. However, if we retrace some of the steps OR took in their methodology, we can see how conflict increased or decreased in the China case as Interdependence increased over the past few years.

OR used the Correlates of War (COW) database to measure the dependent variable, conflict or Militarized Interstate Disputes (MIDs). From the Correlates of War “Codebook for the Dyadic Militarized Interstate,” we define the terms in tables 5.4 and 5.5 (Ghosn et al 2003):

1. disp # (the dispute number from COW’s catalogue of MIDs)
2. state (USA, CHN for China, TAW for Taiwan)
3. startmo/startyear (month and year in which state joined the conflict)
4. hostility level (highest level of hostile action reached by a state in an MID),
which includes:
 - a) 1 = no militarized action
 - b) 2 = threat to use force
 - c) 3 = display of force
 - d) 4 = use of force
 - e) 5 = war

In addition, we have computed and added:

1. dislength (dispute length, which is equal to the number of months both states were simultaneously involved in the MID)
2. hihostlev (the highest hostility level on a 1 to 5 scale either the US or China reached during the MID)

The raw data in tables 5.4 and 5.5 is condensed in table 5.6, which shows the cumulative MIDs per year. Figures 5.2 and 5.3 are graphic representations of the data in table 5.6.

Table 5.4 Sino-US Militarized Interstate Disputes (MIDs), 1949-1977
(Source: Correlates of War from Jones et al 1996 and Ghosn et al 2004)

disp #	state	startmo	startyear	dislength (mos.)	hostility level	hihostlev
50	USA	2	1953		3	
50	CHN	2	1953	35	4	4
51	CHN	9	1950		5	
51	ROK	6	1950		5	
51	USA	6	1950	34	5	5
53	USA	8	1956		3	
53	CHN	8	1956	1	4	4
172	TAW	1	1962		4	
172	CHN	1	1962		4	
172	USA	2	1962	10	3	4
173	USR	9	1958		2	
173	USA	7	1958		3	
173	TAW	7	1958		4	
173	CHN	7	1958	5	4	4
251	CHN	4	1965		4	
251	USA	4	1965	1	4	4

611	CHN	7	1964		2	
611	USR	2	1964		2	
611	USA	2	1964		5	
611	RVN	7	1964		5	
611	DRV	2	1964	99	5	5
633	USA	6	1950		3	
633	TAW	10	1949		4	
633	CHN	10	1949	2	4	4
634	USA	10	1949		1	
634	CHN	10	1949	3	4	4
1216	CHN	12	1965		2	
1216	CAM	12	1965		3	
1216	RVN	12	1965		3	
1216	THI	12	1965		3	
1216	USA	12	1965	5	4	4
1353	USA	5	1962		3	
1353	THI	2	1962		4	
1353	DRV	1	1962		4	
1353	LAO	1	1962		4	
1353	NEW	5	1962		3	
1353	UKG	5	1962		3	
1353	AUL	5	1962		3	
1353	USR	2	1962		3	
1353	CHN	5	1962	26	4	4
1363	LAO	12	1960		4	
1363	DRV	12	1960		4	
1363	THI	4	1961		2	
1363	CHN	4	1961		2	
1363	USA	1	1961		3	
1363	USR	12	1960	1	3	3
1806	CAM	1	1968		4	
1806	RVN	1	1968		4	
1806	CHN	1	1968		2	
1806	USA	1	1968	1	4	4
2002	CHN	5	1960		1	
2002	USA	5	1960	1	3	3

2032	CHN	5	1955		4	
2032	USA	5	1955	1	4	4
2033	CHN	7	1954		4	
2033	USA	7	1954	1	4	4
2035	CHN	8	1953		1	
2035	USA	8	1953	1	3	3
2049	USA	6	1957		3	
2049	TAW	6	1957		4	
2049	CHN	6	1957	1	4	4
2929	CHN	10	1965		1	
2929	USA	10	1965	13	4	4
2936	CHN	9	1969		1	
2936	USA	9	1969	1	4	
2947	CHN	2	1971		1	
2947	USA	2	1971	1	3	3
2948	CHN	8	1972		1	
2948	USA	8	1972	1	4	4
3361	DRV	12	1961		1	
3361	USR	2	1962		2	
3361	CHN	2	1962		2	
3361	USA	12	1961	12	3	3
			Average length in months	11.13	Average hihostlev	3.7

Table 5.5 Sino-US Militarized Interstate Disputes (MIDs), 1978-2001
(Source: Correlates of War from Jones et al 1996 and Ghosn et al 2004)

disp #	state	startmo	startyear	dislength (mos.)	hostility level	hihostlev
4064	USA	12	1995		3	
4064	TAW	7	1995		3	
4064	CHN	7	1995	3	3	3
4065	ROK	8	1994		1	

4065	USA	8	1994		1	
4065	CHN	8	1994	2	3	3
4088	USA	7	1999		3	
4088	TAW	2	1999		3	
4088	CHN	2	1999	8	3	3
4280	USA	4	2001		3	
4280	CHN	4	2001	3	4	4
4281	TAW	3	2001		3	
4281	USA	4	2001		3	
4281	CHN	3	2001	4	3	3
4336	USA	3	2001		1	
4336	CHN	3	2001	12	3	3
			Average length in months	5.33	Average hihostlev	3.17

Table 5.6 Sino-US Militarized Interstate Disputes (MIDs), 1949-2001
(Source: Correlates of War from Jones et al 1996 and Ghosn et al 2004)

Pre-Deng Reforms	# of MIDs		Post-Deng Reforms	# of MIDs
1949	1		1978	0
1950	2		1979	0
1951	0		1980	0
1952	0		1981	0
1953	2		1982	0
1954	1		1983	0
1955	1		1984	0
1956	1		1985	0
1957	1		1986	0
1958	1		1987	0
1959	0		1988	0
1960	1		1989	0
1961	1		1990	0
1962	3		1991	0
1963	0		1992	0

1964	1		1993	0
1965	3		1994	1
1966	0		1995	0
1967	0		1996	1
1968	1		1997	0
1969	1		1998	0
1970	0		1999	1
1971	1		2000	0
1972	1		2001	3
1973	0			
1974	0			
1975	0			
1976	0			
1977	1			
MIDs/year	.79/year		MIDs/year	.26/year

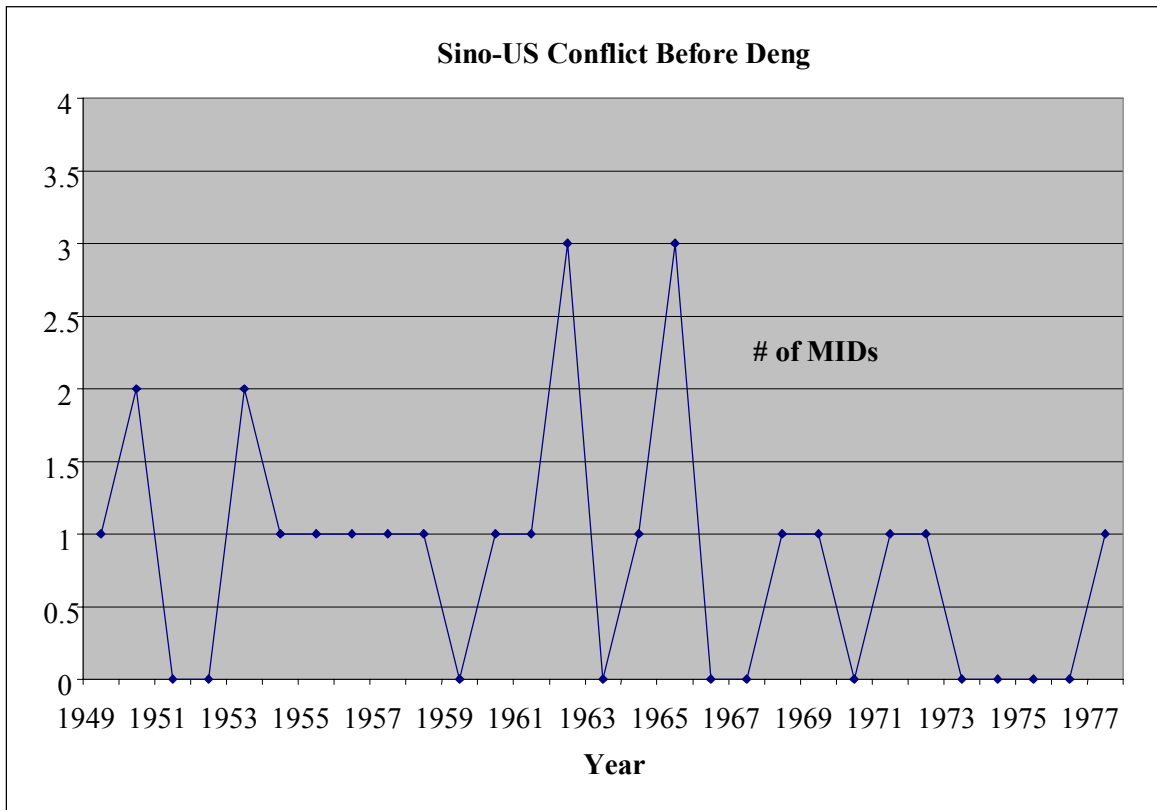


Fig. 5.2. Sino-US MIDs, 1949-1977 (Source: Correlates of War from Jones et al 1996 and Ghosn et al 2004)

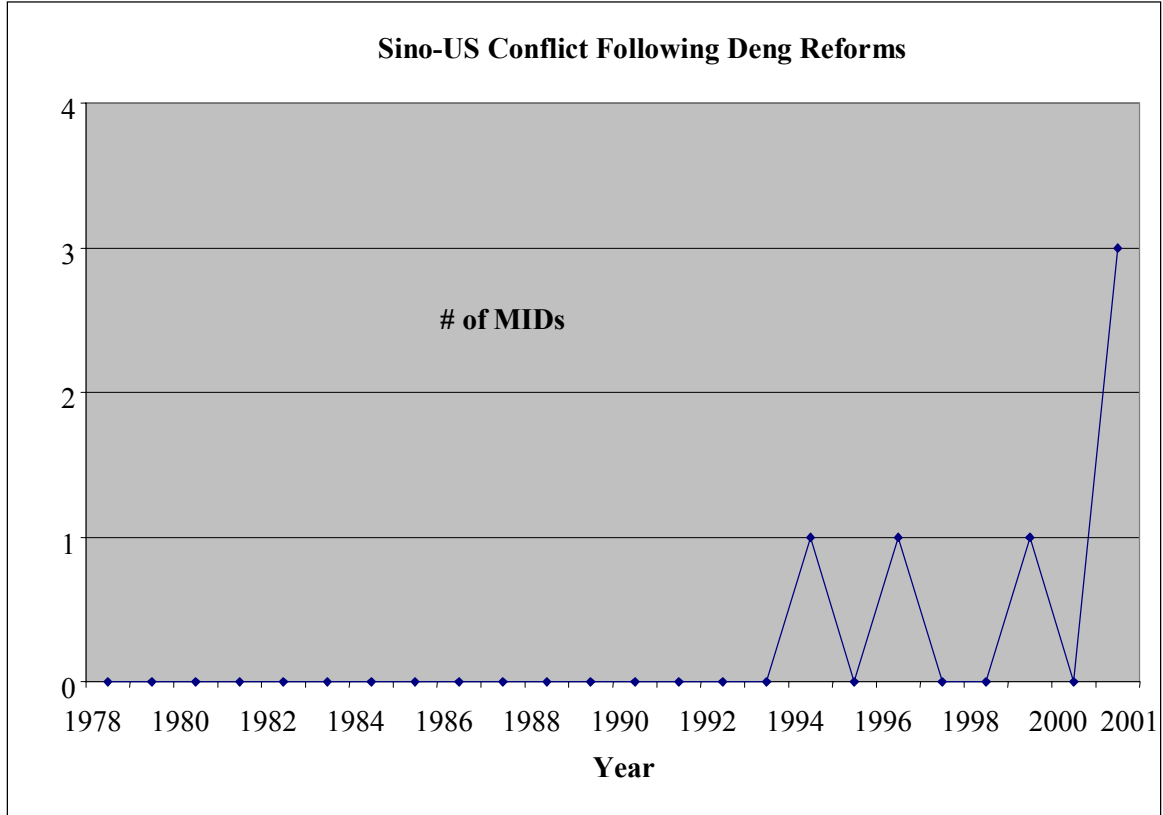


Fig. 5.3. Sino-US MIDs, 1978-2001 (Source: Correlates of War from Jones et al 1996 and Ghosn et al 2004)

An examination of changes in the independent and dependent variables provided in tables 5.4 to 5.6 and figures 5.2 to 5.3 produces contradictory results. During the period of no Interdependence (1949-1977) there were 23 Militarized Interstate Disputes, while during the period of increasing Interdependence (1978-2001) there were only 6 Militarized Interstate Disputes, including only a single fatality (the EP-3 incident in 2001). That is an average of .79 MID/year (23 MIDs/29 years) during the early period compared to .26 MIDs/year (6 MIDs/24 years) following the Deng reforms (table 5.6). Tables 5.4 and 5.5 demonstrate that the length of hostilities were longer during the pre-

Interdependence period (average of 11.13 months versus 5.33 months) and reached a higher average level of hostile action (3.7 versus 3.2 on the 1-5 COW scale). Several hundred thousand military members died during the 1949 to 1977 conflicts, while one airman died in the 1978 to 2001 period (the Chinese fighter pilot in the April 2001 EP-3 incident over the South China Sea). All of these factors tend to support the claim that Interdependence has reduced the level of conflict between the US and China.

On the other hand, the six Militarized Interstate Disputes during the 1978-2001 period all occurred from 1994-2001, and three occurred during 2001, when the two economies were becoming truly intertwined. Again, Interdependence, even at the 90 percentile, is not a guarantee of an end to conflict. MIDs, even those with fatalities, can occur when states are coupled through their trade. There are mitigating factors; for example, the Deng reforms certainly did not impact Interdependence in a significant way until the 1990s. But again, the conflicts did not occur until the period when Taiwan started to express interest in declaring independence from the Mainland. Of course, IT does not take into account all the other factors that might lead to conflict. IT does account for such things as formal alliances, military capabilities and proximity of states, but it does not address the specific security environment and its impact on conflict. In the pre-Deng era, China experienced a change in political system (to communist rule), established a revolutionary government, fought to assert control all of its claimed territory (including Taiwan), joined and later left the Soviet Bloc, fought directly in the Korean War and less directly in the Vietnamese conflict and experienced the internal confusion caused by Mao's Cultural Revolution. The United States did not experience a revolution in political or economic systems during the same period, but it expanded its

international security commitments in order to lead the Free World in the Cold War and also fought directly in Korea and Vietnam.

Indeed the US and China were in direct confrontation during much of the Cold War but found themselves in an informal, strategic alliance against the Soviet Union beginning in the early 1970s. In fact, there were no MIDs between 1972 and 1993, when the Sino-American strategic alliance against the USSR and later Russia was the status quo. This period straddles both the pre-Deng and post-Deng reforms period. In other words, one might look to active, security-driven decisions by national leaders rather than IT's impact to describe why these states did not have conflict during this period. More to the point, there has been a fairly consistent level of conflict over the one issue which is most likely to bring the US and China to war—Taiwan. In the pre-reform period, there were four conflicts involving the US, China and Taiwan (.14 MIDs/year), and three such conflicts (.125 MIDs/year) in the post-Deng reform periods. Whether in a state of Economic Interdependence or not, the Taiwan issue drives conflict between the US and China.

Of course, the US and China are not the only players in this equation, and both members of the dyad have complex relations with other states. The US has had ongoing global security commitments since World War II, and China is emerging as a great regional power. Benjamin E. Goldsmith's 2004 article "Democracy, Interdependence, International Organizations, and Asian Security Debates" looked at the IT data in the case of China and the rest of Asia. He sought to assess, "the relevance of prominent 'Kantian' hypotheses for understanding the international politics of Asia" (Goldsmith 2004, 1). He focused on all three legs of the Kantian peace, and his level of analysis was on a regional

level. He concluded that there is a high degree of Economic Interdependence among Asian states and that two legs of the tripod, democracy and mutual membership in international organizations, decrease conflict. In his research, Interdependence does not have a significant impact on conflict in the region. When it came to dyadic relations with China, high Interdependence tended to increase conflict (Goldsmith 2004, 26).

Goldsmith also found that China has a tendency to have increased conflict with democracies. Goldsmith recognizes this last finding might reflect conflict solely tied to the Cold War. This suggests that his findings regarding China may be influenced by China's recent turbulent past and participation in the Cold War, which put it at conflict with democratic states and disrupted economic development. So while, Goldsmith failed to prove IT for Communist China, he recognized that his data were more indicative of the influence of existing conflict rather for potential conflict.

In the long run, IT might explain why the US-China conflict has not progressed to open warfare since the 1950s. On the other hand, if Interdependence does indeed influence conflict, the dyad in question may not prove the case, because there are many other variables. This is not predictive, but rather explicative of the risk of using aggregate data for a specific case. Of all of IT's attributes, it does not explain why conflict increased during the period of increased Sino-American Interdependence. The data itself support some aspects of the IT, but remain inconclusive. The one clear trend from the period of little trade is that fewer conflicts rose to the level of open warfare, which tends to support the IT concept that conflict between states will continue but remain at lower levels, since states are motivated to continue beneficial trade.

Test 3: The Impact of new Interdependence Subvariants on the Sino-US case

As Interdependence Theory has matured, subvariants have arisen to challenge the original thesis. This has come about as new, more exacting methods have been developed, missing data (particularly on communist states) has been found and new researchers have successfully challenged existing ideas about the nature of Interdependence. Oneal and Russett have participated in this evolution of IT, and many others have joined the effort. In this test, we are particularly concerned with the recent (2003 and forthcoming in 2006) research of Christopher Gelpi and Joseph Grieco (GG), who posit that polity type determines the level of impact dyadic Interdependence will have on the initiation of conflict. As in Tests 2 and 4, we seek to address the research question: How does IT explain the nature of the relationship between the US and China?

GG are concerned with both the utility of IT and its place within the Kantian tripod. They register an important interaction between two legs (Democratic Peace Theory and Economic Interdependence) of the tripod. Gelpi and Grieco work on the premise that the democracy and trade aspects of the Kantian tripod are contingent upon each other. Their measure of this interaction shows that increased trade between a democracy and an autocracy has little or no constraint on dyadic conflict. In their work they parse out the divergent findings from OR's pro-IT thesis (trade reduces conflict) and Barbieri's realist thesis (trade increases conflict). In the process, they attempt to demonstrate how both can be true in different cases of polity and Interdependence.

GG's start with the notion that democratic leaders are beholden to large constituents or selectorates that represent a large part of the population and that their best

bet for staying in power is to provide economic success, which is, in turn, promoted by free trade (2003, 47). Autocrats are in general answerable only to small selectorates, and their strategy for maintaining a satisfied selectorate may have very little to do with economic advancement or free trade. So as noted in Chapter 2, GG's basic notion of IT differs from OR's in that they hold that Interdependence reduces conflict under certain conditions of polity, while OR hold that IT holds in all cases. From this basis, GG work to take IT in a new direction.

Gelpi and Grieco modify OR's work using two methods. First, in their 2003 article, they modified both OR's and Barbieri's data and methods by interjecting an interaction variable for democracy and trade (2003, 50-54). They found that Barbieri's idea held true only in autocratic dyads; in other words, increasing trade between autocracies does marginally increase conflict. They also found proof for Oneal and Russett's hypothesis, at least in the cases of democratic-to-democratic trade and democratic-to-autocratic trade. In a democratic-democratic dyad, GG found that increasing trade from a base of 0 to .9 percent of GDP of the less dependent state decreased the potential for a MID by 67 percent. In a democratic-autocratic dyad, a similar increase in trade reduced the potential for conflict by a scant 12 percent. In the case of an autocratic-autocratic dyad, increasing trade from 0 to .9 percent nearly doubled the chance of conflict (2003, 53-54). In contrast, our look in Test 2 at OR's results on US-China Interdependence pointed to a 27 percent decrease in the risk of conflict due to the less dependent state's, the US, level of dependency at 1.2 percent of the United State's GDP.

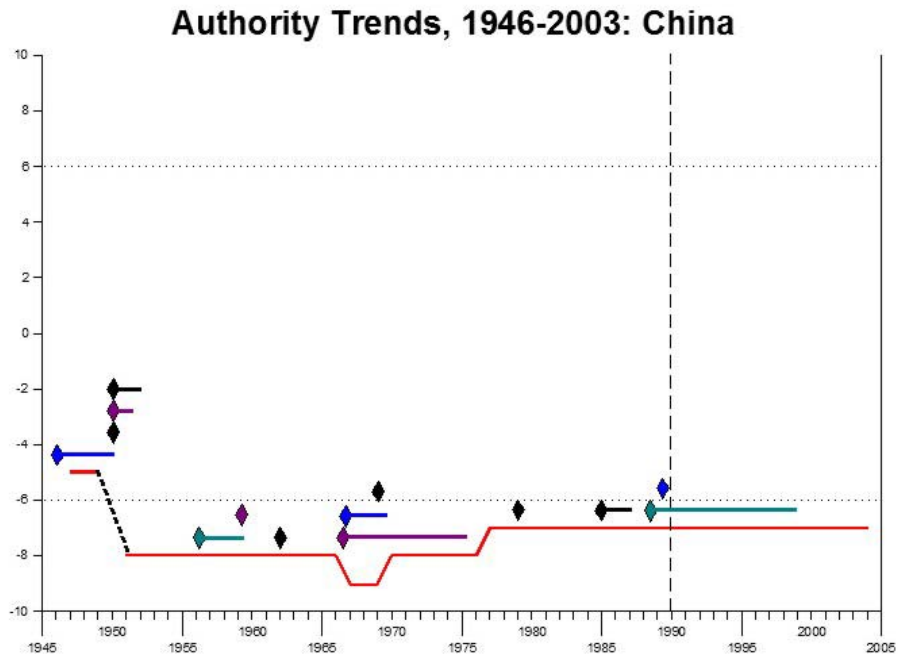
Second, their 2006 article tackles one of the major shortcomings in OR's methodology, the lack of directionality for initiation of conflict. OR found that statistically significant values were provided only by the less trade dependent of the two states in the dyad. OR's "weak link" concept assumes that it is the less dependent state that initiates conflict. GG pointed out that we are aware which state initiated most conflicts in the modern era, and the Correlates of War project, OR's choice for conflict data, maintains such a database. GG further realized that information about the known initiator of conflict could correlate to either trade or polity variables. So, their 2006 study looked at 40,100 dyad-year observations from 1950 to 1992 and identified one state as the challenger (or conflict initiator) and one state as the target of the conflict. They present the hypothesis: "Increases in a state's trade dependence on another country *will reduce* the likelihood that the state will initiate militarized conflicts against its trading partner, *to the extent that the state is democratic*" (2006, 5).

In both studies, GG conclude that democracies are less likely to go to war with each other even when there is no trade, while increased trade provides an additional constraint on conflict (2003, 54-55; 2006, 18). As in the previous study, in 2006 GG found that "the effects of trade are contingent on the presence of democratic political institutions" (2006, 18). However, the later study found "that increasing levels of trade dependence do not constrain autocratic challengers from initiating militarized disputes" (2006, 20).

GG used their dispute initiator formula together with OR's and Barbieri's data and methods in a case where challenger trade dependence moved from zero to five percent of GDP, which is four times the level of dependence of the US in 2002 (2005, 35).

With OR's data, GG found that when the challenger is democratic the risk of conflict falls 22 percent, while the risk *rises* 4 percent if the challenger is autocratic. The figures for Barbieri were 24 percent and 9 percent, respectively. Furthermore, autocratic states are already more disposed to initiate conflict than democratic states.

Relevance of Gelpi and Grieco to the US-China relationship. Since GG balance their recent works on the polity level for members of the dyad, we need to take a look at the most recent Polity database, Polity IV (Marshall and Jaggers 2003). The "2003 Polity IV Country Report for China" provides a snapshot of the current and recent assessments of its polity score. For China, we see that the score is an autocratic -7, on a scale from -10 to 10 with -10 being the most autocratic and 10 being the most democratic polity; see figures 5.4 and 5.5. (The US score is 10, indicating it has the highest score possible on democratic indicators. It has remained unchanged for the period of this study, 1978 to the present.) China's score has remained at -7 throughout the time of the Deng reforms, which is a slight improvement from its score of -9 during the Cultural Revolution of the 1960s and the transition from Mao to Deng in the 1970s.



Legend

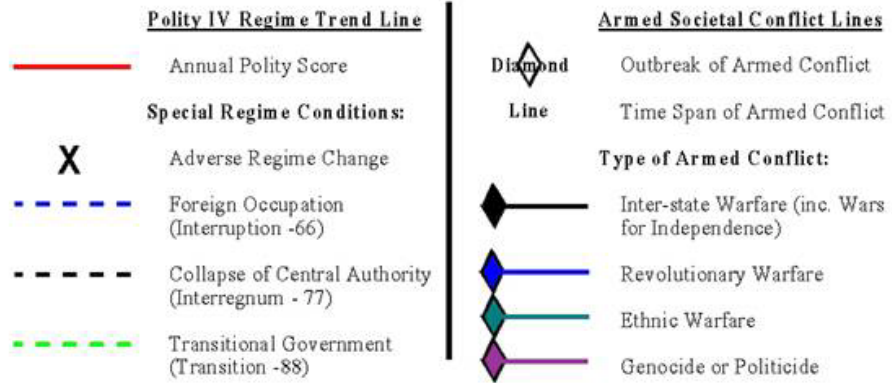


Fig. 5.4. Polity IV China Trend Data (Source: Marshall and Jagers 2003)

Score: 2002 2003 Change					
Polity: -7 -7 0					
Democ: 0 0 0					
Autoc: 7 7 0					
Durable: 54					
Tentative: No					
SCORE	CHN	CCODE	710	Date of Report	03/04/04
Polity IV Component Variables					
XRREG	XRCOMP	XROPEN	XCONST	PARREG	PARCOMP
2	1	4	3	4	1
Date of Most Recent Polity Transition (3 or more point change)					
End Date				Begin Date	
Polity Fragmentation: No					
Constitution	1982				
Executive(s)	Secretary General and President Hu Jintao (CCP); elected by National People's Congress 15 March 2003				
Legislature	Unicameral: National People's Congress (2,979 seats; no competitive elections, recruitment through designation within the CCP; 36 deputies are elected in Hong Kong)				
Judiciary	Supreme People's Court				

Fig. 5.5. Polity IV country report 2003: China (Source: Marshall and Jagers, 2003)

How would GG view the China-US dyad? In their 2003 study, they would find that Interdependence would have a minor impact. We have already indicated that trade in 2002 was 1.2 percent of the GDP of the United States, the less dependent state.

According to Gelpi and Grieco, the present level of trade between a democratic United States and an autocratic China reduces the potential for conflict for any given year by 12 percent or more. In their 2006 study, the autocratic nature of China's government would effectively prevent any conflict suppressing impact of Interdependence. In both cases,

the high level of Sino-American Interdependence would have little or no conflict-suppressing effect.

While GG posit a startling concept when it comes to IT and autocracies like China, there is some reason for caution. The first comes from the researchers themselves, who are well aware that their work represents a new slant on IT. As such, they expect counters to their research, and additional tests of their hypothesis will find either fault with or confirmation of their work (as relayed to this researcher in a telephone conversation with Dr. Joseph Grieco on October 13, 2005). Certainly, Oneal and Russett have crafted numerous variations of their studies, creating both a model for additional studies that build upon their ideas and a target for others who have questioned Interdependence Theory.

Second, GG also realize that there are autocratic states which elect to use a trade strategy in order to satisfy their selectorates and maintain themselves in office. GG posit that such states, “will be constrained by trade from initiating military disputes with their trading partners” (2006, 25). This would suggest that China might be exempted from GG’s findings on the nature of trading autocratic states, particularly if one considers how dependent China remains on trade with the United States. On the other hand, GG take a step away from this proposition by noting that autocracies with a trade strategy, “are *choosing* to be constrained by trade, and thus they could choose to alter their strategies for retaining office if necessary” (2006, 25). GG do not explain how such a state would move effectively from one strategy to another without risking the ire of its selectorates, nor do they address the pitfalls of other strategies for autocrats, such as appeals to nationalism. Furthermore, GG’s foundational notions on why democracies are different

than autocracies do not ring true in the case of China. In their 2003 work, GG note that “the need for public policy success gives democratic leaders a greater incentive than autocrats to promote aggregate economic growth” (2003, 49). But for China’s leaders, economic growth is the primary means (other than appeals to nationalism) for continued legitimacy, both to the selectorate and the general population. Certainly in comparison to democracies, Beijing is more able to use force to maintain control, but democracies have other claims (stemming from democratic political institutions) to legitimacy.

Papayoanou and Kastner examined the selectorates involved in the China case. They found that in the wake of the Deng reforms a wider range of actors make up the selectorate (1998, 15). This diversity of actors came about in part due to the power diffusion strategy by which the Deng reforms were enacted. Decentralization of fiscal and other authorities brought in local leaders into the pro-reform camp. The expanding nature of the economic reforms has also consistently increased the size of the selectorate. Early reforms pitted coastal provincial leaders, which were the first to benefit from special economic zones, against leaders of interior provinces. Now, however, interior provinces are also embracing the new economic model and are attracting FDI. There are, of course, losers in this strategy, and they have good reason to oppose the ongoing changes. State-owned enterprises are among the most important such players (Papayoanou and Kastner 1998, 16-17). Such status quo players are both powerful and disenfranchised by China’s trade strategy. Despite these domestic obstacles, Papayoanou and Kastner found that on balance, “top Chinese policy makers will not pursue an aggressive and conflictual foreign policy that could put China’s international economic ties at risk. Doing so would undermine their support within the selectorate” (1998, 18).

History, of course, reminds us that events are determined by forces outside the control of policy-makers. Papayoanou and Kastner suppose that conflictual forces will be tamped down only as long as economic growth continues. OR suppose that polity is not a significant determinant of conflict, while GG suppose that the lack of democracy decreases or eliminates the impact of Interdependence on conflict. In Chapter 2, we reviewed the work of Mansfield and Snyder, who were concerned with the increased potential for violence from states that experience incomplete transition to democracy. Their evidence showed that the potential for conflict in a dyad increases by about 50 percent if one member of the dyad experiences an incomplete transition to democracy. Mansfield and Snyder started with the same composite Polity profile as OR, but they also considered three of the Component Variables from the Polity data. They were concerned not with democratic transitions so much as the failure to complete democratic transitions and the potential for conflict presented by such regimes.

A review of the year-to-year data in the Polity database shows that there has been no change in either the overall Polity score or the three component variables Mansfield and Snyder consider. For OR, this is not significant, since they do not believe that such transitions are inherently conflicting-provoking. For Mansfield and Snyder, this indicates that during the period 1978 to 2003, we have not seen a regime transition and thus should not expect to have seen the increased potential associated with an incomplete transition to democracy. Mansfield and Snyder do not speak to China's case, but China is the very symbol of pregnant democratic potential, and both of the theorists (OR and GG) we have considered regarded democracy as a key component in reducing conflict. OR consider it to be a powerful but largely independent factor from IT, while GG consider it to be

inherent to the success of Interdependence. Mansfield and Snyder's controversial research suggest that whether or not one believes in the potential for IT to reduce conflict, the progress to another leg of the Kantian tripod (democracy) will itself lead to a higher risk of conflict.

We do not have a method to measure the intent of autocracies who value trade as a way of satisfying their selectorate. As noted above, GG cut the matter both ways. GG's methods also do not address the potential for conflict posed by a failed Chinese move to democracy as envisioned by Mansfield and Snyder. At the very least, Grieco and Gelpi's work suggests that OR overstate the conflict-reducing influence of Sino-US Interdependence. Should GG's hypothesis prove true, the fact that China is not democratic diminishes or even eliminates the conflict reducing impact of Interdependence. GG attempt to correct what they see as OR's failure to identify the directionality of conflict initiation or who started the conflict. Again, OR report that in non-directed dyadic conflicts, they found evidence of the impact of Interdependence only in the less constrained state. Yet, Oneal reported in a January 23, 2006 telephone conversation with this researcher that his work on directed dyads indicates that both the target and initiator are probably influenced by Interdependence. If China is the most important case in question, then GG's fine ideas are left unfinished. Unfortunately, the tentativeness of GG's concepts suggests we should continue to seek our answer elsewhere until their ideas have been fully vetted by academia. China's lack of democratic institutions is clearly a concern for US policy-makers, but there are many other considerations, including conflict over the status of Taiwan and creeping Chinese hypernationalism, that will also drive the potential for conflict with China. Some of these

concerns will be addressed in the next section wherein we examine two case studies that involve conflicting US and Chinese interests.

Test 4: Sino-US Relations in Practice

An examination of two dyadic events constitutes the fourth and last of our tests of Interdependence Theory. Through an examination of two events (China's entry into the World Trade Organization WTO and the 1995-1996 Taiwan Strait Crisis), we compare IT and realism in their utility for explaining US and Chinese actions. We select realism as a comparison point for two reasons. One, realism has long been one of the dominant theories of international relations in the United States. Two, IT is a component of liberalism, which has long been contending with realism for dominance in US foreign policy. We also examine our own findings against constructivism, an emerging theory that bridges both liberalism and realism. The purpose of this investigation is to discern how and how well IT can be used as a tool for explaining and predicting the behavior of states. Our test begins with the WTO case, moves onto the Taiwan Strait case, considers our findings against constructivism, and analyzes IT's utility as an international relations theory.

As we noted in Chapter 3, Robert Yin of COSMOS Corp. holds that case studies are useful as, "an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident" (Yin 1994, 13). In our research we are concerned with an international relations theory in the context of the current and near-term Sino-American

relationship. Our selection of dyadic cases was driven by the need to examine the two most important variables in our research question, Economic Interdependence and conflict. Our first dyadic event, China's entry in the WTO, was the result of internal Chinese decisions to move into the world market and the US's response to this initiative. The WTO will have enormous impact on the economies of both countries. IT proponents would hold that these moves are the strongest indicators that Beijing and Washington place economic cooperation over confrontation. The Taiwan Strait Crisis (TSC) focuses on the one issue -- the status of Taiwan -- which most divides the US and China and would most likely lead to conflict, as it has in the past. The TSC shows that traditional concerns of state security, power and control drive events and possess leaders in Beijing and Washington. The TSC is also the most serious dyadic Militarized Interstate Dispute in the Correlates of War database during the period of this research.

The most important events in international politics are explained by differences in the capabilities of states, not by economic forces operating across states or transcending them. (Kenneth Waltz in *The National Interest*)

The Realist Perspective. The many variants of realism make up what is one of the dominant international relations theories, particularly in the United States. Its major competitor through the years has been liberalism, of which Interdependence Theory is a component. Realism is a not a new concept; it traces its origins to Thucydides and Machiavelli. In the modern era, Hans Morgenthau was arguably the most prominent American proponent of the theory. He argued that "We assume that statesmen think and

act in terms of interest defined as power, and the evidence of history bears that assumption out. That assumption allows us to retrace and anticipate, as it were, the steps a statesman-past, present, or future-has taken or will take on the political scene” (Morgenthau 1994, 35). Realism, in its essence, is concerned with the distribution of power within the international system. While critiques argue that the realist perspective is too simplistic, modern realists or neo-realists, such as Kenneth Waltz, have thought through some of the theory’s early failings. The tenets of the most prominent strain of realism theory, neo-realism, are presented below.

Barry Hughes of the University of Denver sees modern realism as consisting of five basic ideas: the state, state’s interest, power, anarchy and security dilemmas (Hughes, 1997, 46-47). In realism, the state is seen as the primary actor in the state system. For the most part, realists see the state as a unitary, rational actor and do not give much credence to internal machinations or ideological or identity issues. Other players are involved in events, but they occupy a lesser status. Each state pursues its own interests, which usually involve security, autonomy of action and power. Power is the means by which states communicate and pursue their interests. Military power is the essential source of power, but most realists acknowledge economic and other sources of influence also constitute a state’s source of power. Power is finite in the system, so machinations to change the power balance constitute a zero-sum game. The international system is one of anarchy. This is not to suggest a state of chaos, but rather realists see the lack of a higher or central authority (or power) as the reason why states must pursue their own interests. This leads to the last of the concepts Hughes identifies. Anarchy in the system requires states to protect themselves, but the very act of developing capabilities to protect

one's state may lead another state to perceive that it is being threatened by the first state. This may lead to an escalation of measures to improve security, which creates a security dilemma.

Security dilemmas led states to optimize their security through power advantages relative to other states, which in turn has created the modern era's regional and global power structures. States also work in parallel (usually in the form of alliances) to balance the power of a larger power or competing bloc. In the Cold War, this led to a bipolar global power structure, representing both competition (between blocs) and cooperation (within blocs) in the world's security environment. Realists generally describe the world power structure as unipolar, with the United States as the current superpower. Some realists would also describe the US as the world's hegemon, having the power (through the use of force or merely the implied threat of use of force) to dictate the terms of relations between states. Realists have applied their theory to the US-Sino case and provide explanations for behavior within the dyad based upon realist principles. The US and China case also provide fertile ground for theorists, such as Robert Gilpin in *War and Change in World Politics* (1981), who hold there is a pattern of behavior between status quo hegemons, such as the United States, and rising hegemons, such as China. Lastly, as noted in Chapter 2, some realists view trade as a source of conflict rather than as a constraint on conflict. This can be explained in part, because realists see power exchanges between states as having zero-sum gains.

Trade with China is not only good economic policy; it is good human rights policy and good national security policy. (Former Secretary of State Colin Powell, 1 June 2001)

Once China becomes strong enough to stand alone, it might discard us. A little later it might even turn against us, if its perception of its interests requires it. (Former Secretary of State Henry Kissinger, *White House Years*)

Background on China's Entry into the WTO. China formally became a member of the World Trade Organization in December 2001, after a 15 year process of accession (Gertler 2004, 21). China's entry process was the most tortured of any state. This process was difficult for several reasons: many states imposed sanctions against Beijing following the Tiananmen Square Massacre; the digestion of the post-communist Soviet Bloc states slowed down the work of the WTO itself; domestic opposition retarded Beijing's efforts to move forward; many states opposed China's entry as a developing state due to its rapid economic expansion; and lastly, China's accession as a potential world economic power is a huge development, so negotiators worked hard to ensure China came in only after stringent investigation (Lardy 2002, 63-65).

Numerous states and IGOs were involved in this process, since most players recognized that China's entry into the WTO would have global impact. The issues that needed to be addressed were both many and complex. The World Bank identified five principles of WTO accession: "nondiscrimination, market opening, transparency and predictability, undistorted trade and preferential treatment for developing countries"

(Gertler 2004, 25). In order to gain entry, China had to conclude bilateral agreements with 44 member nations. Among the most challenging of these was with the United States, whose Congress did not approve such a step until September 2000 (Gertler 2004, 22-23). In addition to multilateral negotiations, China agreed to a series of unprecedented measures regarding pricing, anti-dumping, intellectual property rights, several technical regimes for specific economic sectors, and a unique, “transition review mechanism” to ensure compliance (Gertler 2004, 23).

China’s long journey actually began long before 1986. Deng’s reforms were the precedents that lead to application in the WTO. Still even in the light of such previous bold decisions, the WTO move seems at first look to be a very riskier policy for an autocracy bent on maintaining internal control. In *Integrating China into the Global Economy*, Nicholas Lardy of the Brookings Institution tries to tackle these questions by arguing that China entered the WTO with a firm grasp of its implications for China’s economy and a strong commitment to meet its obligations under the treaty. Lardy observed that China’s WTO entry is a sincere effort at integration, because it had long ago, under its own hand, began the process of reforming its trade practices. Why has China crafted this strategy and undertaken such risk? Lardy observed in response that in China, “economic growth is the sine qua non for retaining political control” and market reform was the best method for ensuring such growth (2002, 11). Indeed, Lardy posits that the Chinese were motivated in large part by their faith in the market system, and that acceding to the WTO would put more competitive pressure on their own industries, particularly the lethargic SOEs. Moreover, he asserts that the Chinese deem globalization as an unavoidable process and see the WTO as the best avenue to take advantage of the

situation. Lardy suggests that the Chinese leadership is well aware of the potential social disruption (job loss, company closures, etc.), but that in their calculus the benefits will outweigh the threat to social order and their status.

Lardy also explains that China is taking this path in part, because much of the expected disruption from entering the WTO is simply overstated. In other words, the cost and risk is less than outside observers normally assess. China has advanced so much since the mid-1990s that the figures have yet to catch up with reality. One example of this change is found in the textile industry, which had both state and private firms. In 1991 it had 7.6 million workers, but ended up in the red for the first time. In order to return to profitability, some state firms were closed, the industry was recapitalized, and 2.7 million workers were laid off (Lardy 2002, 23).

Before 1978 and the Deng reforms, China's planned economy relied upon a physical planning system for foreign trade. China's barriers to trade were many. Tariffs were at a high rate of 56 percent in 1982 but had fallen to 15 percent by 2001, equivalent to Brazil and Mexico (Lardy 2002, 33). At the same time due to exemptions, the actual rate of tariff collection had fallen to 3 percent, which was the lowest rate of any developing nation (Lardy 2002, 35-37). Nontariff barriers to imports were probably a greater concern for foreign governments, but here again the news has been continued progress. An example is licensing restrictions which hit a peak of 46 percent of all imports in 1986 but fell to 8.5 percent in 2000 (Lardy 2002, 39). China has also removed many of the restrictions on its private firms in order to promote exports. The number of licensed trading companies was allowed to grow almost unfettered and access to foreign currency was increased, in large part by allowing firms to keep their foreign currency.

Chinese firms responded in true market fashion, by increasing their investments and seeking greater exports, taking advantage of China's comparative advantage in labor costs. As previously noted, many states, including the US, took advantage of these reforms to build factories using cheap Chinese labor, to invest in Chinese enterprises, and to start selling to the growing Chinese domestic market.

But Chinese economic reform and subsequent trade and economic expansion presented both opportunities and challenges for US policy-makers. While those who sought engagement were generally favored in the 1980s, several events were to make that dominance less secure. These reasons included the end of the Soviet Union as America's only superpower rival, the perception that economic engagement might empower an autocratic China to behave more aggressively, and China's own internal and external use of force. On this last point, the battle over trade policy with China became more explosive following the Tiananmen Square Massacre of 1989. The US and other Western states imposed sanctions on China following the suppression, and WTO negotiations were essentially put on hold for several months (Lardy 2002, 63). In his 1992 campaign for the presidency, Bill Clinton differentiated himself from the incumbent George H.W. Bush by calling for conditions on the annual renewal of Most Favored Nation status (MFN) tariff treatment for China. The Jackson-Vanik Amendment requires the president to provide a waiver for communist states in order to maintain MFN status. Loss of MFN would entail heavy duties on China's exports to the United States. Furthermore, gaining permanent normal trade status was a prerequisite for signing a WTO bilateral agreement, so progress on the WTO bilateral agreement was directly tied to the yearly MFN battle. Once in office, President Clinton's staff drafted an executive order that placed conditions

(improvement of human rights behavior) on the waiver for 1993. The May 1993 executive order did not address other touchy issues, such as weapons proliferation or trade disputes.

President Clinton's modest attempt to wring human rights concessions from China came at a time when American businesses, some of which had been resistant to get involved in a large but uncertain economy, believed that Deng's reforms marked the true opening of the Chinese market. The executive order from President Clinton galvanized the business community into action in support of unconditional MFN for China. Hughes Aircraft, AT&T, and Boeing Corporation led the effort to pressure the Clinton administration to back off from its new policy. Hughes made public and private appeals that the MFN conditions would cost it one billion dollars in business, 4, 000 to 5, 000 jobs, and potentially the entire market as other nations filled the gap (Sutter 1998, 49). Boeing made similar public and private pleas. These arguments were particularly potent with the Clinton administration, since putting the economy back on track was a priority of its campaign. In a broader sense, the Clinton Administration was being targeted by a coalition of mostly business interests. Uniting under an umbrella organization calling itself the Business Coalition for U.S.-China Trade, the pro-WTO interests believed dissuading the new president from implementing his campaign promises on China as their best bet in maintaining MFN and access to China. In time, more than 800 different corporations and other organizations united in this effort. In many ways, the fight to keep MFN for China was part of a long-term effort to maintain access to all foreign markets. One of the key players in the effort against MFN conditions was a trade association called the Emergency Committee for American Trade or ECAT. Formed in 1967, ECAT

had decades of experience in battles over trade. This experience gave the pro-MFN coalition an advantage over the opposition, which although experienced as lobbyists where less so when it came to the specific issue of influencing trade policy.

Opposing the business lobby, was a coalition of human rights activists, Taiwanese and Tibet nationalists, unions, protectionist industries, and conservatives opposed to China on ideological grounds. Their ability to influence the decision-making process was hampered in part by the situation in China itself. The events of Tiananmen Square had seen a great increase in negative public perceptions toward China, and this aided the anti-trade forces. However, as that event faded from view, the potency and unity of the coalition also waned. The variety of interests in the anti-MFN coalition resulted in a considerable variance in policies and loyalties to the movement. For example, the AFL-CIO under Lane Kirkland at one time supported an end to MFN status for China, but the organization's stance softened when they realized the impact on union jobs of Chinese counter sanctions (Rourke and Clark 1998, 201-24). Some groups such as Amnesty International and the US Catholic Conference were key players on Chinese human rights issues but held no position on MFN.

The pro-MFN forces gained the upper hand over the divided opposition, and soon their influence was felt in both Congress and the executive branch. In May 1994, President Clinton announced that he would renew China's MFN status and that he was lifting conditionality, essentially de-linking MFN from the human rights issue. The House, which had voted repeatedly since Tiananmen Square to condition MFN status, voted 280 to 152 that year to extend unconditional MFN status to China (Sutter 1998, 51). In essence, the pro-trade forces had successfully rolled back President Clinton's new

policy and put the anti-trade forces into a reactive mode. MFN status was granted without conditions for the next few years, but the issue was reengaged over fights for Chinese entry into the World Trade Organization. In 1995, China began a charm offensive to convince the US that its reforms would roll back tariffs even before accession into the WTO. In April 1999, Washington and Beijing reached initial agreement on the terms of China's entry into the WTO (Lardy 2002, 64). The Chinese suspended talks with the US following the May 1999 bombing of China's embassy in Belgrade, but negotiations were restarted in September, and a final agreement was reached in November 1999. In the midst of the Clinton's administration's attempts to sell the agreement to Congress, Beijing made a series of belligerent statements intended to influence the upcoming Taiwanese Presidential elections. In February 2000, China published a white paper reiterating Beijing's intent to use force in the Taiwan case and in March Premier Zhu delivered a speech in which he expressed the willingness to shed blood to prevent Taiwan from declaring independence (Gartzke and Li 2003c, 9). In 2000 after years of lobbying by pro-Chinese trade forces (now actively joined by the Clinton administration), the House and Senate approved permanent normal trade relations with China. China officially entered the WTO in December 2001, providing victories both to those forces who sought profit in trading with China and those who sought to draw China into global norms and institutions.

The US and other concerned states had delayed China's entry into the WTO and in the process won major concessions from Beijing. China was essentially forced to accept the WTO terms and agreed to, "eliminate all quotas, licenses, tendering requirements, and other nontariff barriers" by 2005 (Lardy 2002, 65). In order to allow

China in as a developing country, the US demanded special provisions (Gertler 2004, 23-24). In services, manufacturing, and distributing, China opened its the doors, while the agricultural sector was forced to compete without protection in the international marketplace. The terms for China under “rules-based” issues, those protocols under which it conducts trade, are considerably stricter than those of other recent entrants. Because of a China-specific clause, China has a harder time using WTO mechanisms against importing states, while other states have stronger tools to retaliate against China. In another rules-based issue, anti-dumping, China is disadvantaged because other states can use nonmarket-based tools to quantify dumping by China (Lardy 2002, 57-79; 86-89; 133).

An IMF working paper found that in the short- and medium-term China and most of its trading partners, particularly the more advanced Asian economies, will benefit from China’s accession (Rumbaugh and Blancher 2004, 12-14). Projections suggest that China’s economy will add about one percent more growth a year; even the USA will see increased economic performance due to China’s entry. Other factors may be less clear. China already takes a huge portion of the world’s FDI, and that number is expected to reach 61 percent of the world’s total (Lardy 2002, 135). And while Lardy sees China’s past performance as favoring compliance, the future is less clear, especially considering recent political changes. Lastly, China as a member of the WTO will clearly behave differently than when it was aspiring to membership.

Of course, Lardy’s upbeat assessment does not tell the full story. Gordon Chang provides the contrarian view of the impact of China’s joining the WTO. He believes entry into the WTO will cause the collapse of the SOEs, which will most likely be the

trigger for the collapse of the CCP itself (G. Chang 2001, 187). Chang believes that Beijing is not taking steps to prepare its society and economy for the coming chaos that are being visited upon its shores by the WTO (G. Chang 2001, 67). This assertion does not jive with the substantial evidence that Lardy provides that China is preparing for the WTO in several ways: to meet its obligations to the international community, to preserve its nascent and most critical industries, and to reduce the potential of social unrest due to the WTO. Clearly, some of the objectives are contradictory or not in the spirit of the WTO, yet Beijing, out of self-interest, has been seized with the matter. Chang pooh-poohs the notion that China will be able to inoculate certain industries (as we have seen in Japan and South Korea). So far, Chang's vision of the impact of the WTO accession on Chinese politics has not played out. We do know that the impact of WTO accession on Sino-US dyadic trade may be very high. From 2000 to 2003, Chinese exports to the US increased from \$100 billion to \$152 billion, while exports from the US rose from \$15 billion to \$27 billion (Hufbauer and Wong 2004, 3).

So far, China's compliance record under WTO itself is mixed. Lardy's optimistic forecasts are supported in a recent IMF paper that found, "The tariff reductions planned by China in the context of its WTO accession are the continuation of a longstanding trend. This trend is reflected in the decreasing level and dispersion of tariffs and the continued reduction in NTBs [nontariff barriers]" (Rumbaugh and Blancher 2004, 7). Indeed, Gill and Tay of the Center for Strategic and International Studies report that China's first year results in WTO were "generally positive" (Gill and Tay 2004, 21). But in the following year, Gill and Tay found that "China lost momentum in fulfilling its WTO commitments," citing ongoing problems with intellectual property rights, discriminatory

taxes, lack of movement on opening service and agricultural markets and maintaining market access (2004, 22). It is too early to determine whether China's WTO gamble will pay off in the ways it had planned, and the wisdom of America's cautious response also will not be evident for years to come.

The Interdependence Theorist's View of the WTO Case. Now that we have the background to this case we can ask ourselves: How does IT explain the behavior of the US and China in this situation? Interpreting Beijing's motives for its behavior can be a challenge, since its policymaking process remains somewhat mysterious, although less so than in times past. Consequently, it is difficult to attribute particular motives to China's rulers. This much we do know: China has essentially abandoned its adherence to the economic elements of Marxist-Leninism-Maoism. As noted above Lardy believes that Deng recognized the inevitability of globalization and the power of market mechanism to motivate actors in the economy. Deng and company accepted the *cat philosophy* to economic development; it does not matter if the cat is black or white, as long as it catches mice. In other words, the goal is economic growth, no matter what the means. While Beijing has not embraced the full measure of liberalism, they have undertaken a pragmatic approach that explicitly rejects Marxist-Leninism-Maoism. Some aspects of the Kantian tripod are acceptable to China, which is evidenced by the fact that Beijing has also joined many IGOs since the Deng era. On the other hand, democracy and, indeed any form of power-sharing, are not on Beijing's agenda.

The power of Interdependence is its purported ability to tamp down conflict with other states. To Beijing that quality of IT might be meaningless; it might seek trade merely as an avenue of increasing market forces and improving efficiency. Speaking to

our argument, we note that Beijing is aware of some of the power of Interdependence, since part of its strategy of opening to Taiwan was to intertwine their economies and discourage Taipei from seeking independence (see the Taiwan Strait Crisis below). The Interdependence theorist would not be concerned about Beijing's motivations or understanding of IT, since dyadic Interdependence will have its impact whether or not the actors anticipate or understand it. In this case, we have reported that OR measured US-China Interdependence in the 90th percentile of trading states, which they hold represents a 27 percent decrease in the potential for conflict if the two states still had almost no trade.

In contrast, the United States' appreciation of the utility of engaging China economically is much easier to understand. The US has appreciated most aspects of Kantian thought since its foundation. While China policy has not always been consistent with Kantian ideas, the IT proponent would point to the WTO case as an example of where IT ideas, in the form of economic engagement, won out over other contenders. Indeed, the US's policy of economic engagement has transcended political boundaries, having been supported by both Republican and Democratic presidents. In one sense, the WTO case is just another example in which the US supported free trade because of its long-held belief in market forces. States trade because the activity brings mutual benefit to both players. For the US, the internal mechanism for IT in the WTO case is quite evident. Liberal ideas rest upon the notion that a nation's external behavior is determined by its internal organization; i.e., free societies are generally more likely to have good relations with other free societies. This is because actors in society restrain democracies from pursuing aggressive policies against other free societies. This belief led to such notions as the Marshall Plan, NAFTA and now the WTO. In this specific case, US policy

makers are fully aware of both China's rising military power and the potential for dyadic trade to deter the use of such powers.

GG would be less sanguine than those who support an engagement policy with China. GG would state that the WTO may create economic benefits for both states, but the increased trade that the WTO might produce will probably have little or no effect on the potential for conflict. Again, GG do not address how China's non-democratic, but thoroughly trade-dependent, autocrats would deal with a significant reduction in trade with the US. How would the trade-hungry selectorate within China deal with such a change in policy? Despite the credible warning GG provide, we simply cannot discern whether or not their extension of Interdependence Theory is in play in this case.

IT critics would ask if the US is so convinced that IT works, why did it take the US so long to agree to allow China's entry into the WTO? The liberal response would be that the effort took so long, because autocratic China had to have its feet held to the fire in order to conform to liberal standards. After all, autocrats cheat, and market forces only work if the market is open. They would note that the liberal EU also did not conclude an agreement with Beijing until 2000. Realists would argue that IT does not fully address the issue of power or capabilities of the states in this circumstance. Furthermore, Interdependence Theory's utility is also constrained by the fact that it only considers the constraints on the least dependent states, which is the US in this case.

The Realist's View of the WTO Case. A realist would see the battle over China and the WTO as just another in a series of power struggles between two states. Realists are not concerned with selectorates, ideologies or other domestic matters. As unitary actors, *states* seek increased *power* to pursue their *interests* (security, freedom of

action) in an *anarchic international system*. The WTO case is like any other opportunity for states to test their freedom of action, increase their power and improve their security. A realist would discount ideology as a player in his estimation of China's actions. For China, accession to the WTO dovetailed nicely with its Four Modernizations strategy of building its economic base before improving its military. In this case, China saw an opportunity to improve one form of power, economic, while contributing to the longer-term development of its military might. In the Chinese valuation of relative power, increased market access equated with an overall improvement in relative strength. Some realists would argue that such power would allow China greater freedom of movement and greater potential to balance the US in pursuit of security. Of course, in the process China *lost* some autonomy of action by allowing market forces to control China's command economy.

Realists would suggest that the United States also conformed to realism's expectations. For fifteen years, Washington worked to keep China out of the WTO and sought to create terms that were the most favorable to US interests. While the US did not increase power for itself, it did the next best thing by denying it to a potential challenger state. In this sense denying easy market access was both an execution of freedom of action and a denial of power to a rival. The US balanced China's rising power in the form of limited, economic containment, which was the most the US could do, since the US cannot stop China's advancement short of war, but can mitigate China's rise. While liberals would suggest that engagement has ruled the roost, realists would point to this as a case when the US (and other states) sought a limited containment strategy.

As for the realist concept of *anarchy*, the WTO or any other IGO is made up of states which still have no hierarchical authority, so the individual states will use the IGO to press their own individual interests, although they might gang up on a hegemonic power as the need arises. *Security dilemma* does not specifically show up in this case, but certainly the US acted to slow China's WTO entry in the hopes of forestalling such a situation, since a China with fewer resources is less likely to provoke a security dilemma.

The realist view also has its flaws in this case. A realist would not consider the power of ideology in this case although the failure so far to achieve some of its nationalist objectives, clearly drives Beijing's behavior. Realism fails to explain the internal struggles that both the US and China experience in developing national security policy. Such machinations are prevalent in the US, and the rise of China has seen been accompanied by an increase in activity by actors who are interested in the status of China. Following the incident in Tiananmen Square, the collapse of the Soviet Union and the rise of Chinese economic strength, a group began to focus on China as the next strategic threat. The Blue Team, a collection of conservative, anti-Chinese and pro-Taiwanese groups consisting of think tank fellows, Taiwanese lobbyists, retired intelligence officers, journalists, a few academicians and members of Congress, began to become interested in influencing policy toward China (Kaiser 2000; Berry 2000). The Blue Team was originally funded by conservative activist Richard Mellon Scaife (Kaiser 2000; Berry 2000). (The Blue Team, not too generously calls its opponents—that is anyone who is not anti-Chinese—the Red Team. As such, there is no self-identified Red Team.) The Blue Team operates with a three part strategy. They seek to publicize the Chinese threat to the United States by requiring Defense and State departments to draft annual reports of

military and human rights reports. The findings are then supported and amplified by Blue Team journalists and analysts. A second effort seeks to strengthen American ties to Taiwan, the highpoint of which was the Taiwan Security Enhancement act of 1999, which committed the United States to a higher degree of support to the defense of Taiwan. Lastly, some Blue Teamers also worked to restrict trade relations with China by attempting to stop normal trade relations and membership in the World Trade Organization. The Blue Team has been less active since 9/11, because Chinese cooperation is seen as vital to the war on terrorism (Kaiser 2000; Berry 2000). Of course, critics of liberal theories might point out that the Blue Team's agenda reflects an interest group operating in a free society but advocating an *illiberal* philosophy in dealing with China. The liberal response is that liberal theory acknowledges that liberal states are generally more likely to have conflict with autocracies than they are with free states, so it is not unexpected that the Blue Team or other internal player would herald the idea of confronting an autocracy.

As a further illustration, we can see the weight of public opinion on policy. Before the Tiananmen Square Massacre, 72 percent of Americans viewed China favorably; after the incident, only 34 percent of Americans held China in good regard (J. Nathan 2001, 133). This poor impression of China remained roughly the same (33 percent favorable) in 1997 (J. Nathan 2001, 133). While the effect of such public opinion on decision-making is uncertain, knowledge of this sentiment is a powerful tool. In the 1992 election, both Bill Clinton and Patrick Buchanan successfully used President Bush's policy of moderate engagement toward China as a platform to challenge the incumbent president. Similarly, the human rights groups Amnesty International and Asia Watch

played upon awareness of such sentiments and used well-researched reports on abuses to influence American businesses in their policies toward China (Teles 1998, 52-57).

This policy is good for the United States, good for the PRC, Taiwan and the entire region. (Secretary of State Warren Christopher on the one-China policy, May 17, 1996)

The President and I have both said that we have a one-China policy...the truth is that the one-China policy I think is the one that is most reflective of what is appropriate for the international system. (Secretary of State Madeline Albright, September 8 1999)

Background to the Taiwan Strait Crisis. The 1995-1996 Taiwan Strait Crisis (TSC) represented the diverging regional political objectives between Taiwan and China, on the one hand, and the diverging regional and global interests between the US and China, on the other. The subtext of the crisis was the rapidly increasing Economic Interdependence between all three players in the lead up to the events. The TSC is an important event, because it was the most severe dispute during the period of this research. The Correlates of War database narrative of the Taiwan Strait Crisis 1995-6 MID is provided below (Ghosn et al 2004, dispute # 4064, 10-11).

This dispute consists of a series of incidents in which China seeks to intimidate Taiwan away from moves toward independence and Taiwanese and American responses to these actions. China deployed missiles opposite Taiwan, intercepted Taiwanese vessels, conducted military exercises, and conducted air and naval shows of force. In response, Taiwan repeatedly placed its forces on alert, deployed missiles, and scrambled jets. Beginning in 12/95, the US deployed naval forces to the area as a show of force in China. American naval forces were sent to the region again in March 1996.

In this crisis, the dispute began in July 1995 for Taiwan and China and ended five days after the March 23, 1996 Taiwanese elections. The US is noted as entering the MID in December 1995, when it conducted military operations in the Strait. The US's highest activity was a "show of force," while both Taiwan and China had higher levels of activity in the form of "fortifying borders." None of the participants rose to the level of using force, and there were no casualties (Jones et al 1996 and Ghosn et al 2004). See tables 5.5 and 5.6 to compare to other disputes.

One of the underlying causes of the TSC was Taiwan's movement from autocracy to democracy in the 1980s and 1990s (A. Nathan 1999b, ix). While the KMT had held unlimited power in Taiwan in earlier years and had maintained its claim to be the sole legitimate ruler of all of China, the onset of democracy spawned a strong independence movement. The push for independence challenged Beijing's claim to all of China and threatened one of its top national objectives, reunification. Another cause was the dynamics of internal Chinese politics following Deng's reforms, wherein the CCP relied

upon appeals to nationalism to maintain legitimacy (Friedman 1999, 244). This reliance upon nationalist appeals enhanced the hardliners, who saw the political opening to Taiwan as a betrayal of core Chinese interests. The more moderate figures were also constrained by the frailty of both Deng's health (he died in 1997) and the relative weakness of his successor, Jiang Zemin, who became president in 1993.

Since 1979, Beijing has proposed a "one-country, two-systems" solution, which would allow Taiwan to keep its political and economic systems but would empower only Beijing to conduct foreign and defense policies (Copper 1999, 58; Zhao 1999, 99-100). Due to the growing economic integration between Taiwan and the Mainland, Beijing considered the 1990s an opportune time to press with unification by peaceful means. The height of Sino-Taiwanese rapprochement probably occurred in April 1993 when informal talks were held in Singapore (Goldstein 1999, 197). In January 1995, President Jiang proffered an eight-point plan for reunification (Ji 1999, 78). Taiwanese President Lee Teng-hui responded with his own six-point proposal which was lukewarm to Jiang's plan and emphasized that negotiations would be between two sovereign states. Those in Taiwan who still supported reunification, such as the KMT, promoted a "one-China, two-government" solutions, which essentially left the question of political sovereignty open to future negotiations (Copper 1999, 59). Still, reunification was becoming a less common theme in Taiwan's polity, and some of Taipei's initiatives in the mid-1990s, such as its drive to re-enter the United Nations, seemed to indicate its vision of its future did not include a union with China. These diverging trends in the 1990s were the occasion for the eclipse of China's carrot approach to the Taiwan issue, as well as the birth of Taiwan's assertiveness.

In contrast to this divergence of political objectives at the time of the TSC, China and Taiwan were undergoing a high level of economic integration. Taiwan made China its number one foreign state for investment and the second largest destination for its exports, while China relied upon Taiwan as its second largest source of FDI (Zhao 1999, 21). Cross Strait trade totaled more than \$20 billion in 1995 (Zhao 1999, 24). Furthermore, direct contact between citizens of both entities increased dramatically. Almost 8.5 million Taiwanese visitors traveled to China from 1987 to 1995, and by 1995 there were more than 30,000 firms with Taiwanese financial backing (Chu 1997, 229-232). Beijing allowed such trade as a conscious effort to entangle the two economies in the hopes of diminishing the influence and maneuverability of pro-independence forces (Zhao 1999, 26-27). Indeed, Beijing's strategy of economic integration with Taiwan paid off in one sense; Taiwan's trade dependence with the Mainland went from 1.5 percent of its GDP to 10 percent from 1986 to 1995 (Zhao 1999, 28). However, as the University of Denver's Suisheng Zhao notes, Taiwan was not unaware of China's economic strategy toward Taiwan and attempted a series of counter-measures (Zhao 1999, 33-34). Zhao also observed that "intensified economic ties had not resulted in a spillover effect to overcome political disintegrative tendencies" (Zhao 1999, 35). This is true both because of the internal political development within each country noted above and the lack of any real dialogue between the two polities. Yun-han Chu of National Taiwan University described the China-Taiwan relationship as one of a, "concurrent process of economic convergence and political divergence" (1997, 230). This convoluted relationship played out in the TSC although the dynamics of Chinese-American relations was also a core issue.

Despite the damage to China's international standing following its brutal crackdown against the Tiananmen Square protestors in June 1989 and President Clinton's initial attempts to tie relations to improvement in human rights in China, President Clinton followed essentially the same engagement policy of his predecessor, President George H. W. Bush. The US-China phase of the conflict was kicked into high gear by the visit of Taiwanese President Lee to the US in June 1995 (Zhao 1999, 4). This event prompted Beijing to recall its ambassador to Washington, since it was perceived that the US had both gone back on its word and acted to promote the Taiwanese independence movement (Ji 1999, 82). Prior to Lee's visit, the US had responded gingerly to the growing tension in the Strait. Despite the Taiwan Relations Act's implicit pledge to assist Taiwan in maintaining its security, the US followed a strategic ambiguity approach when addressing whether it would come to Taiwan's rescue in this crisis (Hickey 1999, 278-81). Indeed, Presidents Clinton and Jiang met in a 1995 summit, and the US reaffirmed its one-China policy. The US did take some military actions, including sending the *Nimitz* and *Independence* carrier battle groups through the Strait in December 1995. This constituted the biggest naval operation in the region since the Vietnam conflict (Chen 1999, 127-128, 131-132).

We have set out a context for the TSC in which Beijing held unreasonably high expectations for advancing reunification talks, Taiwan indulged its independence movement, and the US miscalculated Beijing's reaction to the Lee visit. All these events were enough to cause conflict; however, the proximate cause of the crisis itself was the March 1996 Taiwanese presidential elections. The 1996 election was Taiwan's first truly contested national election, which threatened China with the prospect of both democracy

and national identity growing in an entity it considered an integral part of greater China (Copper 1992, 42-3). In July 1995, Beijing began a series of progressively more threatening military exercises designed to warn Taiwan of the perils of pursuing independence (Zhao 1999, 35). Beijing and Taipei then escalated their war of words, which continued until the Taiwanese election the following spring. In the weeks leading up to the March 23, 1996 election, China tested three surface-to-surface missiles in the Strait and conducted large-scale air, ground and sea exercises in the Strait (Copper 1999, 43-44). Despite the military operations, Beijing was not able to dissuade the Taiwanese population from electing the pro-independence candidate, Lee Teng-hui of the KMT. Once the March 1996 election passed, both Beijing and Taipei reduced the level of their rhetoric (Chen 1999, 130).

All sides claim victory in the TSC. The US demonstrated its resolve to support democratic Taiwan and oppose autocratic Beijing's military adventurism. Taipei had reinforced its democratic passage while furthering its legitimacy as a state. Beijing's brinkmanship strategy tamped down the independence movement in Taiwan, legitimized the CCP as the proponent of Chinese nationalism, prevented a broader conflict to suppress Taiwan, and had minimal impact on China's economic strategy (Ji 1999, 90-92). Yet, China's military actions in the TSC both reversed the most significant political opening across the Strait since 1949 and constituted the most serious military conflict in the Strait since the Quemoy and Matsu incidents in the 1950s (Zhao 1999, 1).

The Interdependence Theorist's View of the Taiwan Strait Crisis. IT does not hold that economic integration will end conflict, so a single case can neither prove the theory nor predict a particular case. However, as OR note that "trade's effect on the risk

of interstate conflict is substantial, especially for the most serious disputes—those involving fatalities” (Oneal and Russett 2003, 12). Some strains of IT acknowledge that increased Economic Interdependence equates to increased causes that can lead to conflict, but the partners want to continue trade, so these issues are answered by non-violent means and issues that could lead to violent conflict are less likely to do so if Interdependence is high. These IT adherents would argue that the TSC ended at a fairly low level of conflict due to the high level of Economic Interdependence between the players. Indeed, in this case, we see a sort of triangular IT. All the players had high levels of economic integration, which constrained the parties, so Interdependence constrained the actors in escalating this crisis to a higher level.

GG would say China is autocratic, so the conflict was not reduced. If GG were definite on this matter, we would gain an important insight, since the status of Taiwan is one of China’s gravest concerns. But again, GG leave the door open on whether their concept applies to modern China. Perhaps, autocracies which open up are creating a selectorate (albeit a small one) that demands that openness remain. How would China stop trading without upsetting its selectorate? GG are not clear on this point, and this case and the previous case point to the problem of using GG’s emerging subvariant in this case. This is particularly troubling, since China is the one case where GG’s concept would have the most utility.

IT’s shortcomings in the TSC case are significant. If the important measure of OR’s version of IT is on the less dependent state, which is the US in this dyad, how did Interdependence constrain Chinese actions? IT does suggest that President Clinton employed a strategy of ambiguity because of high Interdependence. Knowledge of such

self-restraint is helpful for US policy makers, but China's behavior is the more important for Washington to be able to predict. In the US-China dyad, the US is less constrained than China, so its level of Interdependence is the more significant in OR's methodology, an issue we have already explored. IT falls a bit short of its full potential, since we do know that China is economically interdependent and should be constrained by this factor. The shortcomings of the current state of IT methodology prevent us from making this evaluation, although OR would argue that Interdependence's impact on the dyad is still valid—the potential for Sino-American conflict is reduced due to high trade levels. On the other hand, China is the less constrained state in its Taiwan policy, which would suggest that Beijing has a greater freedom to use force against Taiwan.

The Realist's View of the Taiwan Strait Crisis. As in the WTO case, states, power, interests, anarchy and the security dilemma are the primary elements of the TSC case or any other case in international relations. For Beijing, the threat or use of force is not unexpected. Beijing's interests are to increase its power and freedom of action. A Taiwan that has declared itself independent is free to use outside powers, such as the US and perhaps Japan, to balance against China. Some realists might also suggest that Beijing seeks to prevent an independent Taiwan in order to maintain territorial integrity, a core state interest. While the international community generally does not recognize Taiwan as an independent *state* and large segments of the Taiwanese polity do not seek full independence, realists would observe that Taiwan has all the characteristics of a state. Furthermore, realists would hold that nationalist passions are irrelevant. Of course, this also plays into the concept of *anarchy*, since there is no power to preserve order between

Taiwan and China. Beijing also seeks to counter America's power in the region, and thus feels free to use force to prevent the US from exercising its powers in the region.

Washington came to the aid of Taiwan in order to preserve its freedom of action in the region, a privilege it has because of its status as the world's only superpower. Some realists would argue that China is akin to Wilhelmine Germany, a non-status quo rising state that is bent on re-ordering the power balance regionally and globally. This is probably a useful analogy although the basic rules of realism are in place in either case. Either for regional influence or to contain a rising power, the US sees value in countering China from threatening or invading Taiwan. Failure to respond to China's actions is the first step in ending US privileges in the region, and Taiwan's fall would have power balance effects both militarily and economically. Of course, Taiwan's interest is the existential one, survival. For this reason, Taipei called upon an outside power, the US, to balance a larger regional rival.

The *security dilemma* plays out in several ways in the TSC crisis. The introduction of increased forces in the Strait region causes a temporary, localized change in power balances, which alone constitutes something of a security dilemma for the players. Over the long-term, the balance of power in the region may also cause a fully developed security dilemma. China would feel threatened by an independent Taiwan, while the US would view a Chinese seizure of the island as the first step to increased Chinese economic power and thus a potentially more rapid arms buildup.

Realism suggests that balancing power in dyadic situations is complicated by miscalculations of the other's power. In the TSC, this complexity is deepened by the presence of a third player, Taiwan. Realists would hold that Taiwan's move toward

independence is not driven by domestic politics and identity issues but rather by a balancing of power imperatives. This could be driven by either China's rising military power or by Taiwan's growing reliance upon trade with China, recalling that some realists, such as Katherine Barbieri, view trade dependence as a *source* of conflict. Taiwan's informal alliance with the US is its biggest source of power against a rising China, but the introduction of the US has its own complications. Taiwan's relative power to the US is fairly unimportant to Taipei, since the US is not a threat. On the other hand, by bringing in the US, Taiwan enters a great power rivalry. For Taiwan that risk is acceptable, since its conflict with China is an existential question.

As in the WTO case, the realist failure to consider internal politics limits the utility of realism in this case. This is particularly troubling in this case, since the US has had a long and complex relationship with Taiwan, the central figure in this conflict. In their book *The Coming Conflict with China*, Richard Bernstein and Ross Munro painted a bleak picture of former high-level US government officials trading their influence for big rewards from Beijing. They propose that luminaries such as Henry Kissinger, Brent Scowcroft, and Al Haig act as intermediaries between the interests of Beijing and some US industries on the one hand and policy makers in the US government on the other. Furthermore, such prominent experts on US foreign policy are active in presenting their supposedly pro-US views to the general public via the mass media (Bernstein and Munro 1997, 105-129). Still, China is only now catching on to the influence game. In the later 1990s, the Mainland had only one law firm on retention in Washington, as opposed to fourteen for Taiwan, and members of Congress made only 58 junkets to China as

opposed to 139 trips to Taiwan (Lampton 1998, 21-26). Realists simply do not account for how such machinations influence policy.

IT, Realism in Two Dyadic Events. IT does a satisfactory job of explaining why US allowed China to gain WTO entry, although it does not clearly address whether or not Beijing appreciates the conflict-suppressing nature of increased trade. We have an explanation for why the US would take fifteen years to make a deal with China, but it is difficult to believe that liberal motivations would allow such a long delay. Realism is more consistent at explaining the behavior of both states in this case, but it comes up short when describing why Beijing elected to have less control over its economy and its freedom of actions. IT is clearly more useful (and optimistic) about describing whether more conflict will break out between the members of the dyad. IT explicitly speaks to the behavior of domestic players, a realm that realism simply ignores. Realism predicts more conflict, and indeed some realists would suggest that the WTO will lead to more trade and thus more conflict between states in a dyad. But realism tells us little about the nature of such conflict, and IT is the superior predictive tool in this case.

Realists would argue that the TSC demonstrates that IT is not valid. Despite the rising level of trade between the players, each side took actions, both military and political, that jeopardized the recent gains in trade. The level of Interdependence did not prevent the US or China from putting their military forces in harm's way. There was no war in this case, only because each side calculated that they had advanced their interests short of war. This may not be the case in the next conflict over the status of Taiwan. Balance of power considerations explain US motives very well and are adequate at explaining China's actions. IT does not explain why China risked going to war with two

of its most important trading partners. Furthermore, its focus solely on dyadic trade fails to take into account the other economic factors involved. Certainly, China also considered the potential for economic loss by threatening Taiwan, a major source of its FDI, or the potential cost to its economy if belligerency or open warfare resulted in sanctions from the US and other Western states.

Liberals hold that IT is part of a policy of engagement. US opened trade and kept it open, with the justification that it would liberalize Chinese society and ultimately reduce conflict. Liberals would argue that this has paid off, with China now in the WTO and opening to IGOs and making peaceful gestures to neighbors. Both realism and IT speak to support for Taiwan. Realists see Taiwan as a bulwark against Chinese expansion, thus serving as an avenue to contain or balance China. Liberals in general would support Taiwan as a democratic state, and IT would suggest that its policy of trade with China will lead to reduced tension.

Liberals are particularly keen on pointing to Taiwan as evidence that democratic reforms follow from economic reforms and that Confucian cultures can successfully foster democracy (Gilley 2004, 12). However, IT is not universally accepted within Taiwan as a cure for its troubled relationship with China. The 2000 election brought the pro-independence Chen into office, and he won re-election to a second and final term in 2004. However, the independence movement has had little success in forwarding its cause. Indeed, in a Taiwan that has become both more accustomed to both its democratic institutions and the growing power of China, the polity has become less enthusiastic about the politics of independence. The opposition Pan Blue coalition, headed by the Kuomintang (KMT), won a majority in the 2004 parliamentary elections. The 2005 local

elections were seen as a rebuke of President Chen's Democratic Progressive Party anti-Beijing policies and its scandal-riddled leadership (Kramer 2005). Analysts suggested that Chen will have to make some concessions to those who seek an accommodation with Beijing although he has not signaled his willingness to do so (Kramer 2005). As for the opposition, they have followed the lead of business interests to become much bolder in simply bypassing Chen to work directly with Beijing (Grauwels 2005). In the spring of 2005, KMT members traveled to the Mainland and signed an agreement with the CCP, and later the KMT chairman met with Chinese President Hu (Grauwels 2005). At the time of this research, it was not clear whether the Taiwan government would take steps to make formal contact with Beijing, but ten years after the TSC, the issue of Taiwan's status remains the touchstone of the cross Strait relationship.

Interdependence's Place Amongst International Relations Theories. The debate between liberal and realist views is one of the oldest arguments in international relations. IT and its new subvariants revived liberalism to some extent, but the dialogue in the international relations community has moved beyond the liberal and realist discussion. A variety of critical international relations theories borrow from both liberalism and realism and then pose the questions of the nature of war and peace from a different framework. Chief among these critical theories is constructivism. We introduce another international relations theory for three purposes. One, we need to demonstrate that understanding complex international situations can not be fully accomplished by examining only the two major theories already discussed. Two, we hope to demonstrate that all major international relations theories have some element of truth or utility, so they need to be

used together. Finally, we will use constructivism to demonstrate the centrality of nationalism and identity to understanding Chinese behavior.

As modeled by Alexander Wendt, constructivism, “involves two basic claims: that the fundamental structures of international politics are social rather than strictly material (a claim that opposes materialism), and that these structures shape actor’s identities and interests, rather than just their behavior (a claim that opposes rationalism)” (Wendt 1995, 71-72). In the constructivist model, social learning produces common understandings of identity which produces a community of shared interests. In the modern era, the state is the prevalent unit of analysis for such communities. While this is true of relations between states, internal societal constructivism explains how a similar process of learning produces societal norms that drive behavior within the state. This recognition that the internal dynamics of a state affect its external relationships is also a hallmark of liberalism. Conflict arises when the interests of different communities collide. So, while realists and constructivists believe that states are important players and that states pursue interests, realists would hold those interests are immutable, while constructionists would say they are subject to change and are determined by dominant norms in society. Like liberalism, constructivism sees cooperation as a normal state behavior. For many liberals, cooperation comes about due to the realization that it produces a social good. Constructivist hold that cooperation, as well as conflict, comes about due to social learning between states, and that norms and shared expectations about the appropriate behavior states drive behavior.

Constructivism would see the WTO as a powerful tool for socializing China. By “playing by the rules” of international order, China learns about appropriate behaviors

and global norms. China is forced to see that its singular world view is not productive. Similarly, constructivists would argue that the United States' acceptance of China as a WTO member socializes the US into perceiving China as an appropriate and full partner, despite its violent past, autocracy and potential as a world power. Here the constructivist reading is not dissimilar from the liberal-IT perspective, particularly in seeing China's entry into the WTO as a sort of salve for healing China's broken relationship with the rest of the world.

As for the TSC, the constructivist would be concerned by the rise of a separate Taiwanese identity, since it creates a division where one did not explicitly exist before. The current period sees several competing identities for those living on both sides of the Strait: does a Taiwanese citizen, born of Chinese Mainland parents consider herself Chinese or Taiwanese, and does she have the same identity as a her neighbor whose parents were native-born Taiwanese? Similarly, Chinese hypernationalism, whether anti-American, anti-Japanese or pro-reunification, suggests a step away from positive social learning. Both tendencies suggest creation of distinct and competing communities at a time when other states in the region are just beginning to envision a larger regional community. This appreciation for the power of identity is constructivism's greatest addition to our understanding of the China-Taiwan environment. Nationalism is a real driving force that realism ignores and liberalism sees as an obstacle that will simply fade away with the onslaught of liberal ideas.

This aspect of the constructivist's view is particularly important for the Sino-American relationship, since the US has been the leading nation in creating and promoting international institutions. America's supporting human rights is a prime

example of how Washington has traded immediate self-interest in exchange for the long-term goal of bringing China to accept international norms. Like liberals, constructivists see a benefit from China's recent urge to join IGOs, particularly those like ASEAN and APEC that have regional influence. Unlike liberals, constructivists are not concerned about how these IGOs create incentives to conform, rather they see it as a socializing process for a China that has been too long isolationist or warped by Maoism.

The constructivist argument faces several challenges. One, despite the rise of regional organizations, there is much to overcome. Some states (e.g., Burma) do not play in the game, some states (e.g., Indonesia, Malaysia) have severe internal divisions, and some are potentially failing states (e. g., Laos, Cambodia). Two, there is no process for the US, China and Taiwan to address their divisions on Taiwan's status. Three, Taiwan is not considered a state, so it remains "unsocializable" to some extent. China will not let the issue become internationalized, since it considers the status of Taiwan to be a purely internal issue. Four, while China has not displayed an aggressive revanchist tendency, it has shown a capacity for hypernationalism that may drive events. For as Wilhelmine Germany had its Alsace-Lorraine, China has its Taiwan.

Test 4 used two dyadic events to determine IT's utility by comparing it with other major international relations theories. China has demonstrated that it is willing to threaten or use limited force even in the face of potentially losing economic ties with the US. Alternatively, IT may better explain why China has traded considerable control over its economy in return for presumed economic growth and why the US ultimately allowed China to enter the WTO. Finally, the introduction of constructivism reminded us that notions of identity and nationalism are important to understanding Chinese motivations

and that multiple perspectives are needed to comprehend and predict the behavior of states.

Results of Test 2-4: Data and Analysis

Chapter 5 (and the 3 tests therein) attempt to address the second research question: How does IT explain the nature of the relationship between the US and China? We explored this question, using three tests, the results of which are provided below.

Results of Test 2: Sino-US Economic Interdependence using Oneal and Russett's Methods.

1. Our look at the dyad in Test 1 told us that the Chinese and American economies are integrated using broad measures, while Test 2 told us that the two states also have high levels of Interdependence using OR's methodology.
2. However, the data on the relationship between conflict and trade are inconclusive.
 - a. The number of dyadic conflicts is much reduced since the Cold War, but more recently there has been increasing conflict.
 - b. The data show the highest level of conflict reached is considerably less than during the no-trade, Cold War period. This supports the notion that

trade may not reduce the number of conflicts but may reduce the level of conflict that arises.

Results of Test 3: The Impact of new Interdependence Subvariants on the Sino-US case.

1. GG suggest that the lack of democracy in China either diminishes or negates the conflict tamping aspect of Interdependence.
2. However, this IT subvariant is still unproven. Additionally, China may be an exception to GG's model, since its leaders are trade-dependent, and its selectorate wants continued trade with the US.
3. As a corollary on democracy, Mansfield and Snyder caution that China as an illiberal or incomplete democracy may make the conflict-reducing aspects of IT irrelevant.

Results of Test 4: Sino-US Relations in Practice.

1. IT has great utility in explaining US motives for allowing China to enter the WTO (albeit only after a strenuous process). IT does not shed much light on Beijing's motivations in this case. However, IT does suggest that the result is highly significant, since the increased trade that follows WTO membership will lead to less conflict. IT is then a very good predictive tool for policy makers.
2. IT explains why the TSC was a fairly low-level conflict, but IT does not explain why all the parties were willing to take such risks by using force.

3. The GG subvariant was not a rigorous tool in these case studies, since its application to the China case is undetermined. At best, we can warn policy makers that IT's influence on Beijing's may be questionable.

Results of Tests 2-4.

1. IT has flaws and shortcoming, as do the other international relations theories.
2. IT should be used in conjunction with other international relations theories.
3. IT has its greatest utility when discussed as a component of the larger liberal theory (the Kantian tripod as refined by OR).
4. IT is necessary but not sufficient for explaining the specific impact of trade on conflict.
5. GG attempt to correct OR's methodological failure of not distinguishing the conflict initiator may be proven true in the future, but the China case may be an exception.

Summary. In this chapter, we have examined the abilities and limitations of IT to explain the impact of economic integration between the US and China. IT does not explain every action, nor predict every outcome. Indeed, its mere ambition is to tie trade to conflict. This it does very well, although it may be somewhat limited by its methodology. We found that the GG subvariant was the most likely new aspect of IT to have relevance for our understanding of the impact of trade upon conflict in a dyad; however, the theory comes up short in determining the case of China, an autocracy which has elected to have high trade levels. In a general sense, we would expect that the potential for armed conflict between the United States and China in the long-term will be

reduced by Interdependence. Given that, non-militarized disputes should be expected to remain at current levels or increase. The current impact of the Kantian tripod is unmet because China has failed to accept democratic practices. In Chapter 6, we turn to the implications of our research for US policy makers. We propose recommendations and then move onto the last our research questions: Given a policy of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation?

CHAPTER 6
IMPLICATIONS AND POLICY RECOMMENDATIONS

Introduction

Those who conduct foreign policy often dismiss academic theorists (frequently, one must admit, with good reason), but there is an inescapable link between the abstract world of theory and the real world of policy. We need theories to make sense of the blizzard of information that bombards us daily. Even policy-makers who are contemptuous of “theory” must rely on their own (often un-stated) ideas about how the world works in order to decide what to do. It is hard to make good policy if one's basic organizing principles are flawed, just as it is hard to construct good theories without knowing a lot about the real world. Everyone uses theories -- whether he or she knows or not -- and disagreements about policy usually rest on the more fundamental disagreements about the basic forces that shape international outcomes. (Stephen Walt in “International Relations: One World, Many Theories”)

Dr. Walt is speaking to the benefits to the policy maker of using theory, which reflects a goal of this research. Theories can organize thoughts and facts, bring meaning to the complex, and provide a common framework and starting point. Certainly, theories

and models have their drawbacks, since they can oversimplify the complex. Much of this research has attempted to examine the benefits and limitations to Interdependence Theory. In this chapter, we will marry our findings to specific policy recommendations. This effort will provide some practical rather than theoretical utility to our efforts and will address our third research question: Given a policy of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation? This chapter has three sections: Implications for US policy makers, Chinese and American national security strategies and recommendations for US policy makers.

As we noted in Chapter 5, all three of the major IR theories we examined have some utility in explaining the events in our case studies. Thus, IR theory is a composite of several theories that may contradict each other at times. But policy makers have little use for open-ended propositions as their foundation for making specific policy. They are not asked to deal with broad, philosophical issues, such as, why do states fight, but rather specific policies, such as, does it make sense for my state to extend trade relations with another state at this time? In the case of China and the US, both states pursue strategies that seek some level of engagement, including trade, within the dyad.

Implications for US Policy Makers

In Chapter 2, we identified that the outstanding work for IT at this time is to define the characteristics of those majority and minority cases (when dyadic Interdependence works to suppress conflict and when it does not). In our research, we

found that OR remain the dominant theorists, while GG have attempted to prove that polity type may either diminish or eliminate the conflict-suppressing aspect of Interdependence. Taken alone, these conclusions are not particularly compelling for policy makers, since there remains a lack of clarity on the policy implications of IT. They would ask: Does Interdependence make a difference in whether China is inclined to use or threaten to use force against the US or its allies? Despite the lack of finality in the US-China case, we can provide policy makers with a few conclusions on how Interdependence changes the US-China relations. These are provided below:

Oneal and Russett provide the best understanding of IT's impact on dyadic relationships. Generally, high levels of merchandise trade reduce military conflict in a dyad although it may increase lesser, non-military conflict specific to trade matters. As pointed out in previous chapters, China has bought into market mechanisms in a big way. It does value trade and will continue to do so for the foreseeable future as a major part of its grand strategy (see below). In addition, OR would point to China's increasing membership in IGOs and its relative improved relations with most of its neighbors as evidence that at least two legs of the Kantian tripod are in effect in China. IT bolsters the argument that engagement and economic openness can impact China's behavior towards the US and the West. The application of IT theory in reverse is also true. Should we significantly impede China's trade with the US, we should expect to see significant increases in the potential for conflict from China.

Gelpi and Grieco provide a warning to policy makers that China may be an exception to IT's conflict-reducing qualities. At this time, GG come up a bit short in negating IT in the case of China; however, they do provide ample reason to consider

Chinese internal motivations. By concentrating on domestic players (selectorates), GG reveal that for the first time in the PRC's history, we can have some insight into domestic Chinese decisionmaking. The "black box" of China's internal political debate has long confounded China-watchers. However, US policy makers can now more readily see and interpret a China in which market-driven interests (part of GG's selectorate) are major players in Beijing. The question GG really pose is: Which does the selectorate value more, the gains it can attain via a confrontational policy or the gains it will see from a long-term strategy of economic engagement and cooperation? GG do not answer the question, but policy makers have two options if GG should prove correct: discount IT in the China case or ensure China becomes democratic to guarantee the conflict-suppressing effect of Interdependence.

IT has strengths and weaknesses as an applied theory. The US cannot solely rely on the power of IT to prevent a military crisis over issues that are considered vital national security objectives to China. Both the OR and GG versions of IT suggest that it is very difficult to judge the actual impact on Beijing's behavior. China's core national security objectives may well trump economic considerations, even if they may lead to significant cost to China. For example, since regaining sovereignty over Taiwan remains one of Beijing's key policy objectives, it is difficult to assess IT's impact on Beijing's behavior.

IT's impact is felt in the United States. Policy makers need to understand that the US decisionmaking process also has been impacted by Interdependence with China. This may lead the US government and other non-governmental actors to policy decisions that may not be in our own best interests. Thus, policy makers can be constrained by or propelled by a variety of interests in the US; policy does not begin and end with a

meeting of the National Security Council. These interests, notably business, labor, environmental, human rights and ethnic groups, will have extraordinary input to the policy process.

Economic Interdependence Theory enjoys the same strengths and weaknesses of any international relations theory. In this case, IT improves our understanding of the nature of economic integration and its ability to reduce conflict. At the same time, the challenge of IT in understanding the security environment is its lack of certainty in a general sense (it only reduces the potential for conflict) and possibly its lack of applicability in the China case (as proposed by GG). Of course, the purpose of policy makers is not merely to understand the environment but to influence that situation in one's interest. So, we turn to the use of IT as a component of US national strategy, and we begin by examining the national security strategies of both China and the US.

Chinese and American National Security Strategies

China's Strategy. Toward the end of his tenure, Deng proposed a vision for China's role in the world that has become known as the *24 Character Strategy*. It states China should, "observe calmly; secure our position; cope with affairs calmly; hide our capacities and bide our time; be good at maintaining a low profile; and never claim leadership" (OSD 2005, 11). In *Interpreting China's Grand Strategy: Past, Present, and Future*, Michael Swaine and Ashley Tellis call this national approach to the world a "calculative" strategy. This calculative security strategy is defined as, "a pragmatic approach that emphasizes the primacy of internal economic growth and stability, the

nurturing of amicable international relationships, the relative restraint in the use of force combined with [efforts to modernize the military], and the continued search for asymmetric gains internally” (Swaine and Tellis 2000, 97-98). This strategy is anchored by the concept that Beijing must acquiesce to international norms in order to continue building its economic and technological base, which will one day guarantee security and freedom of action. Swaine and Tellis also examined the factors that created such a strategy. They hold the Chinese have three motivations: a centuries-long tradition that places China as the predominant cultural, economic and political power in East Asia (an area of intense interest for the US); a desire to right old wrongs and gain respect as a great power; and the central government’s attempt to make nationalism or hyper-nationalism the common ideology of the Chinese people (Swaine and Tellis 2000, 2-5).

In the execution of this strategy in regards to the United States, China has pursued a two-track policy of “cooptation” and “prevention” (Swaine and Tellis 2000, 114 -15). Cooptation takes the form of remaining engaged with the United States and particularly its economic entities, while prevention seeks to undermine US efforts to hinder China’s rising economic and political power. Since economic advancement is key to its long-term strategy, maintaining open trade with both the West and its regional partners is critical to its success. Thus, China relies upon economic integration as a foundation of its strategy but does not seem to recognize the conflict-suppressing nature of such economic relations.

Beyond 2020, Swaine and Tellis see a less clear and probably more dangerous future for Sino-American relations. Assuming that Beijing is indeed thinking along the lines of the proposed strategy outlined above, Beijing will reform its strategy once it no

longer feels it must continue to follow the rules laid out by a Western-dominated international environment. Swaine and Tellis believe that past 2020 Beijing will either pursue an assertive or cooperative strategy. They do not suggest that there will be no conflict between the US and China before 2020, only that the present strategy will remain in place until China reassesses its relative strength. A cooperative China would seem to resemble the United States. An assertive China would attempt to rewrite the rules of international behavior and would seek to address past grievances. An assertive China would threaten US interests by limiting freedom of action in East Asia, controlling access to Asian markets, and weakening our formal and informal alliances in East Asia.

Avery Goldstein, Senior Fellow at the Foreign Policy Research Institute, also holds that we can only identify China's "transition strategy," one that holds only in the current period of American global hegemony or unipolarity (Goldstein 2005, 38-40). In Goldstein's view, since the mid-1990s, China has come to comply with international standards and institutions in order to foster its continued development. At the same time, it has sought to prevent creating a security dilemma for its rivals, so its rise will not be counterbalanced (Goldstein 2005, 12). Still, Beijing's goals of increasing its instruments of power, increasing its regional influence, making its interests heard on the global stage, and achieving control over all its declared territory, particularly Taiwan, suggest that even in the short-term, there are many opportunities for US and Chinese interests to intersection in a conflictual manner.

Goldstein also briefly touched upon an international relations initiative that Beijing surfaced in 2003-04. Both Premier Wen Jiabao and President Hu Jintao put forward a concept that was originally called *Zhongguo hpeing jueqi* or "China's peaceful

rise.” The concept was developed by Zheng Bijian, an influential academician who has held several senior positions in the CCP. In his formulation of the concept, China will not be a “modernized, medium-level developed country” until 2050 (Zheng 2005). In the decades until that objective time, China will seek to rise to become a responsible member of the international community using a strategy that will

transcend the traditional ways for great powers to emerge, as well as the Cold War mentality that defined international relations along ideological lines. China will not follow the path of Germany leading up to World War I or those of Germany and Japan leading up to World War II, when these countries violently plundered resources and pursued hegemony. Neither will China follow the path of the great powers vying for global domination during the Cold War. Instead, China will transcend ideological differences to strive for peace, development, and cooperation with all countries of the world. (Zheng 2005)

If China is not to be a Wilhelmine Germany, how should its neighbors and the United States view an empowered China? Zheng speaks of the mutual opportunities that China’s neighbors can receive from trading with a growing China. While short of a recognition of Economic Interdependence Theory, Zheng does suggest that economic engagement can provide motives for seeking peaceful coexistence. He also acknowledges the importance of the US in playing both economic and security roles in East Asia. This model is in contrast to China’s behavior in the 1990s, when it aggressively sought to confront neighbors over border disputes and failed to play a

proactive role in international disputes, such as the United States' attempt to curb North Korea's nuclear ambitions (Tellis 2005). China now downplays territorial issues and has become a much more important player in the international environment, including matters, such as terrorism, which are of vital interest to the United States. In essence, China has developed and executed a plan to employ soft power with its neighbors, the United States and intergovernmental organizations.

Ashley Tellis (2005) believes that Beijing came to the conclusion that the United States would remain a superpower well into the 21st Century and that counterbalancing efforts against Washington would fail. So, China has pursued a policy that seeks non-confrontational relations with the US and, at the same time, reduces the reasons for its neighbors to join in a US-led coalition to contain China. Thus, a soft power strategy serves China's goals much more effectively than a mere reliance on hard power. There are exceptions to the policy. Taiwan remains outside the pale, since China considers it to be an internal issue although even here Beijing has learned the power of winning friends in Taipei. The other exception is Japan, where both states have been engaged in increasingly shrill accusations over territory, resource development and historical legacies.

Internal political machinations have since changed the terminology used to express the policy, with "peaceful development" and "peaceful coexistence" occasionally being used (Tellis 2005). Goldstein attributes these changes to intergenerational conflict within the CCP (2005, 38). Whatever the terminology, the policy remains a pillar of China's foreign policy. Whether we view the policy as a nod toward soft power or a cynical attempt to lull its neighbors and the US into complaisance while it builds its

strength, this policy is a logical follow-up to the economic engagement strategy put forward by Deng.

America's Strategy. President Bush's national security strategy for China reflects what has been a surprisingly consistent policy approach to China since the end of the Cold War. In 2002, he put forward these basic notions:

The United States relationship with China is an important part of our strategy to promote a stable, peaceful, and prosperous Asia-Pacific region. We welcome the emergence of a strong, peaceful, and prosperous China. The democratic development of China is crucial to that future. Yet, a quarter century after beginning the process of shedding the worst features of the Communist legacy, China's leaders have not yet made the next series of fundamental choices about the character of their state. In pursuing advanced military capabilities that can threaten its neighbors in the Asia-Pacific region, China is following an outdated path that, in the end, will hamper its own pursuit of national greatness...

The United States seeks a constructive relationship with a changing China...

China has begun to take the road to political openness, permitting many personal freedoms and conducting village-level elections, yet remains strongly committed to national one-party rule by the Communist Party. To make that nation truly accountable to its citizen's needs and aspirations, however, much work remains to

be done. Only by allowing the Chinese people to think, assemble, and worship freely can China reach its full potential.

There are, however, other areas in which we have profound disagreements. Our commitment to the self-defense of Taiwan under the Taiwan Relations Act is one. (George W. Bush, *The National Security Strategy of the United States of America*, 2002)

The US remains interested in pursuing a mutually beneficial economic relationship with China, although such a policy clearly will result in increasing China's economic and military power. The US also expresses an intense interest in China becoming a democracy. Both of these strategic components, economic engagement and support for democratic institutions in China, are Kantian ideas that support a generally liberal strategy for China. In the same vein, the US has long pursued policies that emphasized liberal impulses that China has declined to embrace. For these reasons, the US has placed on our agenda with China issues of human rights and freedom of worship as part of our strategy. So while the liberal aspect of the US's strategy has opened relations to China in a truly significant way, the lack of liberal values and institutions within China represents a source of conflict.

On the other hand, the US views China through a realist lens. We are clearly concerned about a rising and aggressive China in East Asia and implications for US influence in the region. For these reasons, the US supports alliances and temporary accommodations with nations in the region (Japan, Taiwan, South Korea, the Philippines,

Pakistan, Uzbekistan, etc.) that are at least partly motivated by concern over China's growing power. Washington works at building international regimes, such as the Biological Weapons Convention, that seek to prevent the spread of technologies from China and other states. Lastly, the US recognizes the one issue which is most likely to bring China and the US into military conflict, Taiwan. Washington supports Taiwan, as it has done in different forms since 1949, in part because of its symbol as a long-time friend of the US and functioning democracy and in part because of its vulnerability to the autocratic and militarily more powerful neighbor across the Strait. Those military realities drive important aspects of the US's military policy.

America's military strategy is increasingly focused on China's rise and its potential as a peer competitor. US defense strategy is most clearly stated in the *Quadrennial Defense Review Report (QDR)*, which is produced by the Secretary of Defense by direction of Congress. While the 2001 QDR failed to mention China by name, the February, 2006 version puts a rising China at the center of future US security concerns: "Of the major and emerging powers, China has the greatest potential to compete militarily with the United States" (Rumsfeld 2006, 29). Secretary Rumsfeld's strategy is to ensure the US has the appropriate resources and force structure to both dissuade China from entering an arms race with the United States and ensure the US has the power to defeat any Chinese aggression. The force structure is dictated by the expected battlespace, so "...the challenge of en route and in-theater U.S. basing place a premium on forces capable of sustained operations at great distances into denied areas" (Rumsfeld 2006, 30).

In other words, to defeat a peer competitor China, the US needs to ensure continued basing in East Asia and long-range naval and air assets to operate against China. So, while the 2006 QDR calls for the Army to invest heavily to develop the Future Combat Systems for its soldiers, it also calls for massive spending on the F-22 Air Force fighter and a large expansion in capital ships for the Navy (Rumsfeld 2006, 42, 46, 48). That the US should consider maintaining its high level of military spending is not too surprising. What is unexpected is that these Air Force and Navy programs are being advanced in an era of tightening budgets, while the US is engaged in expensive, ground force-centric conflicts in Iraq and Afghanistan. In the face of these conflicting security needs (potential peer competitor versus ongoing counterinsurgency), the Bush Administration's willingness to spend precious resources to counter China reflects the seriousness of the perceived threat from Beijing. Still, even the QDR, presumes that the goal is to deter China from going down the path of aggression and instead accept full membership in the community of nations. Taken together, the US defense and foreign relations policies contain elements of both engagement and containment.

Policy Recommendations

In our policy recommendations, we assume that the current situation remains true: both states seek economic engagement as outlined in the section above and a high level of Interdependence exists between the US and China. We then offer ways in which US policy makers can best advance US interests. Our recommendations begin with broad strategy and move to more specific policy components.

Retain Interdependence as a Strategy Component. As noted, US strategy toward China contains both elements of engagement and containment. As a subcomponent of its strategy, advancing Interdependence serves US policy makers well. While we have pointed out the weakness of the Interdependence Theory, IT is not alone among international relations theories in lacking solid predictive qualities. IT has enough promise to retain economic engagement as a pillar of US strategy. The risks of empowering an illiberal China are outweighed by the promise that engagement will create change agents who will modernize Chinese society, promote institutions that will replace liberal ideas for those of nationalism and autocracy, and will pull China further into the community of nations. Indeed, engagement remains a viable option in part, because the opposite policy (economic disengagement) appears impractical and unachievable. The US cannot hope to contain China's economic growth, since few nations would follow our lead and powerful business and consumer interests would likely prevent such a policy from coming into being, barring some significant aggressive act by China. A successful implementation of such a policy would merely punish US economic interests.

An important caveat of an engagement policy is to ensure the internal constraints on US policy makers do not overshadow other aspects of US strategy. The containment aspect of US policy may be overcome by domestic interests who seek to maintain economic engagement, no matter what the cost. Paul Papayoanou suggests this situation existed in Europe before the First World War, when the British and French felt constrained from balancing a rising Germany because of domestic pressures resulting from economic integration (Papayoanou 1997, 135). While the nature of the

Interdependence between the US and China is arguably more complex than that between the European powers in the early 1900s, the European experience with a rising Germany demonstrates the need to remain wary of internal constraints that reduce the ability of democracies to contain autocratic powers intent on upsetting the status quo. Similarly, other policies may influence the ability of the US to effectively implement its engagement policies. Chief among these conflicting policies may be increasing competition for resources, particularly energy resources. While such conflict is not unexpected, the potential for economic impact is substantial. Should the US-Chinese economic relationship shift from one of mutually beneficial trade to one of resource competition, the conflict-reducing aspect of IT would be diminished.

Lastly, the British responses to two very different rising powers, the US and Germany, demonstrate the challenges of developing policy against such states. James A. Nathan observed that while US policy toward China currently employs both elements of engagement and containment, history teaches us that, in the end, one policy or the other wins out (2002, 105-06). In the case of America's rise, the British essentially sought accommodation, or appeasement in the pre-Chamberlain sense (J.Nathan 2002, 114-15). The British elected not to confront the US based upon calculations of the threat that the US posed to British interests (Nathan 2002, 115). The British generally were satisfied with this policy choice. On the other hand, London eventually elected to confront the aggressively, non-status quo Germany that more directly threatened its interests (J. Nathan 2002, 115). In one case, appeasement worked, but in the other confrontation was the superior policy. Nathan suggests that the US will face the same choice with China (J. Nathan 2002, 124). Indeed, the parallels between Germany and China are startling. Both

relied very heavily upon trade with potential rivals, and both also relied upon capital inflows from those same rivals. The lesson for policy makers is to maintain awareness of China's changing nature and growing strength and to be prepared to determine whether or not engagement with China remains a beneficial policy.

Leverage China-Taiwanese Interdependence. The US has little interest in seeing an autocratic China as the dominant power in East Asia. While a free and open China might constitute a preferred international partner for the US, that vision is a distant reality. The US must deal with the China that is before it and not the China of its liberal aspirations. The current China is driven by a calculative strategy that seeks to maximize its autonomy in the region and assert control over its claimed territory, including Taiwan. Added to that mix is a virulent form of Chinese nationalism that is both manipulated by Beijing and beyond its power to contain. The US cannot risk appeasing China by giving into its most ambitious aspirations, but in the case of Taiwan, the US *can* use Chinese-Taiwanese Interdependence to influence aspects of China's objectives.

We have seen an incredible increase of Economic Interdependence between Taiwan and China over the past two decades. As we noted earlier, Taiwan has invested billions of dollars in China, and the dyad members are significant trading partners. This is significant to US policy makers in two ways. First, according to IT, Taipei and Beijing are already constrained in the use of force, which equates to a lessened opportunity for US-Chinese conflict (Kastner 2004). Second, Taiwan's presence in China provides a significant chance for change agents to influence China's economic, social and political development. The presence of approximately one million Taiwanese citizens in China reveals just how closely these two societies have become enveloped with each other

(Bickford 2005). These Taiwanese citizens can be seen as the vanguard for a free and open China, a stated goal of the US's national strategy. Taiwan's citizens, corporations and the liberal ideas they carry are a teaching tool to China that Sinic cultures can become liberal and democratic. *The US should work to maintain and expand Chinese-Taiwanese Interdependence.* A serious attempt to reverse dyadic Interdependence will only increase the potential for conflict between Taipei and Beijing, which bodes poorly for US interests. By maintaining and expanding these ties, Washington can serve to promote a freer China that will serve both US and Taiwanese interests. Both interests will be served if Washington and Taipei are cognizant that Interdependence also brings with it the possibility that domestic interests may pressure the government to act in ways that are inimical to the long-term goals of the US and Taiwan.

Improve Institutions to Resolve Trade Issues. China is dedicated to trade as a core element of its national security strategy. In pursuit of this strategy, China has made great strides to integrate into the international economic system. Still, many aspects of its command economy remain, market institutions and standards are below global standards, and political power is still restricted to the CCP elite. China has become a global trader with inadequate tools, and the implications for trade with the US and other states are significant. While the WTO created specific mechanisms to deal with US-Chinese trade disputes, the relationship is still somewhat underdeveloped and fraught with opportunities for missteps. The US should continue to press for improved mechanisms to handle dyadic trade disputes and pull China deeper into regional and global trade organizations. This is particularly important in the near future. Since China entered the WTO in 2001 and the last major enforcement measures came into place in 2005, the immediate pressure

for China to do more to conform to international standards has lessened. Continuing to refine and reinforce measures to address trade disputes will serve to keep Beijing engaged with US concerns. In addition, expanding efforts to help China develop business practices and standards will make solving trade disputes easier, since the two sides can speak from a common framework.

The other component of Interdependence we addressed in our literature review in Chapter 2 was openness. Openness is a trade measure of how integrated a state is with the global economy. Openness is measured as a state's total trade over its total GDP. We have not concentrated on this variable in this research, since it is not a dyadic measure and cannot be tied directly to the US-China case. OR found that increasing openness by a single standard deviation decreased the level of conflict by 27 percent (Russett and Oneal 2001, 146, 171). With trade amounting to 25 percent of its GDP, China is already highly open, indicating that increased trade has already decreased the potential for conflict (Russett and Oneal 2001, 296). *US policy makers should work to improve and expand multilateral trade agreements that will maintain high levels of Chinese openness in order to reduce the chance that the US will be drawn into a conflict between China and another state.*

Lastly, the high level of trade between the US and China came about very rapidly and represents something of a historical anomaly. As the economic relationship continues to evolve, *US policy makers should prepare for the next trade challenges in the dyad.* The US's high trade deficits and China's yuan valuation will remain matters of concern, but as China's economy advances and expands, Washington should cast an eye toward the next issue of concern. In addition, Washington must prepare for any

eventuality. The US should prepare for plans for the relationship in the event of an evolution, change in or loss of trade with China. This is relevant to this case, since declining Interdependence equates with an increase in the potential for conflict.

Advance the Kantian Tripod: Intergovernmental Organizations.

Over time, the Chinese system of government may or may not become more democratic. If it does, that will increase the prospects for peace: a transition to democracy is likely to be less dangerous than autocratic stability. Even in the absence of democracy in China, however, our evidence indicates that a strong web of commercial ties and intergovernmental organizations can make a big difference.

(Oneal, Russett, and Berbaum 2003, 388)

Oneal, Russett and Berbaum remind us that each of the three legs of the Kantian tripod has a conflict-reducing quality. At the same time, they reinforce each other and together form the foundation of America's broad engagement strategy with China. US policy makers would then expect benefits from increasing the effectiveness of all legs of the tripod, including mutual membership in intergovernmental organizations (IGOs). As we have already indicated, since the Deng era, China has committed to joining IGOs. In a general sense, the US should encourage such participation, since OR believe this will reduce conflict among member states. For OR, this level of mutual IGO participation has already decreased the potential for US-China conflict by 28 percent (Oneal, Russett, and Berbaum 2003, 383). Thus, the US should continue to persuade China to participate in

IGOs. In addition, the US has options (albeit limited) to utilize the Interdependence and IGO legs together.

One specific avenue to accomplish this would be to encourage the creation of an East Asian preferential trade agreement (PTA), since Interdependence within Asia would equate with less conflict between China and its neighbors. This in turn would equate with less Sino-American conflict, since the US would be less likely to be drawn into a regional conflict. An East Asia PTA is still a long way off, but the states in the region are heading in that direction as evidenced by the trend we have seen in recent years wherein intra-Asian trade has grown faster than its extra-regional trade (Kawai 2005, 29-33). Of course, the United States would not want to support an initiative that would injure its economic interests. However, as long as the US retains access to Chinese markets, an East Asian PTA would not necessarily be contrary to US interests.

Advance the Kantian Tripod: Democracy. Of the three Kantian legs, democracy is by far the least developed in China. China has moved aggressively to increase trade and join IGOs, but it has made almost no progress in establishing representative government during the Deng and succeeding regimes. OR do note that from the mid-1960s (a decade before our study period), China was a -9 on the Polity scale while now it is merely a -7. For Oneal and Russett, even this minor improvement in China's political system represents a significant reduction of 17 percent in the potential for conflict within the dyad. Inasmuch as China is willing and capable, further progress in developing democratic institutions will result in less conflict between China and the US. In other words, of all the legs of the tripod, democracy or more precisely Democratic Peace Theory contains the most potential. Interdependence and IGO membership can be

increased, but democracy remains the untapped Kantian source to reduce conflict with China.

The policy option we must consider is *whether* and *how* to encourage democracy in China. In recent years, the US has employed both subtle and direct means to promote representative government in the world. In the Ukraine, the US provided training and minor financial support, while in Iraq “regime change” was used to supplant an autocratic with one that will hopefully become democratic. Indeed, the Cold War saw ongoing efforts throughout the world. In China’s case, the US’s policy options are much more constrained. The US has little direct ability to influence internal Chinese individuals, and China will not tolerate direct efforts. On the other hand, Interdependence already promotes the exchanges of populations and the subsequent exchange of ideas. More succinctly, US and Chinese Interdependence is already a strong factor promoting liberalism in China.

To consider *whether* the US should promote democracy in China, we remember Gelpi and Grieco’s warning that the lack of democracy in China means that IT will not have its desired effect. But, one can read GG’s warning in two ways. Should GG prove correct, one could hold that policy makers should disregard IT, since it would have no impact in the US-China dyad. However, another view of the GG concept is that US policy makers need to *ensure* China remains on a course to full democracy in order for Interdependence to have its effect. Our consistent national strategy has been that democracy is good for China and for US interests, and IT and the GG subvariant suggest that promoting democracy in a state of Interdependence will reduce conflict. Furthermore, IT also suggests the question of *how* to promote democracy in China.

IT may be the best mechanism by which to bring about democracy, while at the same time deepening IT's impact. In *Profits and Principles: Global Capitalism and Human Rights in China*, Michael Santoro examined the role of multinational corporations (MNCs) in China. He believes that MNCs are, "making a positive contribution to democratization and human rights in China" (Santoro 2000, ix). Santoro lays out a convincing case that MNCs, "are 'exporting' human rights values to developing countries" and that much of this is simply a spin-off from normal day-to-day business operations (2000, 33-43). Santoro posits that MNCs are the vital foreign influence in China, and MNCs act as a change agent in China by creating personal wealth, changing worker values and behavior, creating the idea of meritocracy, inspiring teamwork while valuing the individual, and modifying the normative standards in Chinese business (2000, 33-43).

Santoro holds that China is nearing the culminating point where economic performance will naturally sustain democracy although less than one percent of Chinese workers are employed by foreign-invested companies (Santoro 2000, 67). MNCs are not the only agents in change in China. As we noted in Chapter 4, more than 88,000 Chinese and Hong Kong students studied in the US during the 2003-2004 school year (*Chronicle of Higher Education* 2005; table 4.8). The Chinese government claims that its students are returning home (from all countries) at an ever greater rate (13-15 percent increases year-over-year recently), which would enhance the impact of Interdependence (Li 2005, 93). The Ministry of Education reports that "from 1978 to the end of 2004, a total of 814,884 Chinese had gone abroad for study, with 197,884 returning" (Chinese Ministry of Education 2005). On the other hand, some reports indicate that Chinese students are

staying in the US at a very high rate (Bartlett 2005). More worrisome for the future of students as change agents is that the number of foreign students in the US dropped for the first time during the 2003-04 schoolyear and dropped again in 2004-05 (*The Economist* 2005). Some of this loss is due to the strict new visa process put in place following the September 11, 2001 terrorist attacks, while some of the decline is due to the fact that several states, such as Australia, have made a concerted effort to create an attractive alternative for foreign students (*The Economist* 2005). As a further example, Japanese universities now have 77,000 Chinese students, which constitutes 65 percent of its foreign student body (Brender 2005). While Chinese students can become change agents by attending Australian and Japanese schools, the potential reduction in Chinese students studying in the US is not a positive trend for bringing US values to China.

In addition to MNCs and returning students, there are other significant change agents in China. 110,000 Americans are now living in China which represents a new high (Macleod 2005), and China is one of the fastest growing destinations for US students in non-degree programs (*Chronicle of Higher Education* 2005). Lastly, we again note the one million Taiwanese citizens who live and work in China (Bickford 2005). While these numbers may seem small in a population of 1.3 billion, these change agents influence the most progressive and economically powerful members of Chinese society. They are, of course, hampered by the CCP's ongoing efforts to prevent the creation of competing political power bases in China. On the other hand, the Chinese government is implicated in the introduction of liberal ideas into its society. Beijing's policy of economic openness and relatively free population exchanges suggests that these change agents, individuals and MNCs, will continue to shape Chinese society.

Despite our endorsement of indirectly promoting democracy in China, caution is required when we consider how we should encourage democracy in China. Support for democracy must be made in light of Mansfield and Snyder's concept (an idea directly disputed by OR, as relayed to this researcher in a telephone conversation with John O Neal on January 19, 2006) that states that make an incomplete transition to democracy are more likely to fight. This prospect is particularly troublesome in China, since the CCP rests upon a fragile popular foundation, and China's hypernationalism and perceived humiliations portend conflict in an illiberal China. The most prudent method is to aid liberal institutions, such as the legal system, that will have a lasting impact on China and support causes that encourage change but are not directly confrontational with the central government. Such measures give support to the agents of change who have entered China via Economic Interdependence.

In China, increasingly economically powerful elites will have ever greater political influence. As noted earlier, Papayoanou and Kastner found that in the wake of the Deng reforms a wider range of actors make up the selectorate, and the expanding economic reforms have increased the size of the selectorate (1998, 15). Papayoanou and Kastner found that on balance, "top Chinese policy makers will not pursue an aggressive and conflictual foreign policy that could put China's international economic ties at risk. Doing so would undermine their support within the selectorate" (1998, 18). O Neal and Russet came to the same conclusion; IT is working to reduce conflict between the US and China (O Neal, Russett, and Berbaum 2003, 383; 388; telephone conversation with Dr. John O Neal on January 19, 2006).

Summary. In this chapter we looked at the implications of Interdependence Theory for US policy makers in the light of current US and Chinese national security strategies. We found that the Oneal and Russett vision of IT provides the best understanding of IT's impact on dyadic relationships, while we also concluded that Gelpi and Grieco's untested conceptualization of IT provides a warning to policy makers that China may be an exception to IT's conflict-reducing qualities. We warned that US policy makers must remain wary of IT's impact in the United States. We also provided five policy recommendations. We proposed that the US should retain Interdependence or economic engagement as a powerful strategy component. We saw value in the high level of Chinese-Taiwanese Economic Interdependence and urge measures to continue such engagement. We saw a need to improve institutions to resolve trade issues and consider the implications of the evolving nature of US-China trade. We also propose that the US advance mutual membership with China in intergovernmental organizations as a means of advancing the Kantian tripod. Lastly and most importantly, we saw that democracy and Interdependence are mutually supporting legs of the Kantian tripod, since both OR and GG ultimately posit that democracy reduces conflict and that IT is a strong tool for promoting democracy.

CHAPTER 7
CONCLUSIONS
Introduction

The purpose of the research has been to determine the nature of the economic relationship between the United States and China, discern how and how well Interdependence Theory explains this relationship and provide recommendations for US policy makers. We have undertaken this research in a contextual backdrop of increased economic integration between the US and China, the rise of China as a global power and continued opportunities for dyadic conflict over diverging interests in East Asia. In our last chapter, we reintroduce our purpose and research questions to ensure we have addressed the core issues of this research. We also compare our expected findings to our actual conclusions. Lastly, we explore opportunities for further research.

Readdressing the Purpose and Research Questions

Our purpose is to explore the strengths and weaknesses of Interdependence Theory as a framework for weighing the potential for conflict between the US and China. Our approach was designed around three research questions, which we addressed in Chapters 4 to 6.

Our first research question asked: *How and to what degree have the US and China become economically Interdependent?* Here we attempted to gain a ground-truth understanding of US-China economic integration that was both unaided and unencumbered by ONeal and Russett's Interdependence Theory methodology. We found that dyadic integration was both complex and very significant.

Under the Deng reforms, China has remade itself from a command economy into a quasi-market economy, using a state development/laissez faire model. Deng's pragmatic approach to economic reform has led to an embrace of market practices and vastly increased participation in intergovernmental organizations and led to the adoption of global standards of trade. These reforms have continued in the decade following Deng's death, with the entry into the WTO marking a milestone of China's continued commitment to reform and global economic integration. The resulting engagement has transformed China's economy at a frantic rate.

Prior to the 1972 rapprochement between the US and China, there was virtually no dyadic economic relationship. The 1972 opening started the change, but it was not until the Deng reforms of the late 1970s that economic exchanges really began. The results have been remarkable, and China is now the United States' third largest trading partner (Hufbauer and Wong 2004, 3). Furthermore, China has a high level of trade openness, meaning it is also becoming integrated into the world economy. The US maintains a huge trade deficit with China, which is due in part to China's cheap and reliable labor pool and the fact that many countries manufacture goods there. Trade is not the only form of economic exchange, since mutually beneficial capital flows have increased at a fast rate. The US provides China FDI and technology that expands its

industry, while the US gains investment in a growing market. China also invests in the US, by funding its public debt, thereby placing China in the position of relying upon the continued growth of the US economy to guarantee its investments.

Through all of these means and others, the dyad has become economically integrated in ways unaccounted for by the merchandise trade measures used in IT. While Oneal and Russett hold that trade correlates well to the indicators noted above, IT's failure to capture these other types of exchanges may mean the full impact of economic integration is underrepresented by current IT methodology. At the very least, IT methods fail to account for the true nature of Interdependence, although one could forgive the model for failing to do so, since the goal of IT is simply to make a correlation between economic integration and conflict.

Our second research question asked: *How well does IT explain the nature of the relationship between the US and China?* We addressed this question, using the three tests found in Chapter 5. We began by examining the relationship between the two states, using the methods of Oneal and Russett, the chief proponents of Interdependence Theory. Using their measure, merchandise trade, we found results very similar to OR's. The dyad has a very high level of Economic Interdependence. The US is the less constrained member of the dyad, meaning it has more freedom to initiate conflict, since its costs are less, and it has fewer domestic interests pushing for continued trade. OR's data do demonstrate that based upon the current level of Interdependence, the potential for conflict is substantially reduced.

In this section, we also examined the raw data on trade and conflict in the dyad, starting from the notion that such an examination could not be used as a proof of IT's

impact, since IT uses aggregated data from thousands of dyads. The US-China data are somewhat inconclusive, since dyadic conflict is down since the Cold War but has risen in recent years. The data do demonstrate that the *highest level of dyadic conflict* is down in the post-Cold War era. This finding would tend to support the concept that Interdependence does not end conflict per se but suppresses the dyad members from moving their actions to a high level of direct military confrontation, thus preserving the mutually beneficial trade.

In our second test of this research question, we investigated Gelpi and Grieco's assertion that polity type determines whether or not Interdependence reduces conflict, specifically focusing on the presence or absence of democracy. GG hold that China's lack of democracy either reduces or negates IT's conflict-suppressing quality. GG's work may be the most promising advancement of IT that could apply to the China-US case. However, their 2003 findings have not been replicated by others, and their forthcoming article (which would attempt to negate IT's impact in democratic-autocratic dyads) remained unpublished at the time of this research. Furthermore, GG's model may not apply to an autocratic China, since its leaders are trade-dependent, and in a time of crisis, its selectorate will pressure the government to maintain dyad trade.

In our examination of two dyadic events, we attempted to apply our understanding to actual events in the US-China relationship. In the WTO case, we found that IT provided a strong explanation for US motives for letting China into the WTO, while it did not explain China's reasoning. However, IT's strong suit in this case was not in describing past behavior, but in predicting future performance. WTO membership has improved dyadic Interdependence, increased Chinese integration with its neighbors and

expanded China's openness to the world economy. IT predicts that all of these moves will decrease China's drive to take a conflictual approach to other states. The results of the TSC case study were less clear, since we could either speculate that IT impeded China from moving to a higher level of conflict or question why Beijing was willing to risk so much by producing a show of force against Taiwan and the US. The GG subvariant was not useful in these cases, since it remains unknown if the concept applies to China. At the most, GG's concept could inform policy makers that IT's influence on China may be in doubt.

We found that IT is no more flawed than any other major international relations theory. It is best used as a subcomponent of liberalism (or the Kantian tripod) and in conjunction with other theories. IT and liberalism provide a compelling explanation of the international environment, but realism provides a better illustration of power distribution within the system, while only constructivism explained the potential problems stemming from identity and hypernationalism. Lastly, we understand that Interdependence Theory is necessary for explaining the trade-conflict relationship but is not sufficient for predicting state behavior in crises.

Our third question asked: *Given a policy of engagement and increased Interdependence between the US and China, how might US policy makers best optimize the situation?* Our investigations in Chapter 6 found several implications from Interdependence Theory for US policy makers in light of US and Chinese national security strategies that call for high levels of economic integration. Oneal and Russett remain the best source of methodology for the US-China case. As Dr. Oneal reports, twenty-five scholars have published articles which have replicated their findings (as

reported in a telephone conversation with John Oneal, January 19, 2006), while critics have generally remained lone voices against the mainstream of IT. Gelpi and Grieco have produced an intriguing interpretation of IT that remains untested. Policy makers can understand their work as a warning that IT's ability to tamp down conflict may not be in play in the case of China, or they can see GG's work as a compelling reason to ensure China becomes democratic. The final implication looks inward rather than toward Beijing. US policy makers must remain wary of domestic interests (who because of the motivations created by economic integration) may put pressure on the government to act in ways that do not benefit US interests.

Our policy recommendations were mostly supportive of the current US approach to China. We endorsed the long-term policy of broadly engaging China across many policy realms, and we urged that economic engagement remain a strong component of this strategy. We recommended that the US promote Taiwan's continued engagement with China, since IT applies to this dyad and since the US benefits from the resulting decrease in conflict between Taipei and Beijing. Oneal and Russett recognize that trade begets its own low-level conflict, so we acknowledged the need to create further mechanisms to address Sino-American trade differences and to anticipate future challenges in this important economic relationship. Lastly, we urged a redoubling of efforts to promote the other two legs of the Kantian tripod. Joint IGO membership can be further expanded. More importantly, we noted democracy has the most latent potential for reducing conflict between the two states, and the high level of dyadic Interdependence offers a chance for change agents to bring about democracy in China. *A successful*

transition to democracy is important to further reducing dyadic conflict, and IT is an important tool for bringing about democracy in China.

Comparing Expected Findings to Conclusions

Generally, our conclusions are somewhat more upbeat about the uses of IT than the expected results we put forward in Chapter 1. In our expected results, we posited that: IT does not apply in every case, and China may be one of these exceptions; the lack of democracy in China impedes IT's impact; Interdependence's impact is conditioned upon the other legs of the tripod; IT is a useful but incomplete tool for explaining China's behavior in relation to specific cases; and we should expect to see a reduction in armed conflict over the long-term, while lesser, non-militarized disputes will tend to increase. We can address each expected finding in turn:

1. *IT does not apply in every case.* This statement questions whether China is in the majority case; i.e., whether IT has impact in China or does one of the subvariants apply instead. OR have done a fairly thorough job of refuting their critics. As we noted in Chapter 2, they addressed the subvariants presented by Barbieri (trade causes conflict); Mansfield and Snyder (states in transition to democracy are more prone to conflict); and Copeland (Interdependence's influence can be weakened by expectations that trade might change). In the end, only GG's work was both directly related to Interdependence and *not* yet directly refuted by OR. The jury is still out on their findings. While subvariants may ultimately prove exceptions to IT,

Oneal and Russett's methodology, in which Interdependence has impact in all dyads, remains the most proven form of the theory.

2. *The lack of democracy in China impedes IT's impact.* This is essentially GG's argument which we found to be unproven. According to OR, there is no interaction between democracy and Interdependence; they both independently have an impact on conflict. In addition, OR specifically note that China's slight improvement on the Polity scale has already reduced the potential for conflict with the United States.
3. *Interdependence's impact is conditioned upon the other legs of the Kantian tripod.* OR posit that all three legs of the Kantian tripod independently reduce conflict. Increases in the other two legs (democracy and joint IGO membership) will have impact, even if the level of Interdependence remains unchanged. We note that democracy has the most latent potential for reducing dyadic conflict and that IT can provide the exchange of ideas and individuals that may help bring about democracy, but we did not attempt to prove this proposition in this research.
4. *IT is a useful but incomplete tool for explaining China's behavior in relation to specific cases.* We did find IT to be an impractical general theory of international relations, but as part of liberalism, it serves as viable international relations theory. In addition, in the understanding of trade and conflict studies, it is a necessary if not sufficient tool. Oneal and Russett's theory remains the best tool for examining the Sino-American economic relationship. Indeed, understanding the security implications of the economic

relationship between China and the United States cannot be accomplished without Interdependence Theory.

5. *We should expect to see a reduction in armed conflict over the long-term, while lesser, non-militarized disputes will tend to increase.* Oneal and Russett and most other IT researchers agree that economic integration creates its own specific form of disagreements between states. These do not break out into conflict, because the trading states want to maintain mutually beneficial trade. In addition, IT and the other legs of the Kantian tripod lead to the creation of bilateral and multilateral institutions and mechanisms that are designed to prevent disruptions from crossing over into open conflict.

Topics for Future Research

The meaning of Economic Interdependence has changed along with the societies that trade in the international economy. The economic relationship between modern-day America and China is quite different than that between the British and German Empires one hundred years ago when the concept was born. As one example of the difference, China is about three times more dependent upon the United States now than Germany was on Great Britain on the eve of World War I (J.Nathan 2002, 122). In Chapter 4, we spoke to the importance of and prevalence of capital flows and the free movement of labor around the globe. Advances in technology and the advent of the information age have greatly changed the world's economies. Multiple states at very different levels of development may play a role in producing the sophisticated products which consumers

need. The nature of Interdependence has also changed along with the character of societies. In Queen Victoria's day, citizens had low expectations from the state, and they certainly did not believe that the state was responsible for their economic prosperity. As citizens' expectations from the state have grown, the internal dynamics that Gelpi and Grieco spoke to have become more complex. A state with a selectorate that has high expectations of economic goods delivery puts a different degree of pressure on state actors. While Oneal and Russett insist that trade merchandise correlates well with these new economic and societal factors, it is clear that better measures of this variable will produce better understanding of economic integration.

Based upon our research, Interdependence Theory would be best served by the following additional research topics:

1. *Redefine the main independent variable.* Economic Interdependence has expanded far beyond simple merchandise trade. The current standard fails to recognize the potential of much more sophisticated relations in the modern world. Integration is simply a different beast than the merchandise trade that existed in the 1900s when IT was first developed. In that era, sophisticated MNCs did not exist, labor pools were less migratory, and the industrial age ruled rather than the information age. While OR believe merchandise trade is a valid and reliable representation of economic integration, a broader measure is important to identify the nature of Interdependence and track its change over time. As it now stands, IT never truly attempts to measure Economic Interdependence, since such activities as services exchanges, foreign direct investment and capital flows are not accounted for in these studies.

2. *Better understand the interaction of the three legs of the Kantian tripod to understand the true nature of their conflict-reducing qualities.* Many of the subvariants we examined tried to perform this function although the current status of these efforts is quite unclear. Indeed, many of theorists we have discussed are focusing their efforts on better understanding the legs of the tripod. For example, Bruce Russett is developing a typology of IGOs to determine which organizations have the most conflict-reducing qualities (relayed to this researcher in telephone conversations with John Oneal and Bruce Russett on January 19, 2006).
3. *Determine the trade preferences of autocrats.* More research is needed to test Gelpi and Grieco's work on IT and polity type. While GG's general concept may be supportable, it is irrelevant for our case until research can be undertaken to differentiate between autocratic states that prefer trade as a strategy and those that do not. If trading autocrats are constrained in the same manner as trading democracies, then GG's concept has little value in the case of the US-China dyad.
4. *Determine the nature of trade and peace simultaneity.* Most IT researchers argue that *trade increases peace*; they also acknowledge that *peace increases trade*. Peace and trade share simultaneity. The factors interact; trade brings peace and peace brings trade. Some work has been done on this matter, yet most researchers tend to ignore this interaction. Few expect this matter to have a significant impact on Interdependence Theory, since the effect is

clearly weighted in favor of the peace follows trade argument. However, this issue needs to be addressed in order to fully reveal the nature of IT.

Conclusion

Interdependence Theory remains a compelling proposition which has a significant body of work to support its general proposition that increased trade reduces dyadic conflict. Such liberal theories have long informed US foreign policy and are the philosophical foundation upon which the long policy of economic engagement with China is based. Such theory is not without its limitations, as we have noted, and no strategy should rely upon a single proposition. But, policy makers are hobbled in their policy formation, if they fail to consider the power of Interdependence. Indeed, US strategy is multifaceted, relying upon liberal ideas to pull China into the international community, while preparing for the eventuality that China follows a darker course.

Our research strongly indicates that Interdependence Theory is worthy of its place among the small number of propositions that inform America's strategy toward China. A policy that is based upon the notion that economic integration and trade will reduce conflict is not a panacea for the Sino-American relationship. We should not expect to find an easy end to conflict over thorny issues, such as the status of Taiwan, nor should we hope that the US and China will refrain from power struggles over their respective situations in the world. The competition for regional and global position that is inherent in the relationship between the world's superpower and a rising non-status quo power

will naturally bring conflict. Interdependence Theory does hold out the hope that there is reduced potential for such conflicts to move to open warfare.

Since the Deng era, China has gone through remarkable changes that have intertwined its economy with that of the US and the rest of the world. As a consequence, Beijing has adopted market measures for understanding economic matters. Furthermore, the US and China have become dependent upon each other's economy for its own economic well-being. In the years to come, the economies of these two states will become even more interconnected and the relationship more complex. At the same time, we should expect to see a more powerful China emerge. In this coming scenario policy makers are well-advised to employ Interdependence Theory as a tool for both understanding the international environment and forming strategy.

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