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Crafting Payoffs: Strategies and Effectiveness of Economic Statecraft

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CRAFTING PAYOFFS:
STRATEGIES AND EFFECTIVENESS OF ECONOMIC STATECRAFT

Audrye Yunqi Wong

A DISSERTATION
PRESENTED TO THE FACULTY
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Abstract

Economic statecraft – the use of economic tools to pursue political goals – is an important foreign policy strategy for many major powers, and has been an increasingly important tool for China. This book provides a theoretical framework to explain the effectiveness of economic statecraft, focusing on positive inducements, which are understudied relative to sanctions. I argue that effectiveness is influenced by two independent variables: (a) the type of inducement strategy; and (b) the level of public accountability in the target country.

I distinguish between two types of economic inducements: subversive carrots, which circumvent established political processes and institutions; versus stakeholder cultivation, which engages with key domestic actors within established political processes and institutions. In addition, effectiveness depends on the level of public accountability in the target country. Public accountability ensures transparency – via the ability to access information; and exercises oversight – via the ability to impose domestic political costs on elites for policy decisions regarding the sender state.

Testing my theory using the important case of China's economic statecraft, I show that subversive carrots succeed in low accountability countries, but backfire in targets with high public accountability, where it leads to public backlash against China. In contrast, stakeholder cultivation is more likely to succeed in high accountability systems, because it creates domestic political coalitions that are more closely aligned with China's policy preferences.

I draw on evidence from field interviews, case studies, and a survey experiment. Using a mix of cross-country case comparisons, within-case process tracing, and within-country variation in inducement strategy as well as public accountability, I examine the cases of the Philippines, Malaysia, Cambodia, Myanmar,

Australia, and Japan. In addition, I conduct a survey experiment in the Philippines to test the individual-level mechanisms of public accountability.

While this book focuses on China as an important case study, the arguments can be similarly applied to other countries seeking to wield economic statecraft. The findings from this book have important theoretical and policy implications for understanding the conditions under which economic capabilities can be translated into geopolitical influence, and for understanding the role of economic instruments in national security policy.

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Chapter 1

Introduction: Economic Tools and Geopolitical Influence

Economic statecraft is a common foreign policy tool for major powers. In recent years, the United States has imposed sanctions on countries such as North Korea and Iran, in an effort to alter their foreign policy behavior. Russia has threatened to cut off energy supplies to keep Eastern European countries in line. Economic statecraft can also take the form of positive inducements. The Marshall Plan is a prominent example of how Washington used economic assistance as part of a strategy to counter the threat of communism in Europe. West Germany used a mix of trade, investment, and financial incentives to shape its relations with Poland and the Soviet Union and promote German reunification.

Economic statecraft is also an increasingly important tool for a rising China. It has been employed more often as China has wielded more clout in the Asia-Pacific region and in the global economy. From foreign investment in Africa and Latin America to its ambitious Belt and Road Initiative spanning from Central to Southeast Asia, China's expanding economic presence has sparked concerns among policymakers and scholars over Beijing's growing geopolitical influence. Implicit in many analyses is the assumption that China's economic capabilities have enabled Beijing to persuade, punish, or buy over countries to support China's foreign policy interests.

However, the empirical record points to a mixed record of success. China's efforts to increase its economic and political influence have at times been welcomed but have also often sparked resistance from a

range of actors and countries.[1] Although Beijing has provided extensive investment and aid to countries in Southeast Asia, this has not prevented tensions from flaring up over sovereignty disputes in the South China Sea. Countries such as Malaysia, Sri Lanka, and Pakistan are also pushing back against China's economic presence. What determines the political effectiveness of economic statecraft?

In this book, I seek to explain the conditions under which economic capabilities can actually translate into political influence. Most existing literature has focused on punishments via economic sanctions. Economic inducements, on the other hand, have been relatively understudied. They entail the provision of economic benefits or incentives to a target country, such as increased trade, investment, or foreign aid. Focusing on positive inducements, I develop a theory on how the effectiveness of economic statecraft is influenced by the interaction of two independent variables: (a) the type of inducement strategy; and (b) the level of public accountability in the target country.

I distinguish between two types of economic inducements: subversive carrots, in which the provision of economic benefits works outside of established political processes and violate expected political standards; versus stakeholder cultivation, which entails engagement with key domestic actors and interest groups within established political processes and institutions. I argue that the effectiveness of economic statecraft is conditional on the level of public accountability in the target country. Public accountability is defined as the presence of robust societal institutions, such as the media, civil society, and public opinion. In an environment of high public accountability, these societal institutions can demand transparency – via the freedom and ability to access information; and exercise oversight – via the ability to impose domestic political costs on political leaders and elites for policy decisions regarding the sender state. In short, under high public accountability, political elites view themselves as being constrained by, and needing to respond to, public opinion, thus limiting government policy maneuverability.

Drawing on field interviews and survey experimental evidence, I examine the important case of China as a wielder of economic statecraft. I show that the use of subversive carrots is effective in low accountability countries, but has limited political effectiveness in targets with high public accountability, where

1. Andrew J. Nathan, "China's influence and the pushback: Tentative conclusions beyond Hong Kong and Taiwan" (January 12, 2019).

it leads to public backlash against China. On the other hand, stakeholder cultivation is more likely to succeed in high accountability systems, because it engages with pivotal actors in the target country's political system to create domestic political coalitions that are more closely aligned with China's policy preferences. I test my theory across a range of target country cases, including four Southeast Asian countries with varying levels of public accountability - Cambodia, the Philippines, Malaysia, and Myanmar - and two high accountability countries who received different inducement strategies - Australia and Japan. In addition, to test the mechanism of public accountability, I conduct a survey experiment in the Philippines.

Economic interdependence and integration has limited the scope of military solutions in international relations, while opening up new avenues for the manipulation of economic relations for geopolitical purposes. As China becomes more prominent on the international stage, it will have to decide how to reconcile the tensions between strategic reassurance – using economics as soft power – and employing statecraft for its political goals – using economics as a hard form of power. While this article focuses on China, the theoretical framework can be similarly applied to other countries seeking to wield economic statecraft.

My research helps to address an important question in international security and foreign policy: the conditions under which material capabilities can translate into actual political influence. I make new theoretical contributions by examining the conditions required for economic statecraft to be effective, in particular the role of domestic political institutions and processes in target countries. In addition, my findings help policymakers to understand the ways through which states can or cannot use economic tools to alter other countries' foreign policy behavior, and to better assess the geopolitical impacts of China's overseas economic activities. My findings highlight the importance of domestic political conditions in target countries, contribute to understanding the conditions under which economic capabilities can be translated into political influence, and help policymakers evaluate the geopolitical impacts of China's overseas economic activities.

Plan of the Book

In this chapter, I have laid out the trajectory of China's economic statecraft, existing theoretical discussions of economic statecraft more broadly, and my theoretical framework to examine the effectiveness of economic statecraft. The remainder of the book is focused on testing my theory, drawing on a range of data gathered from fieldwork over the last four years: interviews with scholars, government officials and policymakers, and journalists in several countries in the Asia-Pacific; a survey experiment in the Philippines; and data on public opinion as well as Chinese aid.

The first two empirical chapters process trace the drivers and mechanisms of public and elite response to China's economic statecraft, in particular subversive carrots. Chapter 3 shows how Beijing's attempts to entice Philippine politicians to alter existing policies on the South China Sea using subversive carrots led to a strong backfiring effect. Projects were halted and political leaders bowed to public pressure. It also shows how the issue of procedural violation – that inducements did not adhere to domestic political processes and institutions – was the dominant driver of the Philippine response, as opposed to the potential rival explanation of bilateral security tensions.

In Chapter 4, I examine China's use of subversive carrots and stakeholder cultivation in Malaysia. Again, subversive carrots in the form of corrupt, non-transparent investment projects met with public backlash, electoral change, and project cancelation or renegotiation. However, other Chinese investments that adopted a stakeholder cultivation approach were successful in maintaining political support. Together, the Malaysia and Philippines chapters serve as complementary case studies for the mechanism of backlash against China's subversive carrots that operates consistently across a range of potential confounders, even in developing and imperfect democracies.

Next, to provide evidence for the individual-level mechanisms of my theoretical argument, I present in Chapter 5 results from an online survey experiment in the Philippines, showing how subversive carrots soured public attitudes toward China and reduced support for cooperation with China, whereas stakeholder cultivation had opposite and positive effects. The findings confirm that the manner in which economic statecraft is carried out – whether there is procedural violation or not – has significant effects

on attitudes and policies in recipient countries where accountability mechanisms are present.

Chapter 6 focuses on the political outcomes of different inducement strategies in a low public accountability country, Cambodia. I show how Cambodian leaders accepted subversive carrots and supported Beijing's positions in the South China Sea. In contrast, U.S. and Japanese stakeholder cultivation through foreign aid in Cambodia has failed at gaining political influence among ruling elites. The use of subversive carrots over time has also served to entrench existing elites and further weaken accountability institutions, thus creating a vicious cycle. However, unexpected domestic political changes can alter the political payoffs for China. In the last section of Chapter 6, I examine within-country variation in public accountability in another Southeast Asian country, Myanmar. A domestic political transition from the military junta to a more democratically-elected form of government has made leaders more responsive to public opinion, decreasing the effectiveness of subversive carrots and pushing China toward a stakeholder cultivation strategy.

Chapters 7 and 8 together present a paired case study of two high accountability countries outside of Southeast Asia, Australia and Japan, showing how subversive carrots backfire but stakeholder cultivation succeeds. In Australia (Chapter 7), China's use of subversive political donations and academic funding, in an attempt to co-opt public voices and alter politicians' foreign policy positions generated a strong public backlash against China. At the same time, broader stakeholder cultivation through growing economic interdependence has coopted certain domestic voices and buffered some of the backlash, although the reputational costs of subversive carrots have facilitated longer-term politicization of China's economic statecraft.

Chapter 8 turns to a case outside of the contemporary period, to test the external validity of my theory in another time context. I look at Japan during the 1950s to 1970s, when China's use of stakeholder cultivation strengthened domestic political coalitions – including politicians and businessmen – who lobbied in favor of diplomatic normalization with the Mainland over Taiwan. The Australia and Japan case studies further demonstrate how the choice of inducement strategy can lead to very different political payoffs, particularly in high accountability target countries.

In Chapter 9, I discuss the scope conditions and generalizability of my theory. Overwhelming national security concerns are likely to constrain the effectiveness of economic statecraft – or any other foreign policy tool – as in the case of Taiwan, thus imposing a scope condition for my theory. Nonetheless, recent cases of recipient country responses to Chinese investment have been in line with the predictions of my theory, such as Sri Lanka, the Maldives, and Pakistan, pointing to strong external validity outside of the Asia-Pacific. I apply my theory to understanding the evolution of China's economic statecraft, the current issues faced by Beijing, including the context of its ambitious Belt and Road Initiative. Finally, I draw out the policy implications for understanding and responding to China's use of economic statecraft.

Chapter 2

Theoretical Framework

There are many tools of economic statecraft, such as trade, investment, aid, or monetary policy. These tools can be used in two different approaches: a negative approach – through the application of coercive pressure – or a positive approach – through the provision of incentives. Negative economic sanctions involve the sender state's withdrawal of economic benefits from the target, such as restricting imports from that country, reducing exports to that country, or reducing foreign direct investment into that country. Inflicting economic pain pressures the target to change its foreign policy to suit the sender's preferences. In contrast, positive economic inducements involve "the provision or promise of economic benefits to induce changes in the behavior of a target state".[1] This can include increased bilateral trade or investment, or greater flows of foreign aid to the target.

Hirschman discusses how asymmetrical trade relations endows one country with more coercive power over the other, because the latter will be more vulnerable to an interruption of trade.[2] This method of economic coercion could "become an alternative to war" and "an effective weapon in the struggle for power" between sovereign states.[3] Building on this idea, political science and IR scholarship has largely

1. Michael Mastanduno, "Economic Statecraft, Interdependence, and National Security: Agendas for Research," in *Power and the Purse - Economic Statecraft, Interdependence, and National Security*, ed. Jean-Marc F Blanchard, Edward D Mansfield, and Norrin M Ripsman (London: Frank Cass, 2000), 303.

2. Albert O Hirschman, *National Power and the Structure of Foreign Trade*, vol. 105 (Berkeley, Los Angeles, London: Univ of California Press, 1945).

3. Ibid., 15-17.

focused on punitive sanctions as the dominant approach to economic statecraft.[4,5]

However, economic inducements have been employed by a broad range of countries, including the United States and West Germany.[6] Beyond providing potential coercive leverage, enhancing a target country's gains from deeper economic exchanges can serve as a direct means of influence.[7] Although positive inducements are a key component of economic statecraft, there are few theoretical frameworks to understand their success or failure.

China has also received increasing attention as a source of economic statecraft. Scholars have examined the domestic drivers of Beijing's ability to wield economic statecraft.[8] Other studies have focused on the potential coercive effects of trade dependence on China, such as import or export restrictions,[9] and whether economic interdependence with China makes countries more likely to support Beijing's positions on political and security issues.[10] This leaves open the question of China's use of economic inducements and when they are effective at achieving political outcomes.

4. David A Baldwin, "The Power of Positive Sanctions," *World Politics* 24, no. 01 (1971): 19–38; David Allen Baldwin, *Economic Statecraft* (Princeton, NJ: Princeton University Press, 1985); Robert A Pape, "Why Economic Sanctions Do Not Work," *International Security* 22, no. 2 (1997): 90–136; Daniel W Drezner, *The Sanctions Paradox: Economic Statecraft and International Relations*, 65 (Cambridge, UK: Cambridge University Press, 1999).

5. For a criticism of this trend, see Baldwin, "The Power of Positive Sanctions"; David A Baldwin, *Power and international relations: A conceptual approach* (Princeton University Press, 2016).

6. William J Long, "Trade and Technology Incentives and Bilateral Cooperation," *International Studies Quarterly* 40, no. 1 (1996): 77–106; Dale C Copeland, "Trade Expectations and the Outbreak of Peace: Détente 1970–74 and the End of the Cold War 1985–91," *Security Studies* 9, nos. 1-2 (1999): 15–58; Patricia Annette Davis, *The Art of Economic Persuasion: Positive Incentives and German Economic Diplomacy* (Ann Arbor, MI: University of Michigan Press, 1999); Rawi Abdelal and Jonathan Kirshner, "Strategy, Economic Relations, and the Definition of National Interests," in *Power and the Purse - Economic Statecraft, Interdependence, and National Security*, ed. Jean-Marc F Blanchard, Edward D Mansfield, and Norrin M Ripsman (London: Frank Cass, 2000), 119–156; Lars S Skålnes, *Politics, Markets, and Grand Strategy: Foreign Economic Policies as Strategic Instruments* (Ann Arbor, MI: University of Michigan Press, 2000); Randall E Newnham, *Deutsche Mark Diplomacy: Positive Economic Sanctions in German-Russian Relations* (University Park, PA: Pennsylvania State University Press, 2002).

7. Baldwin, *Economic Statecraft*, 213.

8. William J. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control* (Ithaca, NY: Cornell University Press, 2016).

9. Andreas Fuchs and Nils-Hendrik Klann, "Paying a Visit: The Dalai Lama Effect on International Trade," *Journal of International Economics* 91, no. 1 (2013): 164–177; Christina Davis, Andreas Fuchs, and Kristina Johnson, "State Control and the Effects of Foreign Relations on Bilateral Trade," *University of Heidelberg Department of Economics Discussion Paper Series*, no. 576 (2014).

10. Gustavo A Flores-Macías and Sarah E Kreps, "The Foreign Policy Consequences of Trade: China's Commercial Relations with Africa and Latin America, 1992–2006," *The Journal of Politics* 75, no. 02 (2013): 357–371; Scott L Kastner, "Buying Influence? Assessing the Political Effects of China's International Trade," *Journal of Conflict Resolution* 60, no. 6 (2014): 980–1007.

Inducements versus Coercion

Some may view economic rewards as simply the flip side of economic punishments – that political power derives from the implicit threat of pain caused by the withdrawal of existing benefits. Positive inducements create dependency, particularly when the relationship is asymmetric, which then leads to coercive leverage in the future.[11] Relatedly, Chinese scholars have argued that using inducements and punishments in tandem will highlight to other countries their potential losses and make inducements more "precious" – as a Chinese saying goes, strength requires benevolence, but benevolence is displayed by showing strength.[12]

However, the threat caused by dependency stems from a readjusted baseline of expectations in the longer run – after the acceptance of inducements – suggesting that this is a valid future threat of coercion but distinct from the act of providing positive inducements. Thus, it is important to distinguish between positive inducements and negative sanctions, as they produce different behavioral and policy implications, such as the conditions of usage and efficacy, psychological impacts and policy responses of the target state, and longer-term political interactions.[13] While acknowledging the latent coercive potential of inducements, in this book I focus on the immediate responses of target countries to the benefits provided by such inducements.

What are the possible benefits of using incentives instead of sanctions? Positive inducements to entice dissenters to align their policies with that of China could avoid the so-called sanctions paradox,[14] in which countries expect future conflict and hence make only minimal concessions, reducing the effectiveness of economic sanctions. Whereas economic coercion sparks resentment and resistance in target countries, economic incentives can promote goodwill and cooperation, while also benefiting commercial actors in the sender state.[15]

11. Hirschman1980; Kirshner1995.
12. Guoyou Song, "Zhongguo zhoubian jingji waijiao: jizhi xietiao yu zhengce xuanze (China's Peripheral Economic Diplomacy: Coordination of Mechanisms and Policy Choices)," *Guoji wenti yanjiu*, no. 2 (2014): 41–52.
13. Baldwin, "The Power of Positive Sanctions."
14. Drezner, *The Sanctions Paradox: Economic Statecraft and International Relations*.
15. Mastanduno, "Economic Statecraft, Interdependence, and National Security: Agendas for Research," 309.

In addition, WTO rules and interdependent global production networks make punitive trade restrictions harder to implement without leading to adverse reciprocal effects on the initiating state.[16] Acquiring a bad reputation for using coercive economic tactics would also potentially affect the sender state's economy and leverage in future economic exchanges. Target countries can diversify their markets, turning to other countries for goods and capital, assuming they are relatively substitutable. For example, Beijing's restrictions on exports of rare earth minerals to Japan, after the latter government bought the disputed Senkaku/Diaoyu islands, spurred Tokyo to seek other sources of rare earth imports. Moreover, carrots such as FDI and infrastructure-building projects can be sustained longer and have longer-term effects on target countries than trade restrictions or sanctions. For example, reductions in Chinese exports to countries that have had high-level political meetings with the Dalai Lama were only temporary and disappeared by the second year.[17]

On the other hand, economic carrots tend to be costly, subject the sender state to potential pressure to offer similar incentives to future target countries, and adversely affect reputation for future conflict.[18] Thus, negative sanctions are more cost-effective, because they are costless when they succeed. Yet, this could suggest that inducements are more likely to be used when the sender state thinks it has lower chances of success.[19]

When does economic statecraft work?

Economic capabilities may not always translate into actual influence over policy outcomes. Despite its economic power, China has had limited success in prevailing over opposed policy preferences of Southeast Asian countries.[20] During the Cold War, several of Beijing's attempts to build political alliances via economic inducements eventually fell apart, whether with larger powers, the Soviet Union, or smaller

16. Christina L Davis and Sophie Meunier, "Business as Usual? Economic Responses to Political Tensions," *American Journal of Political Science* 55, no. 3 (2011): 628–646.

17. Fuchs and Klann, "Paying a Visit: The Dalai Lama Effect on International Trade."

18. Daniel W Drezner, "The Trouble with Carrots: Transaction Costs, Conflict Expectations, and Economic Inducements," *Security Studies* 9, nos. 1–2 (1999): 188–218.

19. Baldwin, "The Power of Positive Sanctions."

20. Evelyn Goh, "The Modes of China's Influence: Cases from Southeast Asia," *Asian Survey* 54, no. 5 (2014): 825–848.

states such as Albania, North Vietnam, and Mongolia.[21] In the contemporary Asia-Pacific context, China has not been able to fundamentally exploit economic interdependence as a source of coercive power, because in many cases disrupting bilateral economic ties also imposes high costs on Chinese interests.[22]

There has been a longstanding debate on the effectiveness of economic statecraft, especially sanctions.[23] Building on initial discussions of whether sanctions work, the debate has increasingly focused on understanding when and how sanctions work, and pinpointing specific mechanisms and conditions for success.[24] Research has considered the role of international or structural factors.[25] Other scholarship has examined supply-side factors in the sender state, such as state control of commercial actors[26] and domestic institutional structures.[27] Even in authoritarian regimes such as China, the government's ability to direct the behavior of business actors affects its use and implementation of economic statecraft.[28] Domestic institutional structure, in particular an autonomous coordinated bureaucracy with good state-business relations and the power to reward private economic actors for following political/strategic objectives, affects a sender state's ability to provide sustained, effective inducements.[29]

Turning to the domestic political picture in target countries, it is important to disaggregate states into subnational actors, in order to understand the microfoundations of how statecraft works.[30] Scholars have

21. Shu Guang Zhang, *Beijing's Economic Statecraft During the Cold War, 1949-1991* (Washington, DC: Woodrow Wilson Center Press / Johns Hopkins University Press, 2014).

22. Darren J. Lim, "Coercive Economic Diplomacy: Power, Interdependence and Statecraft in Asia," chap. 1 (Introduction) (Unpublished manuscript, 2016).

23. Pape, "Why Economic Sanctions Do Not Work"; David A Baldwin and Robert A Pape, "Evaluating Economic Sanctions," *International Security* 23, no. 2 (1998): 189–198.

24. Baldwin, *Economic Statecraft*; Jonathan Kirshner, "The Microfoundations of Economic Sanctions," *Security Studies* 6, no. 3 (1997): 32–64; David A Baldwin, "The Sanctions Debate and the Logic of Choice," *International Security* 24, no. 3 (1999): 80–107; David M Rowe, *Manipulating the Market: Understanding Economic Sanctions, Institutional Change, and the Political Unity of White Rhodesia* (University of Michigan Press, 2001); Jonathan Kirshner, "Review Essay: Economic Sanctions: The State of the Art," *Security Studies* 11, no. 4 (2002): 160–179.

25. Drezner, "The Trouble with Carrots: Transaction Costs, Conflict Expectations, and Economic Inducements"; Drezner, *The Sanctions Paradox: Economic Statecraft and International Relations*; Adrian U-Jin Ang and Dursun Peksen, "When do Eonomic Sanctions Work? Asymmetric Perceptions, Issue Salience, and Outcomes," *Political Research Quarterly* 60, no. 1 (2007): 135–145; David Cortright and George Lopez, eds., *Smart Sanctions* (New York, NY: Rowman / Littlefield, 2002); Bryan Early, *Busted Sanctions: Explaining Why Economic Sanctions Fail* (Stanford, CA: Stanford University Press, 2015); Lim, "Coercive Economic Diplomacy: Power, Interdependence and Statecraft in Asia."

26. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*.

27. Davis, *The Art of Economic Persuasion: Positive Incentives and German Economic Diplomacy*.

28. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*.

29. Davis, *The Art of Economic Persuasion: Positive Incentives and German Economic Diplomacy*.

30. Kirshner, "The Microfoundations of Economic Sanctions"; Rowe, *Manipulating the Market: Understanding Economic*

looked at regime type,[31] state capacity,[32] domestic institutions and actors,[33] and regime instability.[34] For example, some argue that comprehensive sanctions against democracies are more likely to succeed while targeted sanctions work better for autocracies.[35] On the other hand, transactional carrots may be more effective between democracies due to credible commitments.[36] Others find that institutional avenues and internationalist economic interests make broad inducements more effective,[37] while domestic instability can also push the targeted regime to respond to inducements.[38] In addition, the outcomes of economic statecraft can be influenced by the interaction between international strategic threats and domestic state capacity.[39]

In this book, I examine the specific characteristics of the target's domestic political processes in determining the effectiveness of economic statecraft. The political impact of economic statecraft, and hence its success, will be mediated by political constraints faced by elites in the target country, in particular the level of public accountability. How accountable, transparent, and responsive political elites have to be to the citizenry ultimately affects the political outcomes of economic inducements. This theory highlights the role of public opinion and domestic political institutions in influencing the varying effectiveness of economic statecraft across different target countries.

Sanctions, Institutional Change, and the Political Unity of White Rhodesia; Kirshner, "Review Essay: Economic Sanctions: The State of the Art."

31. Risa A Brooks, "Sanctions and Regime Type: What Works, and When?," *Security Studies* 11, no. 4 (2002): 1–50; Miles Kahler and Scott L Kastner, "Strategic Uses of Economic Interdependence: Engagement Policies on the Korean Peninsula and Across the Taiwan Strait," *Journal of Peace Research* 43, no. 5 (2006): 523–541.

32. Jean-Marc F Blanchard and Norrin M Ripsman, *Economic Statecraft and Foreign Policy: Sanctions, Incentives, and Target State Calculations* (London and New York: Routledge, 2013).

33. Kahler and Kastner, "Strategic Uses of Economic Interdependence: Engagement Policies on the Korean Peninsula and Across the Taiwan Strait"; Scott L Kastner, "When do Conflicting Political Relations Affect International Trade?," *Journal of Conflict Resolution* 51, no. 4 (2007): 664–688; Paul Papayoanou and Scott Kastner, "Sleeping with the (Potential) Enemy: Assessing the U.S. Policy of Engagement with China," in *Power and the Purse - Economic Statecraft, Interdependence, and National Security*, ed. Jean-Marc F Blanchard, Edward D Mansfield, and Norrin M Ripsman (London: Frank Cass, 2000), 157–187.

34. Miroslav Nincic, *The logic of positive engagement* (Cornell University Press, 2011).

35. Brooks, "Sanctions and Regime Type: What Works, and When?"

36. Drezner, "The Trouble with Carrots: Transaction Costs, Conflict Expectations, and Economic Inducements."

37. Kahler and Kastner, "Strategic Uses of Economic Interdependence: Engagement Policies on the Korean Peninsula and Across the Taiwan Strait"; Kastner, "When do Conflicting Political Relations Affect International Trade?"; Papayoanou and Kastner, "Sleeping with the (Potential) Enemy: Assessing the U.S. Policy of Engagement with China."

38. Nincic, *The logic of positive engagement*.

39. Blanchard and Ripsman, *Economic Statecraft and Foreign Policy: Sanctions, Incentives, and Target State Calculations*.

Theoretical Framework: The Effectiveness of Economic Statecraft

In this section, I present a theory on how the effectiveness of economic statecraft is influenced by the interaction of two independent variables: (a) the type of inducement strategy; and (b) the level of public accountability in the target country. This framework considers variation in both the characteristics of the inducements and the characteristics of the recipient. I refer to countries exercising economic statecraft as sender states, and countries on the receiving end as target or recipient states.

Measuring the effectiveness of economic statecraft, especially across a large number of countries, can be challenging.[40] There can be multiple possible policy objectives, differing costs for sender and target, as well as differing stakes and issue contexts. For example, policy change on an issue that involves the target's key national interests would be more difficult than maintaining neutrality in a less vested target country. Structural factors such as trade dependence, existing alliance relationships, or the availability of alternate sources of inducements, can influence the target state's policy calculations. Success and failure can also be evaluated in comparison with the alternative foreign policy instruments available.

I define effectiveness as the attainment of the sender state's policy goals i.e. when economic statecraft achieves a desired change in the target state's behavior to align more closely with the sender's foreign policy preferences. This change would not have occurred without the sender's provision of economic inducements. A government policy change by the target country, in alignment with the sender's intentions, would be the most direct and obvious example of a political outcome. In addition, public statements by political leaders reflect changes in elite attitudes, with resulting implications for foreign policy. Finally, the valence of public opinion regarding the sender state and policy cooperation serves as an intermediary mechanism, reflecting success or failure, particularly in high accountability countries where elites have to respond to public sentiment.

40. Baldwin, "The Sanctions Debate and the Logic of Choice"; David A Baldwin, "Success and Failure in Foreign Policy," *Annual Review of Political Science* 3, no. 1 (2000): 167–182; Baldwin, *Power and international relations: A conceptual approach*.

Types of inducement strategies

Previous works have broadly differentiated economic inducements into two categories: instrumental political conditionality, and broader structural engagement.[41] Focusing on the impact of economic inducements on the domestic politics of the target country, I categorize inducement strategies based on their adherence to established political norms and institutions.

First, inducements can be *subversive carrots*, in which the benefits provided by the sender state violate political and institutional standards such as transparency and rule of law. Subversive carrots thus operate outside of – and actively undermine – usual political processes. For example, they can entail the use of corruption (e.g. bribes or kickbacks) or non-transparent economic incentives through covert proxies, with the aim of buying over political leaders' support for the sender state's policy preferences. Indeed, research has suggested that Chinese aid in Africa has increased local corruption rather than boosting short-term local economic activities.[42] Carrots could also bypass institutional procedures, such as competitive bidding processes or regulatory approval. As such, subversive carrots will often see inflated costs, limited economic benefits especially for the local populations, and other negative externalities such as forced displacement and environmental degradation. Subversive carrots tend to be transactional in nature, whereby the provision of economic benefits comes with expectations for specific political outcomes, such as a public statement aligning with the sender's interests or a desired policy change of the target state.

Alternatively, inducements can take the form of *stakeholder cultivation*, which adheres to established political processes and institutions. Economic benefits are provided in a transparent and legitimate manner to key interest groups and actors, in accordance with required institutional and regulatory procedures. Such domestic actors form a lobbying coalition that is more aligned with the sender government's preferences, serving to transmit these preferences to political leaders.[43] This creates a more favorable political

41. Mastanduno, "Economic Statecraft, Interdependence, and National Security: Agendas for Research"; Newnham, *Deutsche Mark Diplomacy: Positive Economic Sanctions in German-Russian Relations*; Nincic, *The logic of positive engagement*.

42. Ann-Sofie Isaksson and Andreas Kotsadam, "Chinese aid and local corruption," *Journal of Public Economics*, no. 159 (2018): 146–159.

43. Jonathan Kirshner, *Currency and Coercion: the Political Economy of International Monetary Power* (Princeton, NJ: Princeton University Press, 1997); Abdelal and Kirshner, "Strategy, Economic Relations, and the Definition of National In-

environment that incorporates the sender's interests. In the words of Hirschman, these interest groups form a "commercial fifth column" that "exert a powerful influence in favor of a 'friendly' attitude toward the state to the imports of which they owe their existence".[44] Stakeholder cultivation operates by strengthening and mobilizing interest groups in the target country, similar to how domestic coalitions and sectoral interests shape a country's foreign policy and grand strategy.[45] The sender state works within existing political processes and institutions to alter the balance of domestic political interests in the target country in favor of the sender's policy positions.

Economic inducements can take many forms, such as foreign aid with direct grants or concessionary loans, investment projects (e.g. infrastructure construction) based on commercial loans, and trade subsidies or preferential market access for certain products. Regardless of the vehicle through which economic benefits are provided, they can be categorized under one of the above types of inducement strategies, depending on how the vehicle is being used. For instance, aid or investment would be considered subversive carrots if they involved backdoor corruption, but would be considered stakeholder cultivation if they followed transparent regulatory approval processes. My theory argues that this particular characteristic of inducements - whether they adhere to or violate established political processes and institutions in the target country - is important in shaping public response and political effectiveness. Table 2.1 summarizes the attributes of these two inducement strategies.

The role of public accountability

The two strategies of economic inducements discussed above - subversive versus stakeholder - can produce varying results across political systems. The sender's mere economic presence in a target country does not ensure a corresponding increase in political clout. Instead, the effects of such economic capabilities are first mediated by the target country's domestic economic and political institutions.

terests."

44. Hirschman, *National Power and the Structure of Foreign Trade*, 29.

45. Etel Solingen, *Regional Orders at Century's Dawn: Global and Domestic Influences on Grand Strategy* (Princeton, NJ: Princeton University Press, 1998); Kevin Narizny, *The Political Economy of Grand Strategy* (Ithaca and London: Cornell University Press, 2007); Christina L Davis, "Linkage Diplomacy: Economic and Security Bargaining in the Anglo-Japanese Alliance, 1902–23," *International Security* 33, no. 3 (2009): 143–179.

	Subversive Carrots	Stakeholder Cultivation
Description	Inducements operate outside of established political processes and violate institutional standards	Inducements work within established political processes and adhere to institutional standards
Corruption	Present: bribes and kickbacks	Absent: no bribes and kickbacks
Process	Bypasses required regulatory and institutional procedures	Follows required regulatory and institutional procedures
Benefits	Benefits small group of elites in power	Benefits broader range of domestic actors

Table 2.1: Comparison of inducement strategies and observable implications

I argue below that the level of public accountability in the target country is an important condition for when which kinds of inducement strategies succeed. I note a distinction between public accountability and regime type. While high public accountability may be correlated with the presence of a liberal democracy, regime type encompasses a broad range of attributes. The variable of public accountability provides a more precise explanation for the mechanisms by which economic inducements can be translated into political influence in the target country. In addition, there is often a wide variation within democracies and within autocracies of how the state interacts with and manages societal and economic actors,[46] as well as the domestic political incentives shaping how politicians respond to citizenry demands, with implications for foreign policy outcomes.[47] Public accountability influences the outcome of economic inducements by shaping how they interact with domestic political processes in the target country.

My theory explains how the effectiveness of economic statecraft is conditional on the nature of public accountability in the target country. Public accountability is defined as the presence of robust societal institutions, such as the media, civil society, and public opinion. In an environment of high public accountability, these societal institutions can ensure *transparency* – via the freedom and ability to access

46. Barbara Geddes, "What Do We Know About Democratization After Twenty Years?," *Annual Review of Political Science* 2, no. 1 (1999): 115–144.

47. Jessica L Weeks, "Autocratic Audience Costs: Regime Type and Signaling Resolve," *International Organization* 62, no. 01 (2008): 35–64; Vipin Narang and Paul Staniland, "Democratic Accountability and Foreign Security Policy: Theory and Evidence from India," *Security Studies*, 2018, 1–38.

information; and exercise *oversight* – via the ability to impose domestic political costs on political leaders and elites for policy decisions regarding the sender state. In short, under situations of high public accountability, political elites view themselves as being constrained by and needing to respond to public opinion, thus limiting government policy maneuverability. While public accountability can be considered to vary on a spectrum, for simplicity I discuss below the two ideal types of high and low accountability systems.

High Public Accountability

In a country with high public accountability, greater transparency and availability of information allows oversight by the media, public, and civil society. Research has pointed to the role of press freedom and citizen information in curbing political corruption.[48] As a result, subversive carrots that constitute below-the-table transactions and operate outside accepted political processes and institutions, such as bribes or covert political campaign financing, are likely to be uncovered and criticized. High public accountability enables visibility and transparency about the policy decisions and actions of political leaders. Via media coverage and open political debate, the public is exposed to information about backdoor deals with the sender state. As a result, while such carrots may work in the short-term on changing the policy stances of individual politicians, they tend to elicit public backlash and widespread criticism from the political opposition.

In addition, high public accountability provides oversight via public pressure and institutional constraints on political leaders. The presence of domestic political costs thus reduces opportunities for – and the legitimacy of – direct rent-seeking by political leaders, and constrains policy decisions regarding the sender state. For example, negative public opinion forces politicians to back away from closer cooperation with the sender. As a result, we observe negative impacts on public perceptions of and foreign policy cooperation toward the sender state.

The backlash mechanism of high public accountability means that there may be a time lag between

48. Aymo Brunetti and Beatrice Weder, "A free press is bad news for corruption," *Journal of Public economics* 87, no. 7 (2003): 1801–1824; Alicia Adsera, Carles Boix, and Mark Payne, "Are you being served? Political accountability and quality of government," *The Journal of Law, Economics, and Organization* 19, no. 2 (2003): 445–490.

the offering of the inducement through backdoor means and the subsequent political fallout after the public becomes aware. Information about subversive carrots can be uncovered through journalistic investigations, government leaks and whistleblowers, or civil society activism. Open societal debate further mobilizes negative public opinion. In countries with electoral cycles, this means that the contentious issues of subversive carrots is easily politicized by the political opposition against the sitting government, or even by figures within the ruling party against the incumbent leader. Thus, while subversive carrots may sometimes appear to be successful in buying certain individuals off in the short run, the nature of public information as well as oversight and punishment mechanisms in a high accountability system causes eventual political blowback in the medium and long term.

Under conditions of high public accountability, successful economic statecraft requires a strategy of stakeholder cultivation, which engages with a broader set of commercial and public interests. When interacting with firms, politicians, or the public, inducements should be in accordance with regulatory procedures and political processes. Because inducements are transparent and above board, public opinion also becomes more positive toward the sender state. Stakeholder cultivation creates broader and deeper vested interests committed to maintaining a positive relationship with the sender state, forming a domestic political coalition that lobbies for supporting sender's policy preferences, ultimately altering the balance of political interests in the target in favor of more cooperative relations with Beijing.[49] In the longer run, and more subtly, this could arguably reconfigure the target's perceived national interests to accord more closely with those of the sender state.

Low Public Accountability

In contrast, in a country with low public accountability, the sender state can rely on providing subversive carrots to top political leaders as well as crony, politically-connected business actors who control large portions of the economy and also hold key political sway over the policymaking process. Carrots promising specific benefits in exchange for a desired political outcome are more easily agreed upon and executed by

49. Solingen, *Regional Orders at Century's Dawn: Global and Domestic Influences on Grand Strategy*; Kahler and Kastner, "Strategic Uses of Economic Interdependence: Engagement Policies on the Korean Peninsula and Across the Taiwan Strait."

the political-business elite, likely in a non-public and non-transparent manner. Rents such as kickbacks or bribes will reach political leaders more quickly and directly, without the ability for public opinion, media, or societal institutions to acquire sufficient information or exercise due oversight and punishment (and any critical voices can be easily suppressed). That is, political leaders calling the shots on foreign policy toward China face far fewer constraints in operating outside political norms and institutions.

On the flip side, in a low accountability political system, there are fewer opportunities for stakeholder cultivation to successfully reconfigure domestic economic and political interests, since a small circle of political elites maintain dominant control and societal interest groups do not have pivotal influence. While material benefits may reach other domestic actors, such as the broader public, they lack political influence. In fact, adhering to transparent or legitimate political standards would likely disadvantage the use of stakeholder cultivation since benefits do not flow directly to elites in power, who have a strong incentive in directly receiving and keeping any goods for themselves. Thus, stakeholder cultivation would be a costly and inefficient strategy in low accountability systems. This makes subversive carrots an easier and more efficient strategy for China to buy political influence and achieve specific, immediate policy outcomes.

At the same time, subversive carrots are dependent on internal political stability in the target country. Subversive carrots can be vulnerable to domestic political shifts over time, for example if a new leader comes into power, or the relative balance of power shifts away from previously targeted political factions. This shift can be especially detrimental to the sender's statecraft strategy when new political leadership rises to power on the basis of opposition to existing crony relations with the sender state, leading to demands for greater public accountability. This limits the sustainability of subversive carrots as a long-term strategy.

Figure 2.1 shows the differing effectiveness of subversive carrots in high versus low public accountability systems. Table 2.2 summarizes my theoretical expectations based on the above two independent variables: the type of inducement strategy and the level of public accountability.

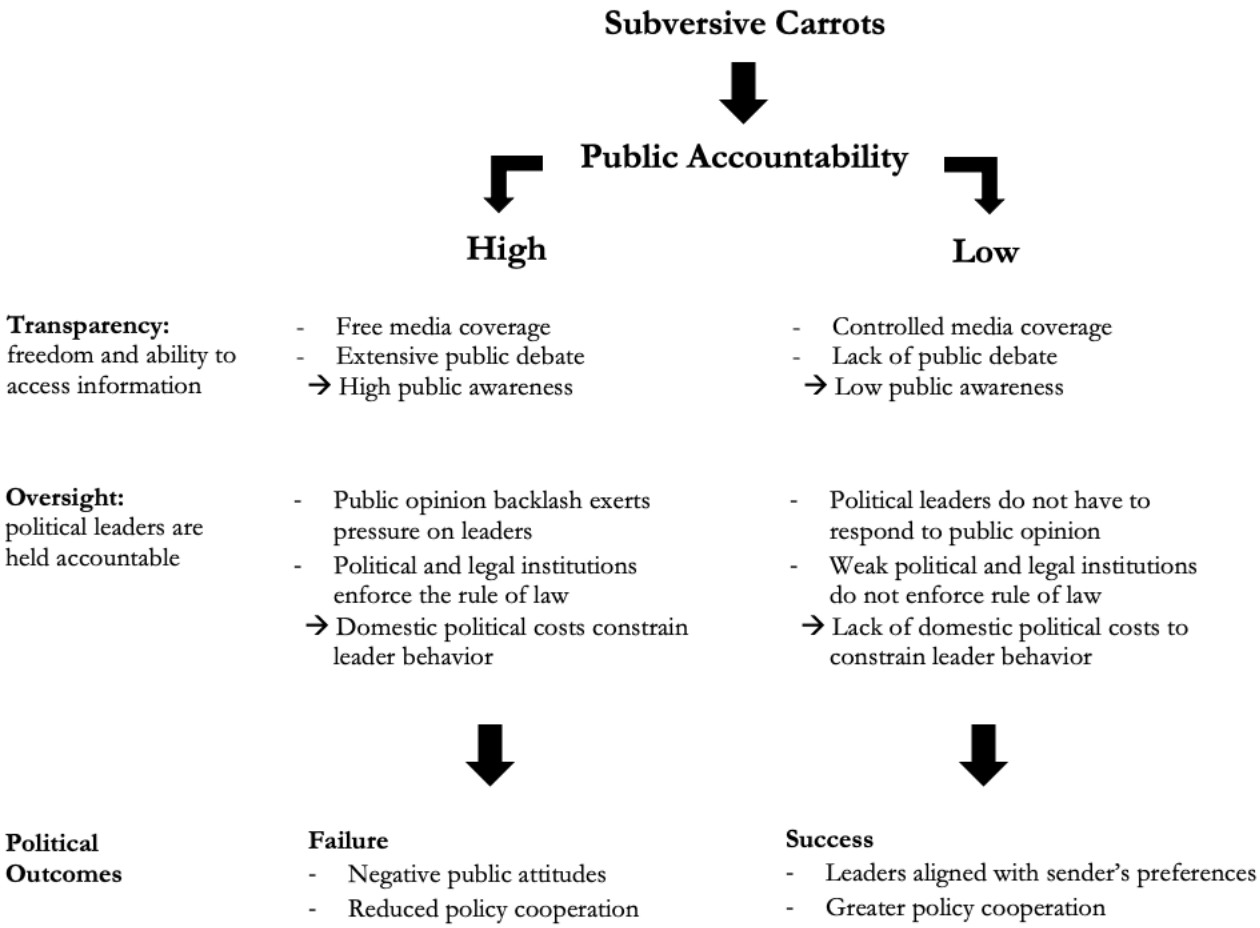

Figure 2.1: Effectiveness of subversive carrots under different levels of public accountability

	Low Accountability	High Accountability
Subversive Carrots	Effective	Ineffective
Stakeholder Cultivation	Ineffective	Effective

Table 2.2: Theoretical Predictions of Statecraft Effectiveness

Inducements, Enforcement, and Effectiveness

One potential challenge with the use of inducements as economic statecraft is the question of enforcement. Carrots are most effective when the bargain can be easily enforced, such as between democracies (which can help ensure credible commitment) or under international regimes (which lowers transaction costs).[50]

As such, a sender state offering inducements can face difficulties in ensuring the target's credible commitment. Once inducements are made, it is difficult to remove those inducements, even if target countries do not comply with the intentions of the sender. This problem is similar to the challenge faced by foreign investors under the 'obsolescing bargaining model',[51] in which host country governments gain greater leverage over investors over time. Target country elites can plausibly defect or fail to uphold the quid pro quo after incentives are received. As a result, subversive carrots might have to be provided repeatedly to prevent defection or be provided in exchange for a one-time or short-term transaction. In addition, the more diffuse nature of stakeholder cultivation suggests reduced certainty in achieving the desired political outcomes (although shifts in the domestic balance of interests in the target could more fundamentally alter incentives on the ground toward the sender's interests in the long run).

What are the implications for the effectiveness of economic inducements? First, issues of costs and defection suggest that positive economic statecraft is less able to produce political results than commonly assumed. Economic statecraft, even inducements, remains challenging to implement. This is particularly relevant to keep in mind given growing alarm among U.S. policymakers and other foreign observers about Beijing's use of economic statecraft to buy over or entice target countries. On the other hand, subversive carrots may alter the name of the game in the longer term – target country elites may be further empowered and more dependent on the sender for economic and political support.

Second, different types of inducements may be more effective at different policy goals. Subversive carrots would still be valuable for specific, short-term transactional goals, such as buying a leader's public

50. Drezner, "The Trouble with Carrots: Transaction Costs, Conflict Expectations, and Economic Inducements."
51. ?.

statement or vote. Stakeholder cultivation will likely prove more effective at diffuse, long-term goals of building reputation and shifting attitudes. Nonetheless, even with issues of defection present, across similar objectives and contexts of using inducements, I argue that we will still see variation in effectiveness based on whether procedural violation has occurred as well as the level of public accountability in the target country.

Economic Statecraft: The Case of China

China presents a theoretically and empirically important case for understanding the conditions under which economic capabilities can be translated into geopolitical influence. The size of China's economy, its high degree of global economic integration, the expansion of its overseas economic activities, and its growing role in international and regional institutions point to its significant material capabilities as a major power. As a 'rising' power of increasing economic and political importance, understanding Beijing's grand strategy and its interactions with other countries are key for theoretical frameworks explaining great power rivalry, power transition, and the nature of international order. China exercises economic statecraft on a wide range of states, both developing and developed, and authoritarian and democratic. Beijing has made state-linked investments and acquisitions in places as far-ranging as Greece, the Czech Republic, Zimbabwe, and Venezuela. This underscores the importance of understanding the outcomes of China's economic statecraft across different domestic political systems.

Economic statecraft has long been an important component of China's foreign policy. During the Cold War, the Chinese government distributed foreign aid as part of its geopolitical strategy against the Soviet Union and the United States. For example, even as it was a poor country struggling to recover from the aftermath of the Cultural Revolution, China upped its economic and military aid to North Vietnam to help it fight the Vietnam War in the early 1970s.[52] China's previously extensive aid programs toward North Korea, Mongolia, and Albania, seeking to gain their support against the Soviets, have even been criticized by some for pursuing geopolitical objectives at the expense of the country's own economic

52. Zhang, *Beijing's Economic Statecraft During the Cold War, 1949-1991*.

development and citizen wellbeing.[53]

Growing from the need to counter international economic sanctions during the Cold War, Beijing's economic diplomacy often adopted a "wedge strategy." Beijing actively expanded bilateral economic ties with U.S. allies (*gege jipo*, or breaking one at a time), and awarded economic inducements to selected countries in Asia and Africa in an effort to cultivate influence and form a bloc against the United States and the Soviet Union, as well as prevent Japanese support for Taiwan. Beijing also used economic inducements to peel away Japanese and European support for sanctions after the 1989 Tiananmen Square massacre.[54]

In addition, Beijing has used its economic leverage to punish and coerce target countries when inducements proved ineffective at achieving political objectives. The Chinese government cut off aid to Vietnam as punishment for its invasion of Cambodia in the late 1970s, and canceled Airbus contracts after French leaders met with the Dalai Lama.[55] When tensions flared over disputed features in the East and South China Seas in 2010 and 2012 respectively, China restricted rare earth exports to Japan and banana imports from the Philippines.

Today, Chinese scholars regard China's economic diplomacy as transitioning into a new phase. Economic diplomacy has become a more prominent feature of China's foreign policy since the 2000s, and Beijing has adopted a more proactive role in pushing its own economic initiatives, particularly as economic and security interests have become more intertwined.[56] In particular, China's relative success after the 2008-09 financial crisis, in contrast to most Western nations, sparked a major shift in Beijing's approach, leading it to become more ambitious and confident in its economic statecraft. The Chinese government sees renewed efforts at economic diplomacy as important in countering the U.S. rebalance to Asia and a

53. Yongsheng Zhou, "Jingji waijiao mianlin de jiyu he tiaozhan - jingji waijiao gainian yanjiu (Opportunities and Challenges facing Economic Diplomacy - Analyzing the Concept of Economic Diplomacy)," *Shijie jingji yu zhengzhi*, no. 7 (2003): 39–44.

54. Zhang, *Beijing's Economic Statecraft During the Cold War, 1949-1991*.

55. Liang Yan, "Zhongguo duiwai jingji zhicai: mubiao yu zhengce yiti (China's Foreign Economic Sanctions: Objectives and Policy Debates)," *Waijiao pinglun*, no. 6 (2012): 16–29.

56. Heath2016; Wei Li and Yi Sun, "Lijie zhongguo jingji waijiao (Understanding China's Economic Diplomacy)," *Waijiao pinglun*, no. 4 (2014): 1–24; Song, "Zhongguo zhoubian jingji waijiao: jizhi xietiao yu zhengce xuanze (China's Peripheral Economic Diplomacy: Coordination of Mechanisms and Policy Choices)."

worsening regional security environment in the last few years.[57] Beijing's new initiatives represent an underlying dissatisfaction with existing U.S.-led regional frameworks and highlight a desire among Chinese elites to take on a greater regional leadership role.[58]

Under President Xi Jinping, these trends have accelerated in the form of more concrete initiatives and the development of a more aggressive form of economic statecraft. China's "going out" strategy of encouraging outward investment by Chinese firms was repackaged into the sweeping Belt and Road Initiative (BRI, formerly One Belt One Road), which is now part of the Party constitution and is seen as Xi's signature foreign policy initiative.[59] While stemming from the "March West" strategy originally articulated by influential Peking University scholar Wang Jisi,[60] which advocated for China to focus its foreign policy engagement on Central Asia and the Middle East and minimize zero-sum tensions with the United States in East Asia, the BRI has now expanded into a far-reaching, if tenuously defined, global initiative that is provoking further geopolitical concerns.

Observations of China's growing economic clout and global presence, particularly the unconditional and less-than-transparent nature of its aid and investment, have fed into the narrative of a rising China seeking to use its power to persuade or coerce countries to support its foreign policy objectives, override U.S. and Western interests, and even create an alternative international order or an anti-Western bloc. For example, a think tank report asserts "China often uses its development and investment policies to gain access to resources or achieve favorable diplomatic outcomes."[61] The authoritarian nature of the Chinese regime and the prominence of state-owned enterprises (SOEs) in China, in which the state has close links with and leverage over major commercial actors, arguably make it easier for Beijing to exercise economic

57. Ga02015.

58. Ye2015.

59. Brenda Goh and John Ruwitch, "Pressure on as Xi's 'Belt and Road' enshrined in Chinese party charter," *Reuters*, October 24, 2017.

60. Yun Sun, "March West: China's Response to the U.S. Rebalancing," *Brookings Up Front Blog*, January 31, 2013, https://www.brookings.edu/blog/up-front/2013/01/31/march-west-chinas-response-to-the-u-s-rebalancing/.

61. Shanthi Kalathil, "Influence for Sale? China's Trade, Investment and Assistance Policies in Southeast Asia," *East and South China Seas Bulletin* 4 (2012).

statecraft,[62] although this does not always eliminate principal-agent problems.[63] The strong degree of state-directed economic activity adds to concerns over sinister, strategic goals behind Chinese economic activities abroad, particularly those in energy, resource, and technologically-sensitive sectors.

Most reports assume that large-scale Chinese aid and investment inevitably produces political influence for Beijing in those recipient countries. However, alternative accounts suggest that claims of Beijing grabbing land, food, and fossil fuels in Africa and Latin America to ensure its own resource security are overblown.[64] The success of China's infrastructure-for-oil deals varies from country to country.[65] Public accountability provides a framework to better understand conditions for the effectiveness of economic statecraft.

The 'State' in Statecraft

While this book focuses on the outcomes of economic statecraft, the assessment and employment of economic statecraft can be a messy process. First, the state is not monolithic. Given the multiplicity of actors and goals involved in overseas economic activities, even authoritarian governments are not always unitary strategic actors in foreign policy.[66]

In the China context, the state does play a significant role in directing and managing the economy.[67] While control is not absolute, due to the scale of the country and the diverse range of actors involved, China's strong state capacity means that there are nevertheless a considerable number of levers that the state can use to incentivize or coerce domestic actors to follow its desired policies. At the same time, because of the nature of policymaking institutions in China, in which the central government relies on local

62. Davis, Fuchs, and Johnson, "State Control and the Effects of Foreign Relations on Bilateral Trade"; Fuchs and Klann, "Paying a Visit: The Dalai Lama Effect on International Trade."

63. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*.

64. Deborah Brautigam, *Will Africa Feed China?* (Oxford University Press, 2015).

65. Ana Cristina Alves, "Chinese Economic Statecraft: A Comparative Study of China's Oil-backed Loans in Angola and Brazil," *Journal of Current Chinese Affairs* 42, no. 1 (2013): 99–130.

66. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*; Audrye Wong, "More than Peripheral: How Provinces Influence China's Foreign Policy," *China Quarterly* 235 (September 2018).

67. Meir Alkon, "Economic Interdependence, Political Risks, and the Limits to Liberalization" (PhD Dissertation, Princeton University, 2019).

governments, bureaucratic agencies, and commercial actors to implement top-level strategic directives, there is often room for domestic actors to reinterpret and reshape broad instructions in pursuit of their own parochial interests and objectives.[68] The pursuit of economic interests has often led to consequences for China's foreign security policies and its relations with its neighbors.[69]

In addition, firms are not always agents of the state. For instance, commercial motives may differ from strategic goals, or the business methods of firms may not be explicitly endorsed by the government. How unified the state is and the degree of state control over commercial actors are important factors affecting the sender country's ability to implement economic statecraft.[70] There is a strong symbiotic relationship between state-owned enterprises and top political elites.[71] At times 'moral hazard' can ensue, in which SOEs are able to pursue their own agendas overseas and engage in riskier behavior because they are acting on behalf of the state and know that the Chinese government will have to bail them out, or because they know that they face limited political consequences.

The Belt and Road Initiative is a prime example of how the multiplicity of actors (and a corresponding inability to clearly distinguish state-led or politically-driven economic activities) can complicate external perceptions and responses. Both within and outside China, virtually all investment projects are rhetorically classified to be part of Beijing's ever-expanding BRI. A senior Malaysian official commented to me that "everyone has latched onto OBOR [One Belt One Road, the initial term for the BRI]", not just Chinese companies but also Malaysian firms seeking to justify their own projects. In fact, the Chinese government has been unable to provide its Malaysian counterpart with a list of BRI projects, because Beijing was not necessarily aware of all ongoing projects, and because of the potential economic and political implications: projects left out of the BRI umbrella could suffer from lack of investor confidence, while

68. Kenneth Lieberthal and David M Lampton, eds., *Bureaucracy, politics, and decision making in post-Mao China* (University of California Press Berkeley, 1992); Andrew Mertha, ""Fragmented authoritarianism 2.0": Political pluralization in the Chinese policy process," *The China Quarterly* 200 (2009): 995–1012.

69. Wong, "More than Peripheral: How Provinces Influence China's Foreign Policy."

70. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*.

71. Linda Jakobson and Dean Knox, *New Foreign Policy Actors in China* (Stockholm International Peace Research Institute, 2010); Sarah Eaton and Genia Kostka, "Central protectionism in China: The "central SOE problem" in environmental governance," *The China Quarterly* 231 (2017): 685–704; Wendy Leutert, "The Political Mobility of China's Central State-Owned Enterprise Leaders," *The China Quarterly* 233 (2018): 1–21.

other private-led projects included in the BRI would appear to be sanctioned by the Chinese government and hence subject to increased scrutiny and demands by host countries.[72]

Intentionality

How much of economic statecraft is a state-led strategy? In addition, how explicit must the political intentions be in economic statecraft? Certainly, under contemporary conditions of globalization, not all overseas economic and commercial activities are necessarily driven by Beijing's political motives or part of official foreign policy. At the same time, naturally or organically-developing economic interdependence can produce opportunities for leverage in the future, or changes in recipient country perceptions of such potential leverage. As part of a Hirschman effect, recipients see a shift in their national interests as a result of economic linkages. This provides a conducive context to exercise economic statecraft with a specific political goal in mind.

In this sense, diffuse or structural economic interdependence could also be seen as a form of economic statecraft. Indeed, economic interdependence is often cited as a reason for countries' growing reluctance to provoke major economic powers, a constraint against war, and a driver for peace.[73] Fear of losing business or eagerness to court new sources of investment and financing has certainly shaped how countries respond to the actions of sender states such as the United States and China – this is a common refrain in the policy world.

Push vs Pull?

Related to the issue of intentionality is the issue of the political origins of economic inducements. Recipient countries themselves are often eager for Chinese investment or aid, which promise much-needed

72. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

73. Dale C Copeland, "Economic interdependence and war: A theory of trade expectations," *International Security* 20, no. 4 (1996): 5–41; Paul A Papayoanou, *Power Ties: Economic Interdependence, Balancing, and War* (Ann Arbor, MI: University of Michigan Press, 1999); Edward D Mansfield and Brian M Pollins, "The Study of Interdependence and Conflict: Recent Advances, Open Questions, and Directions for Future Research," *Journal of Conflict Resolution* 45, no. 6 (2001): 834–859; Edward D. Mansfield and Brian M. Pollins, eds., *Economic Interdependence and International Conflict: New Perspectives on an Enduring Debate* (Ann Arbor, MI: University of Michigan Press, 2003).

economic benefits and development. Demand from target states – which also have more agency than most models of great power politics assume – could thus exert a 'pull' effect, rather than the Chinese government 'pushing' economic statecraft onto these recipient countries. Some PRC government officials have argued that Chinese firms are simply responding to existing structures and incentives in recipient countries when doing business, and those in recipient countries have also acknowledged that weak institutions are easily exploited.[74] This book does not argue that all economic interactions are a function of the sender state – in this case, China – attempting to impose its wishes and goals on target countries. As my theoretical framework suggests, there is often a mutual confluence of (self-)interests between rent-seeking elites in the recipient country and profit-seeking or influence-seeking elites in the sender state. I focus on the political outcomes that result from how the type of inducements being offered interact with the domestic political institutions in the target country, and I would argue that similar outcomes will occur whether the inducement was the result of a 'pull' or 'push'.

Implications for a theoretical framework of economic statecraft

With the above considerations in mind, my theoretical framework does not require any assumption of full state control over economic inducements nor intentional design of inducements to push recipients in a certain direction. In fact, because the core explanatory mechanism is based on whether procedural violation has occurred and whether there are political institutions available to constrain or punish elites, it would still hold regardless of how state-led or politically-intentioned the inducements are. My argument highlights the important role of the target country's domestic political conditions in shaping how economic inducements are received and processed into political outcomes. I argue that this provides a parsimonious explanation for the trends we are seeing in the exercise of economic statecraft today. For example, countries seen to be traditionally close with China, such as Pakistan and Sri Lanka, are increasingly grappling with public skepticism over proffered investment projects.

The interactions between public accountability and the type of inducement strategy used would ap-

74. Interview, National Development and Reform Commission, Beijing, May 17, 2019; Interview, Dato Majid Khan, former Malaysian ambassador to China, Kuala Lumpur, June 10, 2019.

ply similarly to situations of diffuse economic statecraft, when economic inducements are not driven by the state or by political motives. China's overseas economic activities, even if driven by commercial actors, has produced externalities that elicit public attention and response, which creates long-lasting repercussions on China's reputation more broadly as well as attitudes toward China's economic statecraft specifically. In the case of China, this is arguably exacerbated by widespread perceptions of China's authoritarian state capitalism, in which external actors are assumed to be acting on behalf of the state.

Again, the key factor in determining target country responses is how economic inducements are being offered and carried out – that is, whether procedural violation is present or not. Regardless of whether there was an explicit political objective linked to the inducement, the nature of public and elite response in recipient countries will depend on whether the inducement in question comports with domestic processes and institutions.

I argue that a theoretical framework emphasizing the interaction of economic statecraft with domestic politics has greater traction and continued pertinence across a range of countries and contexts. My interviews and conversations with policymakers and political observers across a range of recipient countries point to important differences in how many of these governments view China's economic statecraft and Chinese investment, compared to the United States. In countries such as (but not only) Malaysia and the Philippines, economic inducements are viewed under a lens that is less about geopolitics and more about domestic politics and local benefits.[75] For many of the recipient countries in question, a theory tying the outcomes of China's foreign policy behavior to domestic politics and public opinion in effect serves to better capture the factors that matter most vis-a-vis public attitudes and elite decisions.

Most analyses of economic statecraft focus only on international or strategic factors. My theoretical contribution lies in analyzing and classifying strategies of economic statecraft, and providing a novel framework to think about the outcomes of economic statecraft depending on how it is carried out. In particular, I show how economic statecraft interacts with and affects domestic politics in recipient coun-

75. Interview, Dato Majid Khan, former Malaysian ambassador to China, Kuala Lumpur, June 10, 2019; Interview, Dr Ong Kian Ming, Malaysia Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019; Interview, National Economic Development Authority, Manila, July 2017.

tries, which has not been considered as much in most discussions of economic statecraft or grand strategy. This helps to explain why certain types of economic statecraft work in some cases but not in others. It also suggests how economic statecraft can also be risky because of vulnerability to politicization and getting caught up in domestic elite politics – a frequent pitfall for major powers seeking to intervene or influence small countries.

The Supply Side: Where Does Economic Statecraft Come From?

Policy is not made in a void. How is economic statecraft made and what are some factors that can influence how countries or governments choose to approach or implement economic statecraft? In this section, I discuss how the nature of economic statecraft can be shaped and potentially constrained by (i) the domestic political economy of the sender state; and (ii) the type of foreign policy goals that the sender state has.

While a theory or detailed account of the supply side of economic statecraft generally, or the case of China specifically, is beyond the scope of this book, understanding the broad contours of the supply side is important because it shows that the type of inducement strategy is a function of supply side conditions (domestic political economy, sender state goals), and is not endogenous to accountability in the target country. It also provides intuition for why countries might continue to supply strategies of economic statecraft that are poorly suited for success in a given target country.

The Sender's Domestic Political Economy

The sending state's domestic political economy is fundamental to how elites in that country conceive of state-market relations. The institutions and processes surrounding how business is done in the sender state impact the approach to investment in other countries. Because it entails interactions between political and economic actors, economic statecraft, in particular the offering of economic inducements, is likely to be a reflection of the nature of the sender's domestic political economy.

In China, rapid economic growth since the era of reform and opening up, combined with a contin-

ued legacy of state direction of the economy, has created an environment of co-mingled state-business relations along with endemic corruption.[76] Corruption intensified as political elites sought to benefit from the privatization of state assets,[77] while continued state control over key economic levers meant that business actors had to develop a symbiotic relationship with these political elites. Indeed, the Chinese Communist Party soon saw the benefits of coopting private entrepreneurs and commercial actors into the system for consolidating political stability. The continued weakness of domestic institutions and rule of law, along with the persistent privileging of a group of politico-economic elites, facilitated deeper collusion and corruption as a feature of China's economic engine.

As a result, when engaging in overseas investment or economic statecraft, China is more likely to apply a similar model of political economy. This suggests an inclination toward the use (at least initially) of subversive carrots as the dominant approach to economic statecraft. Note that this is more likely to characterize China's post-reform era statecraft than it is the pre-reform era economic statecraft, which is analyzed in Chapter 8, and which entailed the use of stakeholder cultivation.

Given the general *modus operandi* of business in China in the 90's and 2000's, offering kickbacks to key political power brokers or circumventing troublesome regulations may be seen as a more efficient, 'win-win' solution to achieve economic and political objectives. A lack of know-how and experience in following established institutional processes may further dissuade or inhibit sender states like China from adhering to such processes. According to an NDRC (the National Development and Reform Commission, an important Chinese ministry) official, the lack of 'long arm regulations' in China, unlike the United States, means that Chinese firms tend to pay less attention to regulations in recipient countries and capitalize on weak governance institutions.[78]

In contrast, countries with more rules-based institutions or with more regulated links between the state and market may tend toward employing stakeholder cultivation. Countries that have signed on to the OECD's Development Assistance Committee (DAC) standards for foreign aid are likely to have the

76. Minxin Pei, *China's Crony Capitalism* (Cambridge MA USA: Harvard University Press, 2016).

77. Andrew Wedeman, "The intensification of corruption in China," *The China Quarterly* 180 (2004): 895–921; Andrew Wedeman, *Double paradox: Rapid growth and rising corruption in China* (Cornell University Press, 2012).

78. Interview, National Development and Reform Commission International Cooperation Center, Beijing, May 17, 2019.

incentives and capacity to adhere to established regulations and processes, thus minimizing procedural violations in recipient countries. Limited government control over commercial actors also makes it more difficult to corrall the latter as part of a concerted inducement strategy. For example, the United States has only been able to marshal a relatively limited amount of resources for overseas infrastructure financing compared to Beijing, because the nature of state-business relations means that Washington is less able to redirect commercial actors at its political whim.

Of course, the relationship between supply side political economy and statecraft strategy is not deterministic. However, considering the domestic political economy of sender states lends some suggestive clues to which economic statecraft strategy it is more likely to be employed, at least during an initial learning phase, due to experience, capacity, and path dependence. This general pattern is consistent with the observation that China's use of subversive carrots has been more prominent in recent decades than its use of stakeholder cultivation, particularly when Beijing has also sought to pursue specific political objectives, as explained below.

The Sender State's Objectives

The second factor influencing economic statecraft strategy is the nature of the sender's foreign policy goals. Subversive carrots lend themselves to achieving a specific transactional, short-term goal, such as altering a foreign policy statement or a political vote, often by providing benefits directly to certain elites. Stakeholder cultivation, on the other hand, with its longer time horizon and indirect payoffs, is more appropriate for more diffuse, uncertain, or ongoing objectives.

Table 2.3 summarizes some key attributes of subversive carrots versus stakeholder cultivation, in particular costs, size of the selectorate, time horizon, and the nature of the economic benefits, with implications for type of the ultimate payoffs. While subversive carrots are cheaper, are given to a smaller selectorate, involve direct benefits, and have a shorter time horizon, stakeholder cultivation is more costly, is targeted towards a broader selectorate, involves indirect benefits, and operates over a longer time horizon.

This further suggests a supply-side bias in (contemporary) China toward the use of subversive car-

	Subversive Carrots	Stakeholder Cultivation
Costs	Cheaper	More costly
Selectorate	Smaller	Broader
Time Horizon	Short	Long
Benefits	Direct	Indirect

Table 2.3: Implications of inducement strategies for the type of policy objectives

rots. As a rising and selectively revisionist power,[79] Beijing's priority is modifying the global balance or status quo regarding specific (multiple) issues that it perceives as particularly pertinent for its national security and internal political stability. This suggests geopolitical objectives that tend to be more tangible, delimited, and immediate, for instance changing a political leader's policy position on Taiwan, Tibet, or the South China Sea. As a result, Beijing attempts to use subversive carrots even in clearly high public accountability countries, such as Australia (Chapter 7). In addition, joining the ranks of the economic heavyweights has potentially induced a mindset in Chinese elites that other, smaller countries are easier to buy over, and that carrots are cheap and easy enough that Beijing can afford to throw money around in search of a desired outcome. At the same time, as will be discussed further in Chapter 9, China appears to be learning that buying policy change with subversive carrots is less easy than it may have thought, leading to potential future shifts in how Chinese leaders think about economic statecraft and economic diplomacy, perhaps with a concomitant change in the balance of subversive carrots versus stakeholder cultivation strategies.

Implications

The above discussion of where economic statecraft comes from and what drives the sender's approach to economic statecraft points to two main implications. First, it addresses potential concerns of endogene-

79. See e.g. Evan A. Feigenbaum, "Reluctant Stakeholder: Why China's Highly Strategic Brand of Revisionism is More Challenging Than Washington Thinks," *Macro Polo*, April 27, 2018, https://macropolo.org/analysis/reluctant-stakeholder-why-chinas-highly-strategic-brand-of-revisionism-is-more-challenging-than-washin

ity. The type of inducement strategy chosen has its origins in the sender's domestic political economy and the sender's potential foreign policy objectives. The domestic politics of China (which is key in determining economic statecraft strategy) is independent of the target's own domestic institutions. As such, inducement strategy (one of my explanatory variables) is not determined by or jointly determined with the level of public accountability in the target country.

Second, it provides grounds to explain why there is a relative absence of cases in which China uses stakeholder cultivation in a low public accountability country. A domestically-driven inclination toward subversive carrots means that China is far less likely to even attempt stakeholder cultivation under conditions of low public accountability, which arguably roughly mirrors the condition of state-market relations within China. This explains why stakeholder cultivation has not been as common or dominant a strategy for Beijing in the post-reform era.

Research Design

While the wide variation in political, economic, and social conditions across countries means that it is virtually impossible to achieve perfectly controlled case comparisons, the research design and case selection strategy used in this book aims to minimize confounders and elucidate the explanatory mechanisms of my theoretical framework. I adopt a multi-method approach, combining cross-case comparisons, within-case process tracing, and survey experimental evidence.

Because China's use of large-scale economic inducements – accompanying its expansion of foreign investment and aid – has only gained signifiance in a relatively recent time period, and because it can be hard to quantify a standardized indicator of effectiveness, I use a predominantly qualitative approach based on carefully selected case studies. Case study methods afford advantages such as construct validity and the ability to make inferences about causal mechanisms, particularly those that are less well understood.[80] Relative to regression or statistical analysis, a qualitative approach can help to identify scope conditions, necessary and sufficient conditions for a theory, and which variables might have been overlooked. For

80. Andrew Bennett, "Case study methods: Design, use, and comparative advantages," in *Models, numbers, and cases: Methods for studying international relations* (University of Michigan Press, 2004), 19–55.

example, my findings highlight that the outcomes of economic statecraft – and foreign policy more generally – cannot be easily disentangled from domestic political issues such as corruption and politician performance.

The research design used in this book employs the comparative sequential method, combining cross-case comparison and within-case process tracing.[81] Structured, focused case comparisons allow me to pinpoint public accountability as a necessary condition explaining the political outcomes of economic statecraft.[82] I use both most similar and most different research designs (in the spirit of Mill's method of agreement and method of difference) to eliminate alternative explanations, showing that these factors are not necessary or sufficient, respectively, to explain the effectiveness of economic statecraft. In developing inferences through an iterative research process between theory and data, I implement best practices of transparently discussing available evidence and rival explanations, as well as examining theoretical conditions and generalizability, in order to safeguard against confirmation bias and ad-hoc hypothesizing.[83]

In addition, I use process tracing to establish the causal chain of my theory and show that this is consistently the dominant driver of public and political responses relative to other alternative explanations, across different cases with an array of attributes. Process tracing is particularly useful for examining causal mechanisms and analyzing decision making processes as well as the surrounding policy environment, including leader perceptions and public preferences.[84] A small number of key causal-process observations can play a valuable role in causal inference,[85] particuarly because process tracing pays close attention to the sequential unfolding of events over time, showing how intervening variables link the independent variable to the dependent variable.[86] Tables 2.4 and 2.5 summarize the predictions and observable impli-

81. Tulia G Falleti and James Mahoney, "The comparative sequential method," in *Advances in comparative-historical analysis* (Cambridge University Press, 2015), 211–239.

82. Alexander George, "Case Studies and Theory Development: The Method of Structured, Focused Comparison," in *Diplomacy: New approaches in history, theory, and policy*, ed. P. G. Lauren (Free Press, 1979); Jack S Levy, "Case studies: Types, designs, and logics of inference," *Conflict management and peace science* 25, no. 1 (2008): 1–18.

83. Tasha Fairfield and Andrew Charman, "A Dialogue with the Data: The Bayesian Foundations of Iterative Research in Qualitative Social Science," *Perspectives on Politics* 17, no. 1 (2019): 154–167.

84. Levy, "Case studies: Types, designs, and logics of inference."

85. Henry E Brady and David Collier, *Rethinking social inquiry: Diverse tools, shared standards* (Rowman & Littlefield Publishers, 2010).

86. David Collier, "Understanding process tracing," *PS: Political Science & Politics* 44, no. 4 (2011): 823–830.

cations for my theory of public accountability.

Prediction	Observable Implications
High public accountability → Subversive carrots fail	*Transparency* • Information on inducements available through media/other channels • Media coverage emphasizes violation of political processes and institutions *Oversight* • Public opinion backlash emphasizes how China's economic inducements violate domestic political processes and institutions • Political debate in target country will invoke violation of political processes and institutions in justifying policy response to Beijing *Outcomes* • Elites modify their behavior in response to public backlash. • Elites are punished, through political or legal means, for violating domestic processes and institutions • Elites cite public opinion backlash and institutional constraints as factor in policy decisions
Low public accountability → Subversive carrots succeed	*Transparency* • Information on inducements unavailable through media/other channels • Lack of media coverage on the violation of political processes and institutions *Oversight* • Lack of public discourse on China's economic inducements • Lack of open political debate in target country *Outcomes* • Elites do not modify their behavior in response to public opinion or institutional constraints. • Elites are not punished, through political or legal means, for violating domestic processes and institutions • Elites make policy decisions in line with China's preferences

Table 2.4: Carrots and public accountability: predictions and observable implications

Prediction	Observable Implications
High public accountability → Stakeholder cultivation succeeds	*Transparency* • Information on inducements available through media/other channels • Media coverage emphasizes benefits, adherence to political processes and institutions *Oversight* • Public opinion and a range of domestic actors are positive regarding China and favor China's policy preferences. • Public and political discourse emphasizes the legitimate economic benefits provided by China. *Outcomes* • Elites modify their behavior in response to public opinion and domestic constituencies. • Elites make policy decisions in line with China's policy preferences
Low public accountability → Stakeholder cultivation fails	*Transparency* • Information on inducements unavailable through media/other channels • Media coverage does not emphasize benefits, adherence to political processes and institutions *Oversight* • Lack of diverse public or political discourse on legitimate economic benefits provided by China. • Elite opinion is not positive toward China and China's economic presence *Outcomes* • Elites do not modify their behavior in response to public opinion or domestic actor preferences. • Elites do not make policy decisions in line with China's preferences

Table 2.5: Stakeholder cultivation and public accountability: predictions and observable implications

While past research has tended to focus on China's investments in Africa and Latin America,[87] I focus my analysis on countries in the Asia-Pacific region, close to China's geographic periphery, because it is for these countries where there are significant economic and political-security tradeoffs, and where economic statecraft often has important geopolitical consequences for China and for the target countries involved. In large part because of their geographic proximity, countries in East Asia as well as the Pacific are highly dependent on China's massive economy, yet are also most directly affected by China's military modernization. Beijing has arguably been most concerned and most active in pursuing its security interests, including national sovereignty and territorial disputes, in the Asia-Pacific region.

The book includes at least one case for each combination of the two explanatory variables in my theoretical framework: the type of inducement strategy offered by the sender and the level of public accountability in the target. This design confirms the predictive validity of my theory, showing how the interaction between different values of the two explanatory variables leads to different political outcomes – success or failure.

Moreover, because there can be multiple potential competing explanations, I introduce additional cross-case comparisons that help to disconfirm rival theories and provide additional evidence for the consistent role of public accountability mechanisms despite changing confounders. For example, I show how subversive carrots consistently failed across different high accountability countries, including the Philippines, Malaysia, and Australia.

In addition, I examine within-country variation (at the project level) of the type of inducement provided. This serves to control for country-level characteristics that could possibly influence policy responses to China's economic statecraft. I show how subversive carrots and stakeholder cultivation produced differing outcomes. In both the country cases of Malaysia (Chapter 4) and Australia (Chapter 7), subversive carrots backfired while stakeholder cultivation succeeded under their high public accountability environments.

To test the predicted outcomes of China's subversive carrots, I select country cases with different val-

87. Alves, "Chinese Economic Statecraft: A Comparative Study of China's Oil-backed Loans in Angola and Brazil"; Brautigam, *Will Africa Feed China?*

ues of public accountability. While the theory proposes binary categories of low and high accountability for reasons of parsimony, the book analyzes a spectrum of cases to better unpack the core mechanisms of public accountability.

The book includes extreme value cases of a high accountability country – Australia – and a low accountability country – Cambodia. These clear-cut cases provide strong evidence for how the mechanisms of public accountability lead to political backlash against subversive carrots, while the absence of accountability allows political elites to accept subversive carrots. In both country cases, I also discuss how stakeholder cultivation has empowered vested interests in high accountability Australia, while it failed to gain political traction in low accountability Cambodia.

In tandem, I examine cases of moderately high public accountability, which often occur in the context of flawed democracies – in this book, the Philippines and Malaysia. These cases serve as a hard test for the mechanisms of public accountability – transparency and oversight – in producing similar public and political backlash across countries with differing economic and political situations. This shows the wide applicability of my theory beyond ideal cases at the extreme values, and has empirical implications for how resilient different political systems can be.

As a measure of accountability levels in Southeast Asia, I present data from the World Bank Worldwide Governance Indicators (WGI). While these indicators are not perfect measures of accountability, I include them for illustrative purposes. The World Bank defines 'Voice and Accountability' as "the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media."[88]

To better control for geographic and regional factors, I select several country cases within Southeast Asia. Figure 2.2 shows the varying levels of accountability across Southeast Asian countries, as measured by the World Bank. Figure 2.3 shows the degree of economic interdependence with China across Southeast Asian countries

88. The WGI dataset measures six dimensions of governance using six aggregate indicators, based on over 30 data sources from surveys of households and firms, non-governmental organizations, public sector organizations, and commercial business information providers. More information on methodology and data here: http://info.worldbank.org/governance/wgi/index.aspx

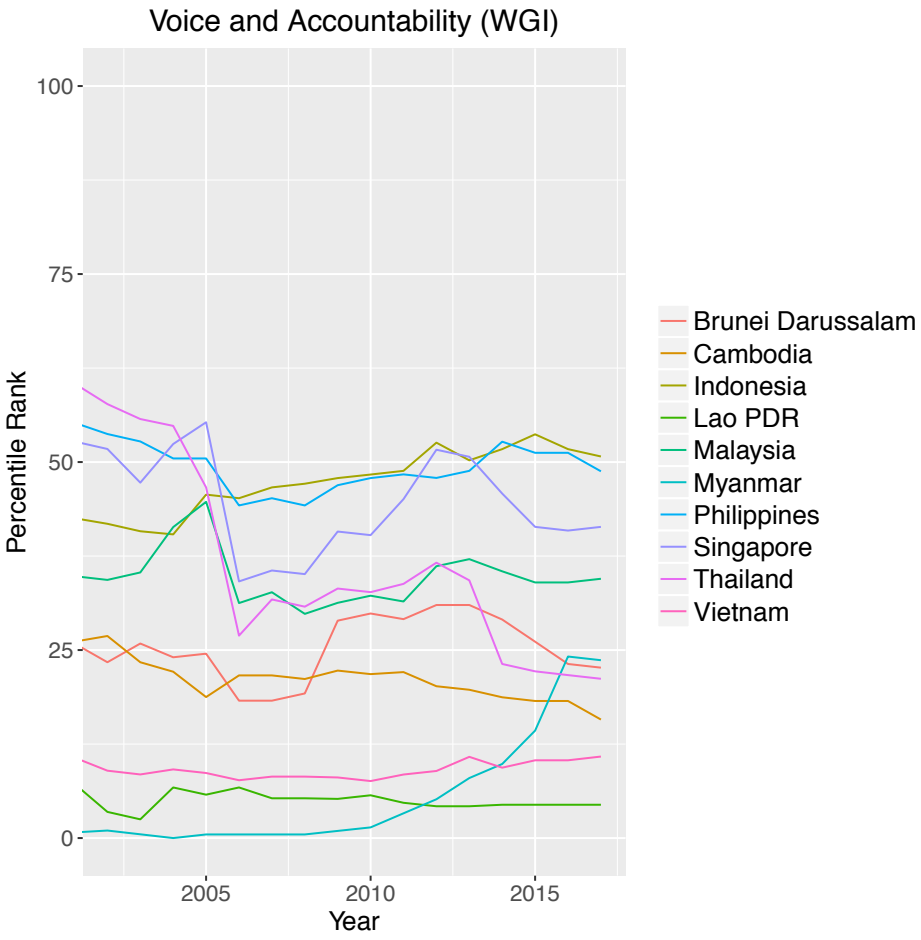

Figure 2.2: Accountability in Southeast Asian countries, measured by the World Bank Worldwide Governance Indicators. Higher ranked = more accountable.

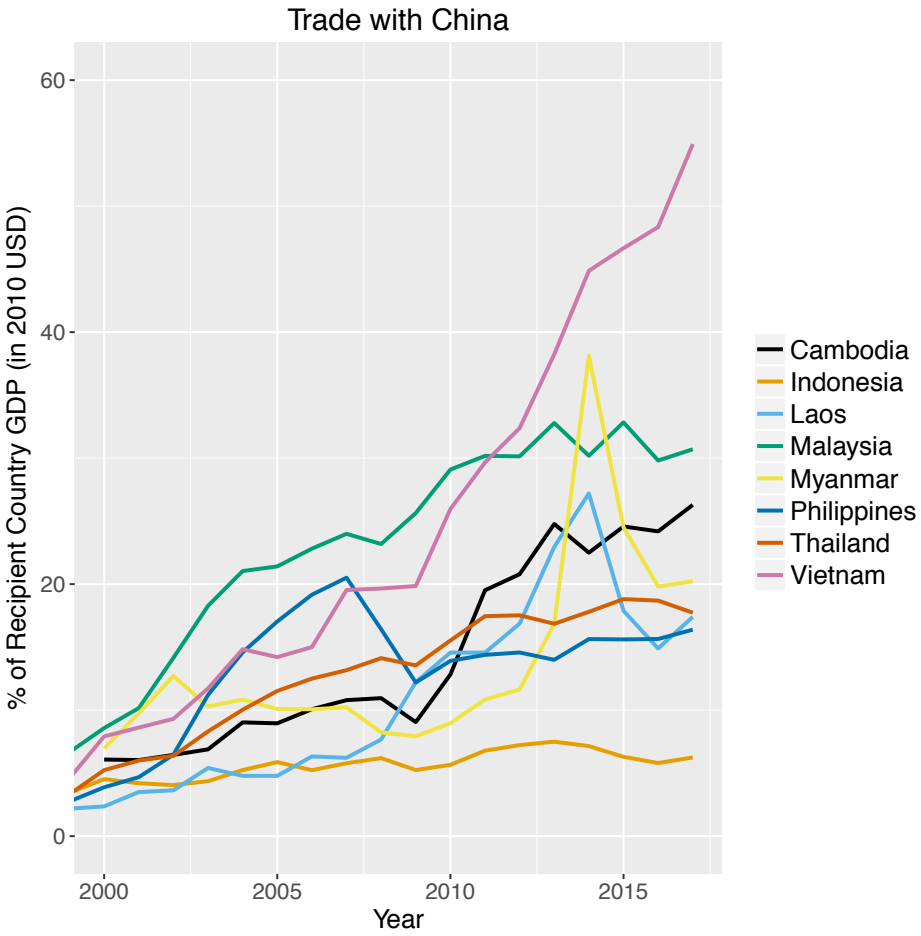

Figure 2.3: Trade with China as a percentage of GDP across Southeast Asian countries. Source: CEIC

For comparison with the success of subversive carrots in low accountability Cambodia, the Philippines serves as a most similar but high accountability case. Of the plausibly higher accountability countries in the region, Indonesia has much lower trade dependence on China (and a history of violent tensions with ethnic Chinese) and Singapore is much more economically developed. In contrast, the Philippines – in addition to being one of the higher ranked countries for public accountability across both measures – is a lower middle income country, as is Cambodia, has a reasonably high degree of economic interdependence with China, and does not have the same legacy of widespread racial tensions with Chinese populations as Indonesia does.

As an additional complementary case study, I also examine China's economic statecraft in Malaysia, which has moderately high accountability relative to other Southeast Asian countries, but suggests different potential confounders from the Philippines case. Malaysia serves as a least likely case for the theory of backlash against subversive carrots. It is a developing country dependent on Chinese trade and investment, it is not a U.S. alliance partner, it has a tradition of relatively positive relations with China, and security disputes are not a major feature of bilateral ties. The Malaysia case thus provides enhanced inferential leverage, since it appears to be a most likely case for the success of subversive carrots based on the above alternative explanations.[89] However, I find that the presence of accountability mechanisms facilitated public backlash and political consequences for leaders in office. Taken in tandem, the two cases of the Philippines and Malaysia provide evidence for the explanatory mechanisms of my theoretical argument – the existence of procedural violation through subversive carrots – that remain constant across a range of alternative factors.

In addition, still within the Southeast Asian context, I leverage within-country variation in public accountability in Myanmar to explain changes in the outcomes of subversive carrots. This shift in accountability – shown by the teal line in Figure 2.2 – resulted from the domestic political transition from a military junta to a more democratically-elected form of govenrment. Examining changes in accountability in a single country allows me to better control for national and international-level factors that could

89. Levy, "Case studies: Types, designs, and logics of inference."

influence the effectiveness of economic statecraft.

Australia and Malaysia further serve as a "most different" case comparison. The two countries are at differing levels of economic development, have different historical and cultural backgrounds, and differing closeness in their political and security relationships with the United States. Examining both cases avoids overdetermination by tracing the similar processes of public accountability in two very different countries.[90]

Figures 2.4 shows accountability levels for the selected case studies (Cambodia, the Philippines, Malaysia, Myanmar, and Australia), while Figure 2.5 shows the levels of trade interdependence with China. It should be noted that economic interdependence was markedly high for all the country cases during the time period under study. Table 2.6 summarizes the major comparable characteristics of my country cases.

	Cambodia	Philippines	Malaysia	Myanmar	Australia
Public Accountability	Low	Moderately High	Moderately High	Low → Mod. High	High
Income	Lower-middle	Lower-middle	Upper-middle	Lower-middle	High
Geography	Continental SEA	Maritime SEA	Mari./Cont. SEA	Continental SEA	Asia-Pacific
Economic Dependence	V. High	High	V. High	V. High	Fairly High
Security Disputes	No	Yes (low during case period)	Minor	No	No

Table 2.6: Summary of country case attributes

90. Henry Teune and Adam Przeworski, *The logic of comparative social inquiry* (New York: Wiley-Interscience, 1970).

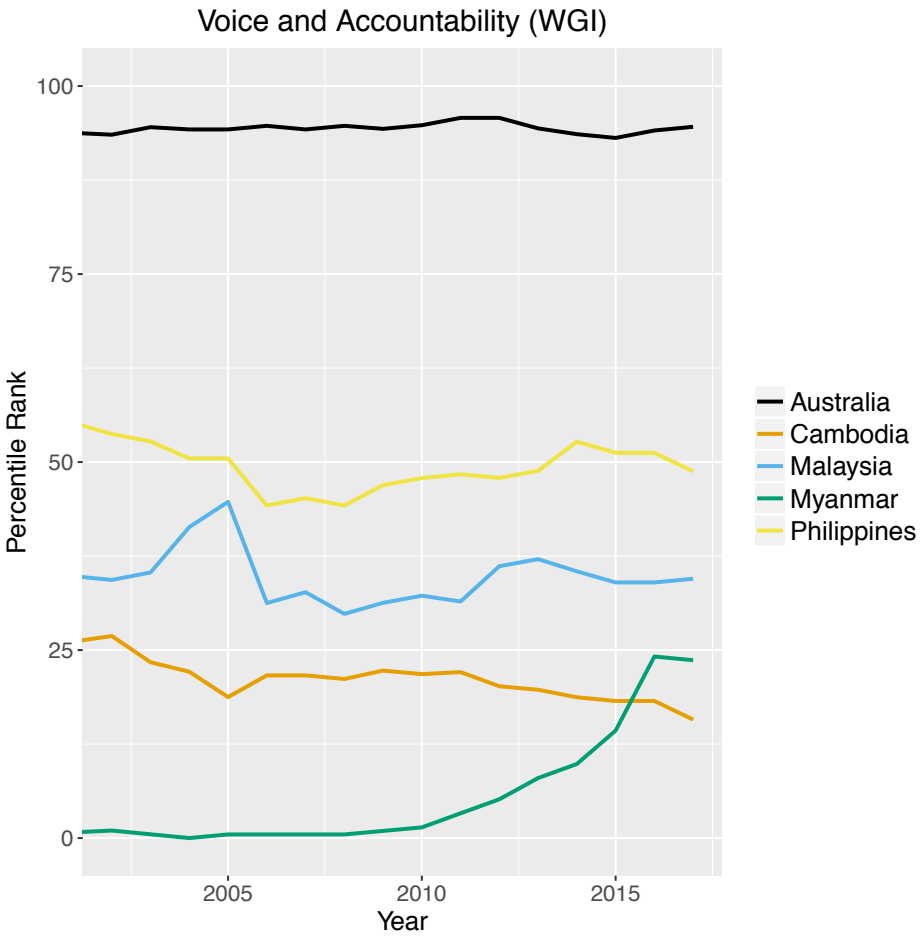

Figure 2.4: Accountability in selected country cases, measured by the World Bank Worldwide Governance Indicators. Higher ranked = more accountable.

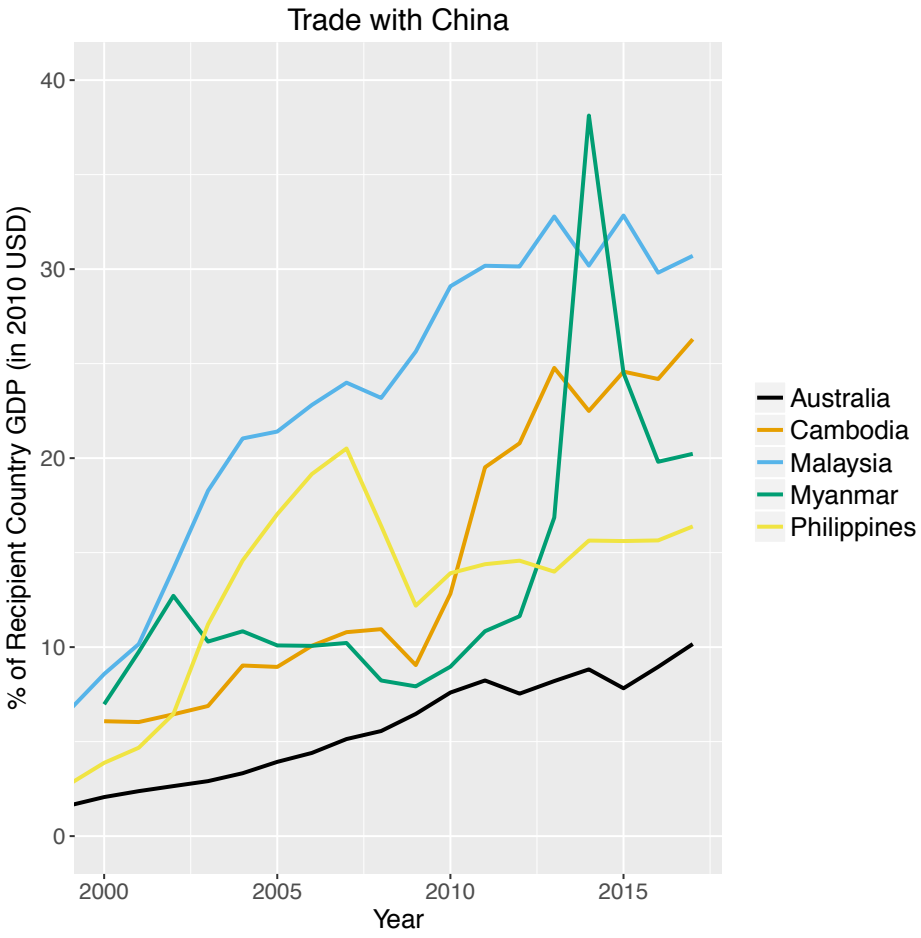

Figure 2.5: Trade with China as a percentage of GDP for selected country cases. Source: CEIC

Alternative Explanations

In this section, I discuss potential rival explanations for target countries' responses to China's economic inducements, including the extent of economic interdependence and structural security factors. I outline their corresponding predictions and observable implications, as well as the research design approach to assess the validity of these alternative explanations against my theoretical framework.

Degree of economic interdependence

One plausible rival explanation is that the target country's degree of economic interdependence (or dependence) on China would influence leaders' policy decisions. This is line with liberal arguments that continued economic interdependence promotes peace and reduces conflict.[91] Other scholars have discussed the broader spillover effects of economic interdependence (or dependence) on political and security outcomes – for instance, whether countries that have closer trade relations with China are more likely to support China's positions on human rights and other issues[92] Political elites in countries that have strong economic ties with China would be wary of the potential material costs from endangering an important relationship, and hence be more likely to support Beijng's policy positions.[93] The same reasoning could apply to the public, who would be supportive of closer economic ties. We should then expect to see minimal public opinion backlash and elite efforts to dampen any discontent relating to China's subversive carrots. In contrast, leaders whose countries are not reliant on Chinese trade and investment would have greater political space to allow public backlash.

However, many of the countries that have displayed political backlash against China's subversive car-

91. Copeland, "Economic interdependence and war: A theory of trade expectations"; Papayoanou, *Power Ties: Economic Interdependence, Balancing, and War*; Mansfield and Pollins, "The Study of Interdependence and Conflict: Recent Advances, Open Questions, and Directions for Future Research"; Mansfield and Pollins, *Economic Interdependence and International Conflict: New Perspectives on an Enduring Debate*.

92. Flores-Macías and Kreps, "The Foreign Policy Consequences of Trade: China's Commercial Relations with Africa and Latin America, 1992–2006"; Kastner, "Buying Influence? Assessing the Political Effects of China's International Trade."

93. Kahler and Kastner, "Strategic Uses of Economic Interdependence: Engagement Policies on the Korean Peninsula and Across the Taiwan Strait"; Flores-Macías and Kreps, "The Foreign Policy Consequences of Trade: China's Commercial Relations with Africa and Latin America, 1992–2006"; Kastner, "Buying Influence? Assessing the Political Effects of China's International Trade."

rots (including several of those examined in this book) have in fact close trade and investment ties with China. This includes developing countries that are reliant on investment from China and/or whose elites and often the public perceive China as an important source of investment financing – such as the Philippines, Malaysia, Sri Lanka, and the Maldives – as well as developed countries who have extensive trade ties with China – such as Australia, where trade with China constitutes around 10% of GDP. Such countries should be loath to reject China's subversive carrots. China's economic importance certainly figured into public debate. Yet, in all these cases, dissatisfaction with the manner in which Beijing's economic inducements violate political processes and institutions in their own country created significant public backlash and led to the backfiring of carrots.

Structural security factors

Another alternative explanation for the political outcomes of economic statecraft is the presence of structural geopolitical or security concerns that limits target country responses. Target country leaders are likely to respond poorly to economic inducements if concessions will be costly or create a reputation for being weak, particularly on issues that are salient or high stakes.[94] Examples include the presence of a security dispute between the target and sender states, or if the target has an alliance relationship with an adversary of the sender. With high stakes security issues, the costs of compliance will be higher, due to national security concerns as well as elite and public criticism.

To ensure that my theory is robust against this alternative explanation, I use a range of research design strategies in the book. First, I conduct a hoop test to show that outstanding security conflicts are not a necessary condition for backlash against China's economic inducements.[95] I draw on evidence from multiple country cases that have no security disputes with China (and thus face low costs of compliance over low stakes issues), yet experienced backlash against Beijing's carrots. This includes the cases of Australia, Myanmar, and Malaysia (the latter two are also not U.S. allies); together, these cases show the explanatory

94. Drezner, "The Trouble with Carrots: Transaction Costs, Conflict Expectations, and Economic Inducements"; Ang and Peksen, "When do Eonomic Sanctions Work? Asymmetric Perceptions, Issue Salience, and Outcomes."

95. Collier, "Understanding process tracing."

role of accountability mechanisms punishing inducements that violate political processes and institutions in the target countries, even in the absence of security disputes and across different levels of economic development.

In addition, I use process tracing within country cases that have security disputes – such as the Philippines – to establish the importance of accountability mechanisms in influencing leader decisions regarding China's subversive carrots. While security concerns or alliance ties can certainly factor into public opinion and political responses, as well as exacerbate any negative backlash, I show that the violation of domestic processes and institutions by subversive carrots is a major part of public discourse and a key driver of elite policy recalibration.

Evaluating these alternative explanations

All the above alternative explanations suggest that the target country would respond in the same manner, regardless of whether subversive carrots or stakeholder cultivation was offered. In contrast, my theory predicts that we would see variation in political outcomes within the same target country, depending on the manner in which inducements were offered by the sender state. For example, Chapter 4 demonstrates Malaysia's differing responses toward China's subversive carrots and stakeholder cultivation. Table 2.7 outlines the predictions of these alternative theories and their observable implications.

To assess the validity of potential alternative explanations, I use process tracing to identify the causal mechanisms leading to backlash against China's economic statecraft. Process tracing examines key intervening variables – such as the nature of public opinion and the content of political discourse – that link the hypothesized cause (how the economic inducement is offered) with the observed impacts on politician behavior and policy positions.

Drawing on evidence from field interviews and primary documents, I argue that the causal linkage between the sender's economic inducements and the target's foreign policy behavior centers on whether the proffered inducements violate or adhere to established political processes and institutions. Moreover, I show that this is consistent across country cases despite variation in alternative explanations, such as the degree of economic interdependence or the presence of structural security factors such as ongoing

Alternative Explanation	Prediction	Observable Implications	Disconfirmatory Evidence
Economic interdependence	High economic interdependence → Economic statecraft succeeds Both subversive carrots and stakeholder cultivation will succeed in achieving political outcomes	• Public opinion will prioritize economic benefits when supporting China • Political discourse and leader statements in target country will invoke China's economic importance in justifying political cooperation with Beijing	• Subversive carrots backfire in high accountability countries with high economic interdependence with China (e.g. Malaysia, Australia, the Philippines) • Subversive carrots and stakeholder cultivation have differing outcomes within the same country, holding economic interdependence constant
Security concerns	Presence of security disputes → Economic statecraft fails Both subversive carrots and stakeholder cultivation will fail at achieving political outcomes	• Public opinion will center on the existence of security concerns when criticizing China's inducements • Political discourse and leader statements in target country will invoke the existence of security concerns as rationale to reject China's inducements	• Subversive carrots backfire in high accountability countries without salient security disputes with China (e.g. Australia, Malaysia) • Stakeholder cultivation works in high accountability countries with salient security disputes with China (e.g. the Philippines) • Subversive carrots and stakeholder cultivation have differing outcomes within the same country, holding security concerns constant • Process tracing shows that dominant driver of backlash is the procedural violation of subversive carrots

Table 2.7: Alternative explanations and observable implications

security disputes or a U.S. alliance relationship.

Chapter 3

Reaping What You Sow: Backlash in the Philippines

In this chapter, I show that China's use of subversive carrots faces important limitations, even in seemingly corrupt, chaotic, imperfect democracies and developing countries. While subversive carrots may work in countries with low public accountability, the way in which they undermine and circumvent the target country's political processes also renders the use of subversive carrots vulnerable to public opinion backlash and domestic political shifts in countries with high public accountability. This limits the ability of subversive carrots to produce China's desired political outcomes.

In particular, I examine how the high public accountability of the Philippine system – with a free press, competitive elections, and civil society – caused China's subversive carrots in the mid-2000s to backfire. Major Chinese-led investment projects bypassed institutional and regulatory procedures, and were also implicated in high-level corruption. In return, Philippine leaders agreed to reverse positions on the South China Sea and signed cooperative agreements that violated the national constitution and threatened to undermine sovereignty. Because China's economic inducements undermined established political processes in the Philippines, this generated severe public opinion backlash and political opposition, ultimately forcing the cancellation of these economic deals.

Additionally, I consider the explanatory power of the public accountability argument against other potential alternative explanations for the observed backlash, including the presence of security disputes

and the degree of economic interdependence. Process tracing of case evidence points to the dominant consideration of China's procedural violations rather than an anti-China backlash driven by security concerns. Moreover, other Chinese-financed projects in the Philippines that followed a stakeholder cultivation approach have proceeded, and Philippine elites and the public remain eager for Chinese investment. Finally, I examine the role of public accountability under the current Philippine president Rodrigo Duterte, showing how accountability institutions have constrained his political inclinations toward China, while discussing a possible future weakening of such accountability institutions under his strongman rule.

The Accountability Backlash: Failure of Subversive Carrots in the Philippines

In the 2000s, under the administration of President Gloria Arroyo, Beijing offered subversive carrots to the Philippines, including major infrastructure deals in exchange for more concessional positions on the South China Sea. However, because these deals were agreed upon outside of the proper legal and institutional channels, China's carrots ultimately backfired under the Philippines' (relatively) high public accountability environment.

While corruption and patronage networks are not uncommon in Philippine politics, the presence of broader accountability mechanisms, including a free press, civil society, active political opposition, and open competitive elections, ensures that societal actors are able to acquire information about subversive carrots and exercise oversight of political leaders. Philippine media has had a reputation for being free, and has played a role in ousting former presidents.[1] Under conditions of high accountability, public opinion backlash and political criticism imposed domestic costs on Philippine leaders, thus acting as an important mechanism to constrain elite behavior and policy choices.

1. Sascha M. Gallardo and Aileen S.P. Baviera, "Filipino Media and Public Opinion on the Philippines-China Disputes in the South China Sea: A Preliminary Analysis," *4th International Workshop on "The South China Sea: Cooperation for Regional Security and Development, Ho Chi Minh City, Vietnam, 18-21 November 2012*, 2012,

Beijing's generosity in investments and loans was remarkable, particularly in building up the Philippines' underdeveloped infrastructure. This was all the more striking and unprecedented when contrasted with historical trends in the bilateral economic relationship. Even relative to other ASEAN countries, the Philippines has remained largely peripheral (for economic reasons) for Chinese trade, investment, and aid.[2]

Major projects included railway lines and a government broadband network. In 2003, China agreed to provide US$400 million via the China Export-Import Bank for the US$503 million, 20-mile long North Luzon Railway, or NorthRail. Subsequently, it agreed to another loan covering 95 percent of costs for the upgrading and extension of South Luzon Railway, adding up to US$932 million. In addition, a US$329.5 million deal signed in 2007 involved the development of the National Broadband Network (NBN), meant to establish an e-government presence throughout the country by linking 2,295 national offices and 23,549 village and municipal offices. China provided a twenty-year loan at 3 percent interest per annum, conditional on a Chinese company being appointed as the exclusive supplier and provider.[3]

The subversive nature of China's carrots

These carrots were offered in a subversive nature. The Chinese-financed infrastructure projects bypassed competitive bidding procedures, were vastly overpriced, and involved corrupt bribes and kickbacks. For example, the NBN deal was converted into a government-to-government agreement that bypassed the usual competitive bidding process. The contract was then handed to ZTE, a telecommunications company with close ties to the Chinese state. Government reviews later found that the contract had ballooned from US$130 million to US$330 million. The NBN project was allegedly brokered by Benjamin Abalos, chairman of the Philippines' Commission on Elections, who had cozy ties with ZTE. He extracted 'commissions' from ZTE in the name of the president and her political allies, which inflated the contract price, and offered bribes to Philippine government figures, including the director-general of the National Eco-

2. Tina S. Clemente, "Understanding the Economic Diplomacy between the Philippines and China," *International Journal of China Studies* 7, no. 2 (2016): 215–233.

3. Ian Storey, "Conflict in the South China Sea: China's Relations with Vietnam and the Philippines," *Asia-Pacific Journal: Japan Focus* 6, no. 4 (2008).

nomic and Development Authority (NEDA), the agency overseeing major infrastructure development projects. This amounted to $41 million in "advances," including $30 million to aid the administration in the upcoming 2007 elections.[4] The president's husband was also improperly involved in the process of securing the deal, while President Arroyo herself played golf with ZTE executives and attended the signing of the contract despite being aware of its corrupt nature.[5]

Parallel irregularities were found in the NorthRail project. This had originally been a Japanese-financed project that was stalled because the Japanese government was hesitant to ignore civil society opposition over local resettlement.[6][7] However, China did not have similar reservations. The project had two phases comprising a 2004 $400 million component (which subsequently underwent arbitration) and 2007 $600 million component (which was never started), and was contracted out to the Chinese SOE China National Machinery and Equipment Corp Group (CNMEG), now known as Sinomach. The deal involved the Speaker of the House of Representatives, Jose de Venecia Jr., who boasted of "convincing two Chinese presidents, two Chinese Prime Ministers, two Speakers of Parliament, and three Chinese Ambassadors to the Philippines for China to undertake the project."[8] The project was also massively overpriced, with the dubious honor of being the world's most expensive railway by unit distance.[9] Driven by de Venecia and other politicians from Central Luzon province, which stood to benefit from the project, NorthRail was found to have skipped over regulatory procedures. CNMEG conducted its own feasibility study, the project lacked qualified engineers, and the supply contract failed to specify required technical details and

4. Aileen Baviera, "The Domestic Mediations of China's Influence in the Philippines," in *Rising China's Influence in Developing Asia*, ed. Evelyn Goh (Oxford University Press, 2015).

5. "JDV confirms visit to China with Arroyos," *Rappler*, January 24, 2012; Leila B. Salaverria, "De Venecia: Abalos presence in China golf big surprise," *Philippine Daily Inquirer*, January 25, 2012.

6. Dennis D. Trinidad, "Institutional Mismatch and Chinese Aid in the Philippines: Challenges and Implications," *Asian Perspective* 40 (2016): 299–328.

7. Interview, National Economic and Development Authority, Manila, July 28, 2016

8. Roel Landingin, "Chinese foreign aid goes offtrack in the Philippines," in *South-South Cooperation: A Challenge to the Aid System?* (Reality of Aid Management Committee, 2010), http://www.realityofaid.org/wp-content/uploads/2013/02/ROA-SSDC-Special-ReportEnglish.pdf; Aileen S.P. Baviera, "The Influence of Domestic Politics on Philippine Foreign Policy: The case of Philippines-China relations since 2004," *RSIS Working Paper*, no. 241 (2012).

9. "Northrail contractor got paid $129M more," *Rappler*, September 11, 2013; Fidel Jimenez, "RP's Northrail project could be world's costliest railway - Drilon," *GMA News*, July 19, 2008; "PH renegotiates Northrail loan with China," *Rappler*, September 23, 2012; Miguel Camus, "PH, Japan seal P97-B commuter rail project," *Philippine Daily Inquirer*, January 29, 2016.

quality standards. It did include a 30% upfront payment in the financing terms, raising suspicions of political corruption.[10]

In tandem with accepting China's subversive carrots, Philippine leaders also altered policies on the South China Sea disputes. Manila and Beijing (later joined by Hanoi) signed the Joint Marine Seismic Undertaking (JMSU) in March 2005. The JMSU was a resource exploration agreement that permitted a Chinese national oil company to conduct a joint survey in the South China Sea,[11] involving an area of 142,886 square kilometers west of Palawan.[12]

However, in 2008, it was reported that the signing of the JMSU undermined existing legal and institutional procedures, and involved controversial policy concessions. Although the text and geographical location of the survey had been kept secret, journalists and analysts reported that a sixth of the designated survey area was in fact part of the Philippine continental shelf and thus outside of any disputed areas.[13] Another report claimed that around 80% of the JMSU was within the Philippines' exclusive economic zone (EEZ), and that the agreement had in effect acknowledged this area as disputed.[14] Figure ?? shows the geographical coverage of the JMSU and its overlap with the Philippines' EEZ. In addition, the Arroyo government had undercut ASEAN efforts to address the South China Sea disputes as a multilateral issue by choosing to deal with China bilaterally without consulting its Southeast Asian neighbors.[15]

Crucially, the JMSU violated the Philippine constitution. By law, the Philippine government is required to maintain "full control" over the exploration, development, and utilization of natural resources in Philippine territory (including the exclusive economic zone), and any joint ventures must involve corporations whose capital is least 60 percent owned by Filipino citizens.[16]

Moreover, the JMSU subverted established political processes and institutional procedures in the

10. Landingin, "Chinese foreign aid goes offtrack in the Philippines."
11. International Crisis Group, "Stirring Up the South China Sea (II): Regional Responses," *Asia Report*, no. 229 (2012); Storey, "Conflict in the South China Sea: China's Relations with Vietnam and the Philippines."
12. Ernest Z. Bower, "The JMSU: A Tale of Bilateralism and Secrecy in the South China Sea," *CSIS Southeast Asia from the Corner of 18th & K Streets* 1, no. 23 (July 2010).
13. Barry Wain, "Manila's Bungle in the South China Sea," *Far Eastern Economic Review* 171, no. 1 (2008): 45.
14. Miriam Grace A. Go, "Arroyo gov't pleasing China since Day 1," *ABS-CBN News*, March 14, 2008.
15. Wain, "Manila's Bungle in the South China Sea."
16. Attorney Neri Javier Colmenares,"Spratlys deal unconstitutional: Joint Marine Seismic Undertaking void," *GMA News*, March 17, 2008.



Figure 3.1: Map showing the geographical coverage of the JMSU and its overlap with the Philippines' EEZ. Source: International Crisis Group https://medium.com/@CrisisGroup/stirring-up-the-south-china-sea-iv-oil-in-troubled-waters-7d4b7286aac0

Philippines. Both foreign and Filipino journalists have charged that Arroyo agreed to the JMSU in exchange for an influx of corrupt Chinese financing.[17][18] As an illustration, in 2006 the Chinese government unexpectedly offered $2 billion of aid loans from its Export-Import Bank per year until 2010, easily dwarfing the $200 million offered separately by the World Bank and Asian Development Bank, and a $1 billion loan under negotiation with Japan.[19]

The agreement was pushed forward by two key political figures. The House Speaker, Jose de Venecia Jr., was again an important player and a key political ally of Arroyo. He also had very cozy ties with the Chinese government. De Venecia had helped to broaden international linkages with the Chinese Communist Party, and was linked with domestic oil interests (apparently, his website previously proclaimed himself as a 'believer in informal diplomacy and the role of parliament in back-channel conflict resolution'.).[20] Another political player was the president of the Philippine National Oil Company, Eduardo Manalac, who had close links with Chinese oil companies.

De Venecia apparently made commitments to his Chinese counterparts without consulting his Philip-

17. Baviera, "The Domestic Mediations of China's Influence in the Philippines."
18. Miriam Grace A. Go, "Arroyo gov't pleasing China since Day 1," *ABS-CBN News*, March 14, 2008.
19. Jane Perlez, "China competes with West in aid to its neighbors," *International Herald Tribune*, September 18, 2006.
20. Baviera, "The Domestic Mediations of China's Influence in the Philippines."

pine policy colleagues.[21] According to a senior career bureaucrat, and corroborated by others present, at a Christmas party in 2005, de Venecia declared that if Manila did not sign the JMSU, China would not give promised loans.[22] In other words, Philippine leaders' interests in extracting rents left them willing to make policy concessions to China. Although Congress should have been informed of any deal with a foreign government, interviews with Philippine lawmakers confirmed that the deal did not go through the proper legal proceedings.[23]

Furthermore, government bodies that would have normally handed such foreign and security policy issues, including the Department of Foreign Affairs, National Security Council, and even the Department of Energy, were sidelined during the JMSU negotiations. In fact, DFA bureaucrats had recommended against proceeding with the agreement, because it would violate the 2002 ASEAN Declaration of Conduct as well as the constitutional provision reserving resource exploitation rights in the Philippine EEZ to Filipino nationals.[24] Thus, China provided economic inducements in ways that undermined established political institutions and processes: regulatory processes and bureaucratic actors were sidelined; agreements were non-transparent and kept secret from Congress and the public; and constitutional requirements were violated.

Public Backlash: Transparency and Oversight

China's subversive carrots sparked strong public and political backlash in the Philippines. Public accountability mechanisms, in the form of transparency and oversight, imposed political costs on Philippine leaders for their policy decisions, and led to the cancelation of these Chinese-financed infrastructure projects. Moreover, evidence shows that the backlash was primarily against the violation of political processes and institutions in the Philippines, including the extensive corruption and the bypassing of required regulatory procedures.

21. Baviera, "The Influence of Domestic Politics on Philippine Foreign Policy: The case of Philippines-China relations since 2004"; Baviera, "The Domestic Mediations of China's Influence in the Philippines."
22. Interview, Filipino journalist, December 4, 2017.
23. Interview, Filipino journalist, December 4, 2017.
24. Baviera, "The Domestic Mediations of China's Influence in the Philippines," 112.

Informational transparency – the first component of public accountability – was a key mechanism facilitating public backlash. An active free press and an environment of open, even raucous political debate in the Philippines meant that information on China's subversive carrots could be revealed to the public, and that these issues could be discussed freely. This led to public and political backlash. In addition, public accountability facilitated oversight of Philippine leaders, who faced domestic political costs for accepting subversive carrots. They had to reverse their policy choices in response to public pressure, and further faced oversight and punishment through political and legal institutions. This ultimately led to the failure of China's subversive carrots.

Media reporting was instrumental in revealing information about these corrupt deals. A few days after the NBN-ZTE deal was signed in April 2007, a Philippine journalist broke the news about an "unnamed Comelec official" who played a role in approving the project. A Philippine lawmaker subsequently identified Abalos, the election commission chairman, as the individual in question.[25]

In addition, media coverage, public debate, and subsequent political oversight centered on the corrupt, subversive nature of China's economic inducements along with the implicated political figures.[26] Public debate also challenged the constitutionality of the JMSU, and criticized the lack of transparency on the agreement's terms.[27]

For example, the National Union of Peoples' Lawyers criticized the JMSU for violating the Philippine Constitution, called for public scrutiny of all agreements, and "urge[d] the people to assert their right to demand accountability."[28] A range of prominent political and economic actors openly criticized the corruption underlying Chinese-financed infrastructure projects. Former senior government officials slammed the Arroyo administration for undermining transparency and democratic processes, describing a "widespread clamor for truth and accountability."[29] A major business association issued a statement

25. "Timeline: Exposing the ZTE Overprice," *ABS-CBN News*, November 24, 2008.
26. "Ripe for reckoning," *Philippine Daily Inquirer*, March 15, 2012.
27. Baviera, "The Influence of Domestic Politics on Philippine Foreign Policy: The case of Philippines-China relations since 2004"; International Crisis Group, "Stirring Up the South China Sea (II): Regional Responses"; Storey, "Conflict in the South China Sea: China's Relations with Vietnam and the Philippines."
28. Atty. Neri Javier Colmen, "Spratlys deal unconstitutional: Joint Marine Seismic Undertaking void," March 17, 2008.
29. James Konstanin Galvez, "Critics blink on resign call: Look beyond resignation,' former Cabinet officials say," *Manila Times*, March 14, 2008; Efren L. Danao, "Lacson pursues broadband paper trail," *Manila Times*, March 15, 2008.

saying "we must see to it that those who are revealed to have broken the law, no matter how high up, must be made to account for their transgression."[30]

Furthermore, the Philippine government launched an extended investigation process, which was well-covered by the media. A Senate probe was re-launched regarding irregularities in the Northrail project.[31] The Senate also formed four working groups and held thirteen public hearings regarding the NBN-ZTE project between September 2007 and September 2008. The investigative process served to inform the public about intricate details of the case as well as to exercise oversight over the elites involved.

Key witnesses were called to testify during these hearings. A rival bidder for the ZTE contract claimed that the president's husband had told him to "back off" from the project and that Abalos had promised US$70 million in kickbacks to the First Gentleman. In addition, the NEDA director-general (and Secretary for Socioeconomic Planning) testifed that Abalos, the election commission chairman, had offered him US$3.7 million to approve the ZTE contract, and that he had informed President Arroyo about the bribe.[32] A NEDA consultant for the NBN-ZTE project further pinpointed Arroyo and her husband as "masterminds behind the NBN-ZTE crime" and described how promised kickbacks had inflated the price of the contract.[33]

Despite knowing about potential irregularities, and soon after her husband had undergone a major heart surgery operation, Arroyo proceeded with a 12-hour trip to China to be present at the signing of the agreement. According to Senate witness testimonies, the PRC ambassador to Manila had written a letter requesting her "personal attention to coordinate," and that ZTE officials had asked for Arroyo's presence as a precondition for releasing US$30 million in kickbacks to aid administration candidates in the 2007 legislative elections. In addition, documents showed that the president had given special authority to two Cabinet members to sign the NBN-ZTE deal and another MOU with ZTE. [34]

The Senate investigation produced a 200-page report by the Committee on Accountability of Public

30. Carlos H. Conde, "Business groups join fray in Philippine corruption scandal," *New York Times*, November 7, 2008.
31. Fel V. Maragay, "Senate probe of JdV's role in railway deal gains steam," *Manila Standard*, November 19, 2007.
32. "Timeline: Exposing the ZTE Overprice," *ABS-CBN News*, November 24, 2008.
33. "What went before: NBN-ZTE deal," *Philippine Daily Inquirer*, January 12, 2008.
34. Tony Bergonia, "Arroyo not just witness at NBN-ZTE deal signing," *Philippine Daily Inquirer*, March 6, 2008.

Officers and Investigations.[35] The report explicitly identified the implicated political figures and listed the national laws that they had violated.[36] It also criticized Chinese companies for undermining political institutions and processes. "It is also worth mentioning that ZTE should be warned in the manner that it conducts its business in the Philippines. While we welcome foreign investment, we only welcome investors who are wiling to abide with the laws of the Philippines and will not foment graft and corruption in government. ZTE should be mindful of its dealings with government officials and must act above suspicion that it is involved in any form of bribery.[37]

Similarly, the NorthRail project faced legal and political consequences. In 2006, a group led by an activist lawyer filed a lawsuit arguing that the deal had violated Philippine law on government procurement.[38] The Supreme Court turned down a petition by the Chinese SOE involved, NCNMEG, to halt legal proceedings, while a lower court ruled that the deal did not meet exemptions from procurement law.[39] The project was later terminated under the next president, Benigno Aquino III. After renegotiating the loan repayment with China, the Aquino government later revived the much-needed development project in early 2016, with a Japan ODA grant that had more favorable loan terms.[40]

As a result of the scandals, public opinion became much more negative toward China and toward the Philippine president. Figures 3.2 and 3.3 respectively show a sharp dip in public trust of China and approval ratings of President Arroyo around the time of the ZTE-NBN and JMSU scandals. Activists even launched a 'AB-ZTE-FG' protest ringtone to "let our call for truth and transparency ring across the country."[41]

In addition, several anti-government rallies were held in Manila and other cities protesting Arroyo's corruption, demanding greater transparency and accountability, and calling for her resignation. The Chinese-financed project scandals were seen as another spark for dissatisfaction and a symbol of the ad-

35. 'NBN-ZTE Scandal," Republic of the Philippines Senate Blue Ribbon Committee Report No. 743, November 11, 2009.
36. Republic of the Philippines Senate Blue Ribbon Committee Report No. 743, see e.g. p.2-3
37. Republic of the Philippines Senate Blue Ribbon Committee Report No. 743, p.125.
38. Trinidad, "Institutional Mismatch and Chinese Aid in the Philippines: Challenges and Implications."
39. Landingin, "Chinese foreign aid goes offtrack in the Philippines."
40. Miguel Camus, "PH, Japan seal P97-B commuter rail project," *Philippine Daily Inquirer*, January 29, 2016.
41. "Consumer protest group launches new ringtone: AB-ZTE-FG!" *Philippine Star*, September 25, 2007.

ministration's entrenched corruption and fraud. Some media outlets even described the case as having "grown to such proportion as to create a huge protest almost approximating the previous Edsa temblors," the latter a reference to past anti-regime popular movements.[42] The movement saw the participation of a diverse number of actors, including politicians, business groups, religious organizations, civil society activists, university students, lawyer groups, and leftist political groups.[43] In the words of the national bar association's president, "President Arroyo has committed another series of illegal and unconstitutional acts with her approval of the ZTE contract despite knowledge of the corruption that accompanied the transaction and the cover-up that ensued...We demand that all officials involved in the corruption that accompanied the ZTE contract and the other violations of our constitutional rights be held accountable."[44]

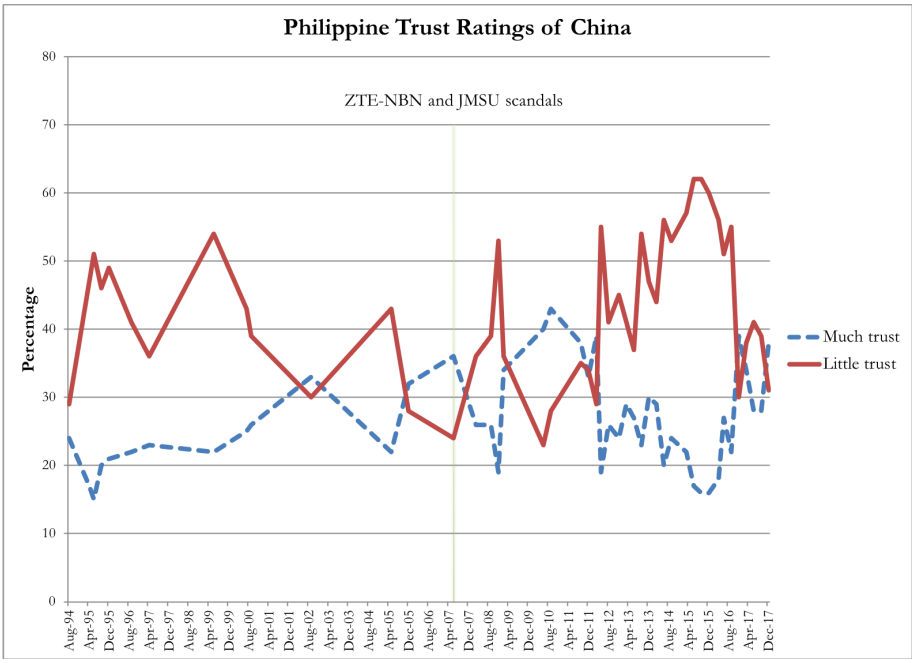

Figure 3.2: Philippine trust ratings of China. Data from Social Weather Survey, a public opinion polling institute in the Philippines.

Political pressure and public criticism forced President Arroyo not only to cancel the NBN-ZTE deal but also to suspend other Chinese-financed infrastructure projects and set up a special committee to re-

42. "EDITORIAL: The response to the bishops," *Manila Times*, February 28, 2008.

43. James Mananghaya and Jaime Laude, " 'Fellowship of the streets' " *Philippine Star*, February 29, 2008; "Rallies for truth and Arroyo resignation end peacefully," *ABS-CBN News*, March 1, 2008.

44. James Mananghaya and Jaime Laude, " 'Fellowship of the streets' " *Philippine Star*, February 29, 2008.

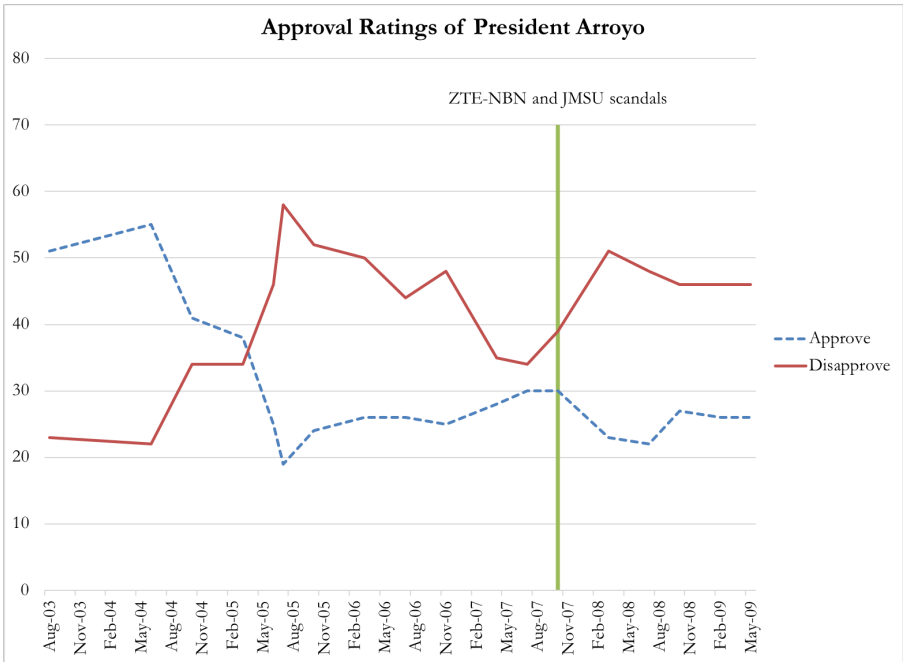

Figure 3.3: Philippine public approval ratings of President Gloria Arroyo. Data from Pulse Asia, a public opinion polling institute in the Philippines.

view these projects.[45] This included a US$1 billion dam construction deal to increase the drinking water supply in Metro Manila.[46] The JMSU was also allowed to lapse in June 2008. Philippine observers attribute this to public pressure and media coverage of the issue.[47] In May 2008, Philippine legislators had filed a petition with the Supreme Court to nullify the JMSU on the basis that it violated the Constitution.[48] In February 2010, Manila passed the Archipelago Baseline Act, which set forth Philippine sovereignty boundaries and "restricted the Philippine government from entering into future JMSU-like agreements without going through due process and transparency."[49]

Additionally, implicated Philippine elites faced legal punishment and political consequences. In the wake of the Senate hearings, the electoral commission chairman who had accepted Chinese bribes, Ben-

45. Aurea Calica, "Grand infrastructure projects pose corruption risks," *Philippine Star*, September 27, 2009; Raissa Robles, "Arroyo freezes US$2.45b projects funded by Beijing after ZTE scandal," *South China Morning Post*, October 6, 2007.
46. Landingin, "Chinese foreign aid goes offtrack in the Philippines."
47. Interview, Filipino journalist, December 4, 2017.
48. Tetch Torres, "SC asked to quash South China Sea tripartite deal," *Philippine Daily Inquirer*, May 21, 2008; Buena Bernal, "SC asked: Void expired PH-China offshore oil exploration pact," *Rappler*, May 29, 2014.
49. Bower, "The JMSU: A Tale of Bilateralism and Secrecy in the South China Sea."

jamin Abalos, resigned from his position.[50] He was subsequently charged and tried in court by government prosecutors.[51] The director-general of the National Economic Development Authority (NEDA), which oversees major infrastructure development projects, was also found guilty of misconduct.[52] A number of impeachment complaints and plunder cases were filed against Arroyo in connection with the NBN-ZTE project.[53] In late 2011, the Office of the Ombudsman charged Arroyo with graft and indicted her for playing golf and having lunch with ZTE officials while the deal was being evaluated by the Philippine government; her husband also faced bribery charges.[54]

The strongly-worded Senate Committee Report criticized these political figures as "scavengers and predators ready to feast on the carrions of their preys," and described the NBN-ZTE scandal as "a story of how people in high places…took advantage of their relationships…to cajole the Executive into entering a national broadband contract that would obtain something our country did not need, and which is manifestly disadvantageous to the Filipino people." The report concluded that "everyone in this story stands accountable to the Filipino nation."[55]

Beijing had thought that large-scale subversive carrots would be sufficient to buy political cooperation and accommodation from Manila – leading to an unpleasant shock.[56] The tendency of Chinese aid to operate through less transparent, more informal procedures (including the use of bribes and kickbacks) came into tension with Philippine institutions and rules governing aid that adhere to traditional DAC standards, such as transparency and competitive bidding.[57] As a result, China's subversive carrots met with significant political blowback once they were discovered to have circumvented and undermined political processes and institutions in the Philippines.

50. Carlos H. Conde, "Benjamin Abalos, Filipino elections official, resigns in a scandal that may threaten Arroyo," *New York Times*, October 1, 2007.

51. "Abalos conviction in NBN-ZTE case sought," *Rappler*, April 14, 2014. He was later acquitted.

52. Buena Bernal, "CA affirms guilty verdict on Neri in NBN-ZTE deal," *Rappler*, May 12, 2014.

53. Ruben D. Manahan IV, "GMA faces sixth plunder case over $330-million broadband deal," *Manila Times*, September 9, 2011; "What went before: NBN-ZTE deal," *Philippine Daily Inquirer*, January 12, 2018.

54. "Former Philippine president's husband arrested on bribery charges," *Associated Press*, March 13, 2012; "What went before: NBN-ZTE deal," *Philippine Daily Inquirer*, January 12, 2018.

55. "NBN-ZTE Scandal," Republic of the Philippines Senate Blue Ribbon Committee Report No. 743, November 11, 2009.

56. Interview, Tina Clemente, Manila, July 26, 2016.

57. Trinidad, "Institutional Mismatch and Chinese Aid in the Philippines: Challenges and Implications."

This underlines the importance of public accountability. In the Philippines, a free press, open political system, and legal institutions were able to ensure transparency and oversight. This resulted in major public backlash against China's use of subversive carrots. By imposing domestic political costs on Philippine leaders, accountability mechanisms played an important role in constraining elite behavior. Elites had to respond to public opinion and faced constraints from institutional enforcement and the rule of law. Domestic actors and institutions in the Philippines were able to enforce the requisite standards and punish political leaders for violating these standards. As a result, China's subversive carrots backfired and failed in changing the Philippines' foreign policy.

Alternative Explanations

A low degree of economic interdependence with China is an unlikely alternative explanation. As seen in Figure 2.3, the Philippines' trade with China as a proportion of GDP was actually very high during the case study period, even relative to most other Southeast Asian countries. This reflected the Arroyo administration's emphasis on economic cooperation with Beijing.

Another potential rival explanation for the backlash is that the Philippines is a dispute claimant in the South China Sea, making it more difficult for Beijing to change Manila's foreign policy. While the existence of territorial disputes certainly exacerbated negative perceptions toward China, close process tracing points to the importance of public accountability institutions in explaining the nature of the Philippines' response to China's subversive carrots. First, during the case study period in the mid 2000s, economic and political relations between the two countries had been on the upswing. Beijing was seen as a largely cooperative actor who was becoming more amenable toward multilateral security engagement; in 2002, China and ASEAN signed a much-anticipated Declaration on the Conduct of Parties in the South China Sea.[58] Territorial disputes were not as salient an issue for the Philippine public, especially compared to the period after 2012, when there was a physical standoff between the two countries over Scarborough Shoal.

58. Evan S. Medeiros and M. Taylor Fravel, "China's New Diplomacy," *Foreign Affairs*, 2003,

Second, as shown in the above analysis, much of the public and political criticism of the Chinese-financed infrastructure projects centered on the presence of corruption implicating the Philippine president and other political elites, as well as the unconstitutional nature of the JMSU agreement. Public demonstrations over these corruption scandals called for the resignation of the president, as opposed to being about anti-China rhetoric.[59] This supports the theoretical mechanisms of public accountability, which highlights the political costs of procedural violation, when leaders accept carrots that circumvent established political processes and institutions.

Third, stakeholder cultivation has worked in the Philippines despite security concerns. There have been successful instances of Chinese-financed projects in the Philippines, which would not be expected if ongoing security disputes were the main driver of public backlash. Other projects complying with Philippine regulations have made progress. A waterworks improvement project, initially suspended after the NBN-ZTE scandal, was successfully completed after both countries incorporated a limited contractor bidding process that complied with the Philippines' procurement law, in contrast to the scandal-ridden infrastructure projects that had been scrapped.[60] And soon after the NBN-ZTE deal was canceled, a consortium involving China's national power grid operator, State Grid, won an auction bid to manage the Philippines' electricity grid.[61] State Grid recently announced plans to install solar panel system for communities in a largely agricultural Philippine province whose administrative jurisdiction includes a former U.S. naval base (now a special economic zone) and the disputed Scarborough Shoal.[62]

Additionally, my field interviews with government officials and scholars in Manila highlight a continued ambivalence in public attitudes toward China. Despite concerns over sovereignty disputes, there remains plenty of eagerness for Chinese investment and aid. Given a desire for economic growth and infrastructure development, Beijing is seen as a major potential source of help. And as discussed in the following section, apparent interest in Chinese financing under the current Philippine president suggests

59. Carmel Crimmins, "Thousands gather in Manila for anti-Arroyo protest," *Reuters*, February 29, 2008.
60. Roel Landingin, "Angat aqueduct: rare success in China-funded infra projects in PH," *Rappler*, July 16, 2012.
61. Roel Landingin and Richard McGregor, "China State Grid group wins Philippine auction," *Financial Times*, December 12, 2007.
62. "China's State Grid to provide solar power for Zambales," *Philippine Daily Inquirer*, February 15, 2019.

that ongoing territorial disputes are not the predominant explanation for public backlash against China. In fact, public demands for greater transparency and government efforts to improve regulatory standards underline the mechanisms of public accountability in circumscribing any use of subversive carrots. Public backlash is not simply about anti-China sentiment, but about renegotiating the transparency and oversight of economic inducements.

Whither the Philippines under Duterte?

After the new Philippine president Rodrigo Duterte assumed office in June 2016, Beijing seized an opportunity to recalibrate the bilateral relationship, adjusting both its political rhetoric and economic statecraft. As president, Duterte announced a "separation" from the United States and a "springtime" in relations with China. Beijing's official statements started to adopt international legal language, indicating a willingness to open negotiations and use a "provisional arrangement of a practical nature" to settle disputes.[63]

China has also renewed its offers of economic inducements. During Duterte's visit to Beijing in October 2016, the two countries signed $24 billion worth of deals, including $15 million for investment projects, across a broad range of industries, and $9 billion in credit facilities. In late January 2017, a cabinet-level delegation from the Philippines finalized $3.7 billion worth of economic cooperation agreements, covering the fields of infrastructure, transportation, telecommunications, railways, irrigation, and living standards.[64]

Despite the declared optimism, infrastructure projects have been slow in moving forward, pointing to political caution on both sides as well as ongoing difficulties in resolving the terms and conditions of these agreements. Public accountability mechanisms in the Philippines have served to constrain leader behavior and policy decisions. Civil society groups have criticized the efficacy of infrastructure projects such as the proposed four-lane China Friendship Bridge in Manila, and Filipino public sentiment remains ambivalent toward China, with demand for "greater transparency and fairness around China's transactions with the Philippines".[65] Philippine observers, even those supportive of cooperative relations with

63. Interview, Chito Sta. Romana, former journalist and now Philippine ambassador to China, July 29, 2016.
64. "China, the Philippines confirm cooperation programs worth 3.7 billion USD," Xinhua, January 23, 2017.
65. Samantha Custer et al., "Ties That Bind: Quantifying China's public diplomacy and its "good neighbor" effect," *Aid-*

Beijing, have called for Chinese companies to "respect Philippine laws and regulations" and avoid "shortcuts by bribing Philppine officials."[66] My interviews with Philippine analysts suggest that public memory of past scandals would engender political backlash should any deals be found to be illegal.[67]

Domestic political institutions have also continued to hold political leaders accountable. Referencing the project scandals under Arroyo, Philippine senators have called for a review of the deals signed with China, specifically emphasizing the importance of transparency and accountability.[68] The Senate Minority Leader publicly stated that "it is imperative that we scrutinize these new deals to assess whether the agreements are consistent with the Constitution and our laws...We are prepared to go to court on this."[69] The Finance Secretary took pains to emphasize that the Duterte administration had learned lessons from the Arroyo's administration's "scandalous mismanagement of Chinese financing."[70] Newly announced Chinese-financed projects continue to face scrutiny by Philippine lawmakers.[71]

Furthermore, to reassure domestic skeptics and mollify public opinion, the Philippine government has institutionalized more stringent, regularized, and transparent procedures for Chinese financing. These efforts include greater transparency in the review and procurement process. The Philippine government now decides on the specific contractor, chosen from a list nominated by the Chinese embassy in Manila. Decisions on financing now has a new layer of bureaucratic mandate and be handled jointly by NEDA, allowing for more holistic review.[72] In November 2016, NEDA approved a new set of guidelines specifically focused on improving transparency and coordination when processing Chinese investment and aid activities. The Investment Coordination Committee (ICC) of NEDA acts as a clearing house for China-assisted projects. Manila has requested that China accredit qualified companies, which would then be

Data at William & Mary, June 2018, 26,28.

66. Kristin Huang, "Duterte's dilapidated hometown to get makeover with China's 'Belt and Road' investment," *South China Morning Post*, May 12, 2017.

67. Interview, Aileen Baviera, professor at University of the Philippines Diliman, December 2, 2017.

68. Paolo Romero, "Senate to review deals with China," *Philippine Star*, November 22, 2018.

69. Cecille Suerte Felipe, "Franklin Drilon seeks review of 29 Philippines-China deals," *The Philippine Star*, November 23, 2018.

70. "Dominguez on dealings with Chinese loans: We learned from past 'mismanagement'," *The Philippine Star*, December 6, 2018.

71. "DOF: China loan deal vetted vs graft," *Philippine Daily Inquirer*, March 1, 2019.

72. Interview, National Economic and Development Authority, Manila, July 28, 2016

screened and selected by the Philippine government.[73] This effort to improve regulatory oversight comes amid concerns that many of Beijing's newly pledged investments involve 'tainted' Chinese firms.[74]

Moreover, Philippine policy over the South China Sea disputes has remained fundamentally unchanged. The Duterte administration sent a high-level official delegation, led by the Defense Secretary and including Philippine military chiefs, to the disputed Spratly Islands, and started construction activities to repair structures on these islands.[75] Neither of these actions had been undertaken by recent Philippine governments. Philippine pilots have continued to patrol disputed areas in the South China Sea, despite intensified Chinese radio warnings.[76] Duterte himself has threatened war with China should 'red lines' be crossed, such as the unilateral extraction of natural resources in the South China Sea.[77] He has also criticized Beijing's construction of artificial islands and its efforts to claim the surrounding airspace and waters.[78]

At the same time, there are uncertainties ahead for existing public accountability mechanisms in the Philippines and how they will continue to circumscribe the effectiveness of China's subversive carrots. Duterte has floated talk of declaring a revolutionary government, which would essentially override any constitutional barriers and leave little to hamper China-Philippine deals.[79] Moreover, the media has also been "cowed," with major (critical) outlets such as the *Inquirer* and *Rappler* being sold to Duterte's political allies or facing attempts to buy out original investors.[80] Members of the Duterte administration

73. "NEDA Board approves Availment Guidelines for Chinese support for proposed PHL investments," Department of Finance, November 15, 2016; "NEDA-ICC to act as clearing house for China investments," *Philippine Star*, November 19, 2016.

74. Aaron Lozada, "'Tainted' Chinese firms eye new projects in Philippines," ABS-CBN News, October 26, 2016.

75. Lucio Blanco Pitlo III, "Duterte's Underappreciated Foreign Policy Gains," *PacNet No. 51*, Pacific Forum, July 25, 2018.

76. Patricia Lourdes Viray, "Philippine pilots continue to fly, disregard Chinese warnings – Palace," *PhilStar*, August 13, 2018, https://www.philstar.com/headlines/2018/08/13/1842192/philippine-pilots-continue-fly-disregard-chinese-warnings-palace.

77. "Philippine President Rodrigo Duterte will go to war with China if it crosses 'red lines' and claims disputed resources, foreign ministry warns," Associated Press, May 29, 2018, https://www.scmp.com/news/china/diplomacy-defence/article/2148204/philippines-rodrigo-duterte-will-go-war-china-if-it.

78. "Duterte: China should temper its behavior in disputed waters," Associated Press, August 14, 2018.

79. Interview, Filipino journalist, December 4, 2017.

80. Interview, Filipino journalist, December 4, 2017; Martin Petty and Karen Lema, "Philippines' Duterte blasts news site Rappler, but denies stifling media," Reuters, January 16, 2018, https://www.reuters.com/article/us-philippines-media/philippines-duterte-blasts-news-site-rappler-but-denies-stifling-media-idUSKBN1F50HL; Purple Chrystyl Romero, "Philippines' Duterte: From War on Drugs to War on Media?" *South China*

find it difficult to openly challenge the status quo due to the president's authoritarian governing style.[81] Changes in democratic checks and balances, including Duterte's consolidation of power, could affect the outcomes of China's subversive carrots, and shift the dynamics of Philippines foreign policy toward China and the United States.[82]

Conclusion

China's use of subversive carrots has backfired in countries with high public accountability. In this chapter, I examine the Philippines, but there are several parallel cases elsewhere. Negative public sentiment toward Beijing's subversive carrots – and the accompanying corruption and procedural lapses – in countries such as Malaysia, Sri Lanka, and the Maldives have resulted in Chinese investments becoming an electoral issue, leading to political incumbents losing office. Chinese analysts have acknowledged that a great power can provide economic benefits but may not always see desired results.[83]

Given that backlash has occurred in a number of countries often perceived as politically cozy with or economically dependent on Beijing, this underscores the importance of public opinion and accountability mechanisms in circumscribing the effectiveness of subversive carrots. China has also fumbled in trying to apply its subversive carrot strategy to more developed democracies. In Australia, the use of political donations through Chinese businessmen acting as a proxy for the Chinese government to alter legislator statements on the South China Sea created fierce public and political backlash. I further discuss the Australia case in Chapter 7.

The findings in this chapter suggest that China's attempts at using subversive carrots have not been as effective as many observers assume. Arguably, China's foreign policy is still on a learning curve. While Beijing has so far found it easier and more efficient to directly provide subversive carrots to political elites, it has perhaps started to realize that such a strategy is neither necessarily resilient to domestic political

Morning Post, January 20, 2018, https://www.scmp.com/week-asia/politics/article/2129536/philippines-duterte-war-drugs-war-media.

81. Custer et al., "Ties That Bind: Quantifying China's public diplomacy and its "good neighbor" effect," 25.

82. Richard Javad Heydarian, "Tragedy of Small Power Politics: Duterte and the Shifting Sands of Philippine Foreign Policy," *Asian Security* 13, no. 3 (2017): 220–236.

83. Interview, Southeast Asia analyst at Shanghai Academy of Social Sciences, Shanghai, July 20, 2016.

shifts nor sustainable in the longer run in a broader range of countries. For China or any other country seeking to exercise economic statecraft, a careful consideration of the target's domestic politics and level of public accountability will have strong implications for the attainment of desired political outcomes.

Chapter 4 presents a complementary case study of subversive carrots and stakeholder cultivation in another Southeast Asian country with moderately high public accountability, Malaysia, demonstrating the consistent explanatory power of procedural violation in determining target country responses across a range of potential confounders. In Chapter 5, I test the microfoundations of public accountability using a survey experiment in the Philippines, which examined public opinion responses to the two different inducement strategies - subversive carrots and stakeholder cultivation.

Chapter 4

Malaysia Renegotiates: Subversive Failure vs. Stakeholder Success

The May 2018 general election in Malaysia was characterized by harsh campaign rhetoric over Chinese-financed investment projects in the country and the accompanying extensive government corruption. As a result, the Malaysian opposition won an upset victory. Soon after coming into office, the new prime minister, Mahathir bin Mohamad, quickly suspended these major Chinese-led projects. In April 2019, after months of negotiations, the Malaysian government announced that a new deal had been struck to resume one of the most prominent infrastructure projects – the East Coast Rail Link – with modified terms and at significantly lower costs.

This chapter examines how public accountability mechanisms in Malaysia facilitated public and political backlash against China's subversive carrots – corrupt investment and infrastrucutre projects. Elites were punished for accepting subversive carrots. In addition, the nature of the political debate and controversy surrounding Chinese-financed projects, as well as the subsequent renegotiations, underscore how the response centered on *how* inducements had been offered – in a way that circumvented domestic political processes and institutions in Malaysia. In fact, public accountability constraints in Malaysia pushed elites to demand greater transparency and oversight of Chinese investments, and pressured Beijing to shift its strategy to one of stakeholder cultivation, offering inducements in an above-board manner.

Malaysia presents a hard test case given its close economic ties with China and its relatively robust political relationship. China is Malaysia's largest trading partner, its largest foreign investor, and its largest tourist market outside of Southeast Asia. Malaysia is also China's third-largest trading partner in Asia (after Japan and South Korea), accounting for around 25% of China's total trade to Southeast Asia.[1]

Apart from a high level of economic interdependence, Malaysia and China have long proclaimed a 'special relationship'. In 1974, Malaysia became the first ASEAN country to normalize diplomatic relations with Beijing, under the leadership of Abdul Razak (father of the recently ousted prime minster, Najib Razak). Kuala Lumpur has had relatively positive and stable ties with Beijing. Compared to other claimant countries, the Malaysian government has generally been more low-key in its approach toward the South China Sea disputes, which by and large it does not regard as a primary security or sovereignty concern.

This chapter further contrasts the Malaysian backlash against subversive carrots with its receptiveness toward – and the success of – China's use of stakeholder cultivation. While many other rival theories would predict a uniform political response toward China's economic statecraft, we in fact observe variation in outcomes within Malaysia, depending on how a particular Chinese investment project has been carried out. Amidst the backlash against and renegotiation of corrupt Chinese projects, the Malaysian government has pushed forward on other investments involving China that are above-board and that bring local benefits ie. stakeholder cultivation proved to be successful. This fits with the predictions of my theory of procedural violation.

In tandem with the Philippine case, the Malaysia case provides further evidence for the explanatory power of my theoretical framework – whether economic inducements involve procedural violation – in determining the political outcomes of China's economic statecraft. Through such cross-case comparisons, I show how my argument holds across a range of cases despite variation in the presence of potential alternative explanations.

1. Prashanth Parameswaran, "The Truth About China's 'Interference' in Malaysia's Politics," *The Diplomat*, October 2, 2015; Marvin C. Ott, "What Is Going on in Malaysia – and Why Does It Matter to the United States?" *The National Interest*, December 18, 2018, https://nationalinterest.org/feature/what-going-malaysia\T1\textemdashand-why-does-it-matter-united-states-39072.

Exposing Dirty Deals: China's Subversive Carrots in Malaysia

Again, media reporting was key in revealing information about corruption scandals, subversive carrots, and Beijing's involvement. PM Najib had been previously implicated in a money laundering scandal with Malaysia's state sovereign wealth fund, 1MDB, under investigation in several countries including the United States. According the the U.S. Department of Justice, US$4.5 billion was siphoned from 1MDB between 2009 and 2014, with the help of a Malaysian financier, Jho Low, and two former Goldman Sachs bankers. Najib, who founded 1MDB and chaired its advisory board, now faces over 40 criminal charges in connection with the scandal, and is accused of siphoning US$700 million into his personal bank accounts.[2] The laundered money was used to bankroll exorbitant lifestyles and purchases, including a US$27.3 million diamond necklace for Najib's wife, a US$3.2 million Picasso painting given to Leonardo DiCaprio, and the (ironic) financing of the movie "The Wolf of Wall Street."[3]

Subsequently, Beijing was found to have made a secret deal to bail out 1MDB and Najib's troubles. The *Sarawak Report*, a Malaysian newspaper with a record of digging up corruption scandals, revealed documents from a whistleblower in which the Malaysian government inflated the costs of a Chinese-financed rail project (the East Coast Rail Link, awarded to China Communications Construction Company, a Chinese SOE) by 100% – from RM 30 billion to RM 60 billion (almost US$14.5 billion). This "additional differential" was to cover the debts owed by 1MDB. CCCC would pay US$850 million to cover debts to a Saudi-Arabia sovereign wealth fund, and it also agreed to assume responsibility for US$4.78 billion in interest and principal from outstanding 1MDB debts.[4]

The contract was awarded to CCCC and the terms of the financing agreed upon before officials from a special-purpose vehicle set up to oversee the ECRL project were even brought on board.[5] In addition to CCCC being guaranteed the contract directly, thus bypassing competitive bidding, the company also

2. See e.g. Gigi Choy, "Explained: Malaysia's 1MDB scandal," *South China Morning Post*, February 16, 2019, https://www.scmp.com/week-asia/explained/article/2186477/explained-malaysias-1mdb-scandal.

3. Richard C. Paddock, "Malaysia Opposition, Led by 92-Year-Old, Wins Upset Victory," *New York Times*, May 9, 2018.

4. "Najib's Secret Deal With China To Pay Off 1MDB (And Jho Low's) Debts!" *Sarawak Report*, July 26, 2016, http://www.sarawakreport.org/2016/07/outrage-najibs-secret-deal-with-china-to-pay-off-1mdb-and-jho-lows-debts

5. M. Shanmugam and Jagdev Singh Sidhu, "ECRL - a Hobson's choice," *The Star*, May 19, 2018.

won favorable commercial terms such as a 10-year tax break and the ability to select its own suppliers and subcontractors. Malaysia also agreed to adopt Chinese rail technology in its infrastructure projects.[6]



Figure 4.1: Map showing original plans for the ECRL project. Source: https://www.scmp.com/news/asia/southeast-asia/article/2180576/future-massive-china-backed-malaysian-rail-link-hinges

The East Coast Rail Link (ECRL) constituted one of the largest and more prominent Chinese-financed investment projects in Malaysia (see Figure 4.1). The railway would connect the east and west coasts of Malaysia, spanning 430 miles (688 km). At a launch ceremony in August 2017, calling the project a 'game changer and a mindset changer for Malaysia,' then-PM Najib said that the project would be financed with an 85 percent loan from China Exim Bank (and the rest through local banks).[7] Project costs later ballooned to 81 billion ringgit, or US$20 billion, and the Malaysian media reported that only 15 percent of the work had been completed even though the government had already coughed up US$4.8 billion.[8]

The ECRL was part of a recent spree of infrastructure projects, including many financed by China.

6. See also Philip Bowring, "Desperate to Survive, Malaysia's PM Sells His Country to China," *Asia Sentinel*, August 10, 2016; Jeevan Vasagar, Caroline Binham, an Simeon Kerr, "China to help 1MDB settle multibillion-dollar legal dispute," *Financial Times*, December 6, 2016; Bhavan Jaipragas, "Has China offered to bail out Malaysia's 1MDB? At what cost?" *South China Morning Post*, December 7, 2016.

7. Liz Lee, "Hard-pedaling soft power, China helps launch $13 billion Belt and Road rail project in Malaysia," *Reuters*, August 9, 2017.

8. Hadi Azmi, "Malaysia Railway, Pipeline Projects Canceled, Mahathir Tells Chinese," *Benar News*, August 21, 2018, https://www.benarnews.org/english/news/malaysian/projects-stopped-08212018163217.html.

After a 2016 visit to China, Najib had returned with $34 billion of signed deals, including railway, port, pipeline, and real estate projects.[9] Chinese FDI into Malaysia increased by 119% in 2016 and grew 64% year on year in the first quarter of 2017.[10] Malaysia was expected to receive over the next two decades almost US$96 billion of Chinese investments.[11] Other projects included a US$100 billion property development project, Forest City, in Johor, as well as major port development projects and industrial park investments.

Another Chinese-financed venture that would come under scrutiny was a pair of pipeline projects. A subsidiary of the Chinese SOE China National Petroleum Corporation, China Petroleum Pipeline Bureau (CPPB) had been awarded contracts in November 2016 to build a 373 mile (600km) long oil pipeline along the western coast of the Malaysian peninsula, as well as a 411 mile (662km) long gas pipeline in the state of Sabah. To be financed through loans from the Bank of China, the contracts had been negotiated directly by former PM Najib's office, overruling red flags raised by the attorney general's office.[12] In addition, the pipeline projects and the ECRL were simultaneously approved by Najib's Cabinet in 2016 in the same document despite being unrelated, suggesting some irregularities.[13] According to the Malaysian finance ministry, project funding from China Exim Bank had been diverted to buy land in Penang that was owned by 1MDB, in order to bail out the scandal-ridden fund from its debts.[14] The new administration announced that the Chinese contractor had been paid 88% of the project's value – or US$2 billion – but had only completed 13% of the work.[15]

In January 2019, the *Wall Street Journal* reported on Malaysian government documents showing Bei-

9. Marvin C. Ott, "What Is Going on in Malaysia – and Why Does It Matter to the United States?" *The National Interest*, December 18, 2018, https://nationalinterest.org/feature/what-going-malaysia\T1\textemdashand-why-does-it-matter-united-states-39072.

10. Liz Lee, "Hard-pedaling soft power, China helps launch $13 billion Belt and Road rail project in Malaysia," *Reuters*, August 9, 2017.

11. Bhavan Jaipragas, "11 projects that show China's influence over Malaysia – and could influence its election," *South China Morning Post*, August 5, 2017.

12. "Malaysia to probe US$2 billion in payments made to Chinese pipeline firm under ousted ruler Najib Razak," *South China Morning Post*, June 5, 2018; Marvin C. Ott, "What Is Going on in Malaysia – and Why Does It Matter to the United States?" *The National Interest*, December 18, 2018, https://nationalinterest.org/feature/what-going-malaysia\T1\textemdashand-why-does-it-matter-united-states-39072.

13. Stefania Palma, "Malaysia suspends $22bn China-backed projects," *Financial Times*, July 4, 2018.

14. Stefania Palma, "Malaysia suspends $22bn China-backed projects," *Financial Times*, July 4, 2018.

15. Hadi Azmi, "Malaysia Railway, Pipeline Projects Canceled, Mahathir Tells Chinese," *Benar News*, August 21, 2018, https://www.benarnews.org/english/news/malaysian/projects-stopped-08212018163217.html.

jing's involvement in bailing out 1MDB in return for investment deals.[16] Minutes from 2016 meetings between Malaysian and Chinese officials show that Malaysian officials proposed that Chinese SOEs build the East Coast Rail Link and the gas pipeline in Sabah for "above market profitability." The chairman of China's State-owned Assets Supervision and Administration Commission (SASAC), which oversees Chinese SOEs, said that it was necessary to make the public to believe "all initiatives are market driven for the mutual benefit of both countries," and further mentioned that he had "cancelled all his key engagements in Beijing to attend" because the matter "has been approved by President Xi Jinping, Premier Li Keqiang"[17] – pointing to high-level involvement and approval from Chinese leaders. In addition, Chinese officials said they were surveilling and bugging WSJ journalists in Hong Kong reporting on the 1MDB scandal, and offered to use their influence to get other countries to drop their investigations into 1MDB.

Malaysian officials subsequently proposed that the Chinese SOEs involved in the projects would make payments that would "indirectly be used to repay 1MDB debt." Documents from September 22, 2016 stated that both countries agreed to move ahead with the infrastructure deals despite the fact that "they may not have strong project financials"; there was no need to "waste time studying the actual project financials to see if they can sustain the debt etc.," because the Malaysian government was supporting the deals for strategic reasons. Two months after that meeting, then-Prime Minister Najib signed the deals in Beijing.[18]

More generally, senior Malaysian government officials have described privately the existence of "Chinese middlemen" who serve as corrupt intermediaries interfacing with recipient country governments. These actors would approach the Malaysian government in search of infrastructure projects, offering financing at low interest rates – but at inflated project costs. Such middlemen representatives would often be part of Chinese embassy circles and attend government meetings, thus acquiring a veneer of being an official part of the Chinese government. They might also be affiliated with provincial governments in

16. Tom Wright and Bradley Hope, "China Offered to Bail Out Troubled Malaysian Fund in Return for Deals," *Wall Street Journal*, January 7, 2019.

17. Tom Wright and Bradley Hope, "China Offered to Bail Out Troubled Malaysian Fund in Return for Deals," *Wall Street Journal*, January 7, 2019.

18. Tom Wright and Bradley Hope, "China Offered to Bail Out Troubled Malaysian Fund in Return for Deals," *Wall Street Journal*, January 7, 2019.

China, requesting that a certain percentage of funds or workers in any agreed project would go to that province.[19]

One example is the China Rainbow International Investment Corporation (see Figures 4.2 to 4.5), an entity with minimal public information about the individuals involved or their claimed existing investments in Malaysia. A high-ranking government official in Malaysia (who requested anonymity) provided me with documents showing how CRIIC approached the Malaysian government in search of investment projects and offering their services as a liaison between Beijing and Kuala Lumpur. The organization also touted their previous expertise with existing Chinese investments in Malaysia, although their project descriptions and claims of involvement did not correspond with the actual situation. There was also very limited information available about the named representatives of CRIIC. According to the senior Malaysian official who was involved in making recommendations on this issue, the Malaysian government did not make any official response to CRIIC.[20]

19. Interview, senior Malaysian government official, Kuala Lumpur, June 2019.
20. Interview, senior Malaysian government official, Kuala Lumpur, June 2019.

中国虹桥国际投资有限公司
CHINA RAINBOW INTERNATIONAL INVESTMENT CO..LTD

Date: 1 June 2018

YB TUAN LIM GUAN ENG
Finance Minister
Ministry of Finance Malaysia
No. 5 Persiaran Perdana Presint 2,
Federal Government Administrative Centre,
62592 WP PUTRAJAYA
Tel : +603-8882 4526

Dear YB Lim Guan Eng,

INTRODUCTION TO CHINA RAINBOW INTERNATIONAL INVESTMENT CO., LTD AND REQUEST TO ESTABLISH A SPECIAL TASKFORCE TO HELP COORDINATE RELATIONS BETWEEN CHINA & MALAYSIA

Congratulations ***YB*** on being appointed as Finance Minister, Malaysia.

2. We are humbled to introduce ourselves to ***YB*** – China Rainbow International Investment Co., Ltd. (CRIIC) is a Chinese Investment & Financing Company owned by the All-China Federation of Returned Overseas Chinese and sanctioned by the Government of the People's Republic of China as a catalyst for the "One Belt, One Road" Initiative. We have a broad track record in financing major infrastructure and development projects around the world.

3. Throughout the past two (2) years; we have engaged considerably with the Government of Malaysia (specifically the Ministry of Finance) and had preliminarily finalised the financing and execution of the following national initiatives:

(i) Financing and the execution of the **Sabah Pan Borneo Highway** master development (at a provisional Gross Development Cost (GDC) of approximately MYR 25 Billion*; as advised by the Project Development Partner (PDP) and Ministry of Finance of Malaysia).

(ii) Financing and execution of the **MRT3** project (with a provisional Gross Development Cost (GDC) of up to MYR 55 Billion*; subject to Detailed Value Engineering);

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Figure 4.2: Letter from China Rainbow International Investment Co. to Malaysian Finance Minister, p1

(iii) 49% equity investment in the **Special Border Economic Zone (SBEZ) project at Kota Perdana, Bukit Kayu Hitam, Kedah** *(whereby we have paid a refundable earnest deposit of MYR 23.5 Million to the Government of Malaysia in order to commence Due Diligence studies for the said project)*.

It is pertinent to note that our proposals does not involve any front end/arranger fees; in order to ensure the efficiency and competitiveness of the aforesaid. Furthermore, the Interest Rate of our hybrid financing is approximately three percent (3.00%).

4. All our proposals include **local participation of Malaysian contractors at a ratio of 40% and above for each project**; in addition to our firm commitment to further increase local participation in the form of human resources, materials and expertise; as and where possible.

5. More importantly, we would like to formally assist the Malaysian Government in communicating with the Government of the People's Republic of China to discuss and address any concerns or sentiments that the Malaysian Government may have and to further strengthen relations between our two great nations via mutually beneficial bilateral trade investments and opportunities to partake in Government Infrastructure Projects including competitive financing options. For this we would like to humbly request to make an appointment with ***YB*** by inviting the following parties to have an open discussion (*we will require up to one (1) month to make the necessary arrangements*):

i. His Excellency Bai Tian the Ambassador Extraordinary and Plenipotentiary of the People's Republic of China to Malaysia;
ii. Representatives from **State-owned Assets Supervision and Administration Commission of the State Council** (SASAC), the commission responsible for managing most State Owned Enterprises (SOE's);
iii. **National Development and Reform Commission of the People's Republic of China** (NDRC), established to study and formulate policies for economic and social development, maintain balance of economic development, and to guide restructuring of China's economic systems.

6. We shall be making a formal visit to Kuala Lumpur, Malaysia on the **5th of June 2018**, till **7th of June 2018** and look forward to the opportunity of discussing the aforementioned agenda with ***YB***. The

Figure 4.3: Letter from China Rainbow International Investment Co. to Malaysian Finance Minister, p2

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name list of visiting dignitaries is attached as "***Appendix A***" to this letter.

7. We anticipate a more equitable business environment and sustained economic growth and stronger relations between China and Malaysia; and as such are keen to resume the implementation of our initiatives; or, alternatively, the discussion of other mutually beneficial modes of co-operation between our countries.

Thank you.

Yours faithfully,

KUHAN ARUNASALAM
Executive Director – Malaysia
China Rainbow International Investment Co., Ltd.

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Figure 4.4: Letter from China Rainbow International Investment Co. to Malaysian Finance Minister, p3

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Appendix A: List of attendees for the aforesaid formal visit on the **5th - 7th of June 2018** include:

a) Representatives from the **China Development Bank of Shaanxi**
   (i) Cheng Yongxu – Governor / President
   (ii) Wang Feng – Director of International Co-operation Department
   (iii) Qiu Zhiqin – Credit Division Manager

b) Representatives from the **China Construction Bank, Malaysia**
   (i) Felix Feng Qi – Governor / President
   (ii) Jaden Jia Peng – Senior Vice President

c) Representatives from the **China Rainbow International Investment Co., Ltd.**
   (i) Li Dacan – Chairman / President
   (ii) Kuhan Arunasalam – Executive Director, Malaysia
   (iii) Kisan Lim – Director of Operations, Malaysia
   (iv) Benny Ong – Business Development Manager

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Figure 4.5: Letter from China Rainbow International Investment Co. to Malaysian Finance Minister, p4

Accountability Backlash: Oversight and Punishment

Backlash over Chinese investments quickly became an electoral issue in the 2018 general elections. This included strong criticism of 1MDB corruption and its linkages with the non-transparent nature and high costs of the ECRL project.[21] Some observers drew a parallel with the backlash over Chinese investments under Arroyo and the subsequent victory of Aquino in the Philippines.[22]

The ECRL was one project singled out in campaign rhetoric for being corrupt and wasteful. During the election campaign, Mahathir promised to put Chinese-backed projects under greater scrutiny and renegotiation. He specifically criticized Chinese-led infrastructure projects for involving corruption and imposing terms that did not bring benefits to the local population or Malaysian businesses.[23] A prominent Malaysian economist, KS Jomo, had also cast doubt on the viability of the ECRL. Pointing out that the existing inter-city rail network only carries around six million tonnes annually, he contradicted claims that the ECRL would carry almost 60 million tonnes of freight annually by 2035.[24] He also criticized the ECRL as "designed to profit certain parties with a possible aim of covering up the lies and losses" relating to the 1MDB corruption scandal.[25]

Local politicians and the public also criticized Chinese investments for lacking transparency, with dissatisfaction on Najib's China policies often swaying votes to the opposition. One local entrepreneur interviewed in a Reuters report described Chinese investments as "fishy and don't seem to benefit the locals as we hoped for...Of 10 people that I know, eight people have already swung to Pakatan [the opposition party]."[26] Dr Ong Kian Ming, then an opposition party legislator and subsequently Deputy Minister Of International Trade and Industry (MITI) under the new Mahathir government, told international media

21. Interview, Cheng-Chwee Kuik, professor at National University of Malaysia (UKM), New York, April 13, 2018.
22. Richard Javad Heydarian, "What Mahathir's Return Means for China and the Region," *China-US Focus*, June 5, 2018.
23. Anisah Shukry and Yudith Ho, "Malaysia's Mahathir Pledges to Review China Investment if Re-Elected," *Bloomberg*, https://www.bloomberg.com/news/articles/2018-04-08/mahathir-pledges-to-review-china-investment-after-malaysia-vote; Richard Javad Heydarian, "What Mahathir's Return Means for China and the Region," *China-US Focus*, June 5, 2018.
24. M. Shanmugam and Jagdev Singh Sidhu, "ECRL - a Hobson's choice," *The Star*, May 19, 2018.
25. Bhavan Jaipragas, "Malaysia's ECRL: Officials flip-flop over future of US$20 billion China-backed project," *South China Morning Post*, January 30, 2019.
26. Liz Lee, "Selling the country to China? Debate spills into Malaysia's election," *Reuters*, April 26, 2018.

that "the Malaysia government needs to be fully transparent on the details of this deal...nothing comes for free and the Malaysian taxpayer deserves to know the true cost of the bailout."[27]

A fractured opposition – including former political rivals – united in an effort to defeat the ruling party, Barisan Nasional. 92-year-old Mahathir Mohamad came out of political retirement to lead the opposition coalition, Pakatan Harapan (PH), to an upset victory against Najib, his former protege. This was the first time BN had lost power in Malaysia's history, and was attributed to a wave of public opposition to Najib's large-scale corruption.[28] Pakatan Harapan campaigned on heavy criticism of Najib and a promise to fight corruption and demand accountability. In an interview with the Deputy MITI Minister, who is also a Member of Parliament from the PH coalition, he told me that a major driver for the change in government was about the issue of transparency and reputation, and "the inflated cost of the ECRL jives with the narrative of the previous government being non-transparent."[29] While the 1MDB scandal was a complicated and more abstract issue, the entanglement of specific Chinese-financed projects made it easy for politicians to use these projects as easy, powerful symbols and tangible examples of corruption and debts that would be paid across multiple generations.[30]

After coming into power, the new Mahathir government quickly announced the suspension and review of three major Chinese-financed investment projects – the ECRL and two pipelines – worth about US$22 billion.[31] Concerns centered on the lack of transparency and inflated costs, including large amounts of debt (estimated at US$250 billion).[32] Additionally, the new government pinpointed these projects as being directly implicated in Najib's corruption troubles, including the misappropriation of project funds from China's Exim Bank to bail out 1MDB debts.[33] Concurrent with these investigations, top Malaysian

27. Bhavan Jaipragas, "Has China offered to bail out Malaysia's 1MDB? At what cost?" *South China Morning Post*, December 7, 2016.

28. Alexandra Stevenson, "China Yields on Malaysia Rail Project as Global Infrastructure Program Is Re-Examined," *New York Times*, April 12, 2019.

29. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

30. Interview, Liz Lee, Reuters journalist, Kuala Lumpur, June 11, 2019.

31. "Malaysia suspends construction of major Belt and Road rail project," *Reuters*, July 4, 2018; "Malaysia suspends multi-billion dollar China-backed deals," *AFP*, July 5, 2018.

32. Richard Heydarian, "For Prime Minister Mohammad Mahathir, revisiting China's Malaysian projects is part of resetting a relationship," *South China Morning Post*, September 1, 2018.

33. Stefania Palma, "Malaysia suspends $22bn China-backed projects," *Financial Times*, July 4, 2018.

officials raised the possibility of renegotiating the terms of these Chinese-financed projects.[34]

In a 2018 interview with the *South China Morning Post*, PM Mahathir criticized past Chinese investments for operating in ways that "were not to Malaysia's advantage or even good for Malaysia." While he emphasized that "we welcome FDI from anywhere, certainly from China," he stated an opposition to projects in which "we gain nothing at all": "when it involves giving contracts to China, borrowing huge sums of money from China, and the contract goes to China, and China contractors prefer to use their own workers from China, use everything imported from China, and even the payment is not made here, it is made in China...that kind of contract is not something that I welcome."[35] The Deputy Minister for International Trade and Industry criticized the lack of transparency in such a financing model involving Chinese firms and Chinese banks, with disbursements done in China, because Malaysia had little access or information about the nature of such deals.[36] In another interview with *The New York Times*, Mahathir pointed to documents – a proposal from a Malaysian construction company – showing that the East Coast Rail Link could have been built for less than half of the contract awarded to CCCC.[37]

In line with the predictions of my theoretical framework, the new Malaysian government's policies toward China were marked by demands for greater transparency and fairness, rather than blanket anti-China sentiment. Mahathir has openly rejected claims that he is 'anti-China'. Soon after his election, he told foreign ministry staff in an internal memo that "our strong ties with China...will continue to flourish," met with the Chinese ambassador in Kuala Lumpur, and sent a key adviser (a prominent Malaysian-Chinese businessman) to discuss continued cooperation with China.[38] Both the prime minister and senior government officials have emphasized that they value good relations with China and welcome Chinese investment, as long as the terms are mutually beneficial for Malaysia.[39] During a August 2018 trip to

34. Philip Wen, "Malaysia investigates China-backed project links with 1MDB: official," *Reuters*, July 5, 2018.

35. Exclusive interview with SCMP, July 5, 2018, see footage here https://www.scmp.com/news/asia/diplomacy/article/2153984/malaysian-prime-minister-mahathir-mohamad-plans-visit-china.

36. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

37. Hannah Beech, "'We Cannot Afford This': Malaysia Pushes Back Against China's Vision," *New York Times*, August 20, 2018.

38. Coco Liu, "Robert Kuok part of Malaysian PM Mahathir Mohamad's plans for strong ties with China," *South China Morning Post*, May 24, 2018.

39. "China urges Malaysia to address project woes through talks," *Associated Press*, August 14, 2018; Bhavan Jaipragas, "'We

Beijing, even while publicly slamming Najib's corruption and 'stupidity' as well as referencing "unequal treaties", PM Mahathir took pains to clarify his stance on rectifying the 'lopsided' nature of Chinese-financed deals rather than an anti-Chinese position.[40] In spring 2019, Mahathir was the first world leader to confirm his attendance at China's second Belt and Road Forum, and later publicly expressed his support for Huawei's 5G technology.[41]

Actors outside of the Malaysian government have also echoed similar views on the problems of subversive carrots. Malaysian business leaders remained optimistic about overall Malaysia-China relations, viewing the review of Chinese-financed projects as a positive development and encouraging greater transparency to win public support. The CEO of YTL Group, a major infrastructure conglomerate in Malayisa, said that countries should "welcome [BRI] projects in a transparent way, hold them up to public scrutiny."[42] Even the Chinese government appeared to acknowledge Malaysia's position and its financial concerns, rolling out the red carpet for PM Mahathir's visit to Beijing. The foreign ministry adopted a positive tone on bilateral relations, saying that "we should approach these problems through friendly negotiations with the purpose of maintaining friendly ties and adopting a long-term view."[43] During a visit to Malaysia, the recently-elected prime minister of Pakistan described the two countries as being "in similar positions... We [Mahathir and I] both came into power after the people gave us a mandate on an anti-corruption platform. We face similar situations of unprecedented debt and so have a lot to share and talk about on dealing with the crisis and how to come out of it."[44]

Political elites also faced domestic political costs and punishment for accepting subversive carrots. At a post-election news conference, Mahathir emphasized that "the rule of law will be fully implemented.

like rich partners": Malaysia's Mahathir heads to China for fence-mending trip," *South China Morning Post*, August 16, 2018.

40. Bhavan Jaipragas, "Chinese 'projects will not go on': Mahathir blasts Najib's 'stupidity'," *South China Morning Post*, August 21, 2018; Bhavan Jaipragas, "Mahathir Mohamad. Malaysia's anti-China rebel? Not so fast …," *South China Morning Post*, August 22, 2018.

41. Tashny Sukumaran, "Malaysia 'values China': Mahathir signs up to Xi's second belt and road summit," *South China Morning Post*, February 15, 2019; "Dr M: Malaysia to use Huawei technology as much as possible," *The Star*, May 50, 2019.

42. Tashny Sukumaran, "Forget the US$23 billion question. China-Malaysia ties are strong," *South China Morning Post*, October 10, 2018.

43. Bhavan Jaipragas, "Mahathir Mohamad. Malaysia's anti-China rebel? Not so fast …," *South China Morning Post*, August 22, 2018.

44. Tashny Sukumaran, "In China's debt, Malaysia and Pakistan pledge to help each other," *South China Morning Post*, November 21, 2018.

And if the law says that Najib has done something wrong, then he will have to face the consequence."[45] Former prime minister Najib is facing extensive corruption charges. In addition to 32 charges for money laundering and graft, he was also charged with six counts of criminal breach of trust. These charges related to the Chinese-financed ECRL and pipeline projects as well as broader 1MDB transactions.[46] Other former senior government officials were also charged, including Najib's deputy and his treasury chief.

Renegotiation: A Shift toward Stakeholder Cultivation

Even while the Malaysia-China relationship appeared to be on rocky footing because of pushback on the ECRL (often portrayed in foreign media as a swing away from China), Malaysian leaders took pains to emphasize the continued importance of welcoming Chinese investment – subject to the constraints of transparency and accountability. Soon after his election, PM Mahathir told the SCMP that "we welcome investment, foreign investment from any country, so long as they bring in the capital, they bring in the technology, they set up plants here, and they employ Malaysians from workers to engineers, and they produce goods for the domestic market and for exports." [47]

The East Coast Rail Link was eventually renegotiated as a new agreement in April 2019. This process underscores two key observable implications of my theoretical framework. First, the Chinese-financed project itself was acceptable as long as it met conditions of accountability and transparency. That is, the backlash response to China's subversive carrots was driven by concerns over procedural violations of domestic institutions and standards, and not by other factors. Second, this accountability backlash against corrupt subversive carrots pushed Beijing toward a stakeholder cultivation approach in its economic statecraft, in an effort to improve its political success.

The long process of renegotiation centered on Malaysia's demands for a stakeholder cultivation rather than subversive carrot approach. At a corporate forum, Dr Ong Kian Ming, the Malaysian Deputy Minister for International Trade and Industry (MITI), told the audience that "we are reviewing the ECRL

45. Richard C. Paddock, "In Malaysia, the Old Prime Minister Promises a New Order," *New York Times*, May 10, 2018.
46. "Former Malaysian PM Najib faces six more corruption charges over state funds," *Reuters*, October 25, 2018.
47. Exclusive interview with SCMP, July 5, 2018, see footage here https://www.scmp.com/news/asia/diplomacy/article/2153984/malaysian-prime-minister-mahathir-mohamad-plans-visit-china.

project with China because of the high costs and lack of transparency in negotiations by the previous Government."[48] As Deputy Minister Ong said in another interview, "what we want to have is greater clarity, not just on the cost of construction but also the cost of operations...we want to be able to come to a win-win solution."[49] Given that the ECRL project itself was not a new idea, the pushback (and resulting renegotiation) was primarily about corruption, affordability, and the lopsided nature of the deal.[50]

The renegotiation process involved a broader range of stakeholders on the Malaysian side, with representatives from the relevant government ministries. The delegation included special envoy Tun Daim Zainuddin and a range of senior government officials from the Attorney General's Chambers, the Finance Ministry, and the Transport Ministry.[51] According to Daim, the fugitive financier Jho Low (previously implicated in the 1MDB scandals) had contacted him to offer to help in the negotiations, but Daim said that he had turned it down, saying "'Why don't you come back here? Come and brief me here.'"[52] Negotiations hit a stumbling block in late January 2019 when CCCC apparently could not meet the Malaysian government's requirements of reduced costs and including more local products and services.[53] However, in February, the Foreign Minister announced that "China understands our constraint and they're willing to scale down the size of the project and the cost. The discussion is probably in the last mile."[54] According to PM Mahathir, "If it must go on, the price must be affordable by us. But on the other hand if we build a railway line that is going to cost us a lot of money and give us no returns we just cannot afford to do that."[55] Recovering costs were apparently a major sticking point, given the amount of money that had been lost through government corruption in Malaysia.[56]

48. Ooi Tee Ching, "Malaysia looks to better transparency in BRI projects," *New Straits Times*, March 10, 2019.
49. Hari Raj, "Mahathir's Malaysia still 'open for business' with China despite stalled rail link: top trade official Dr Ong Kian Ming," *South China Morning Post*, February 28, 2019.
50. Interview Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.
51. Ida Nadirah Ibrahim, "Daim not sole broker in China renegotiations, ECRL firm clarifies," *Malay Mail*, May 9, 2019.
52. Justin Ong, "Daim: Jho Low tried to dangle aid in China during ECRL talks," *Malay Mail*, May 8, 2019.
53. Trinna Leong, "Malaysia cancels deal with China company, seeks new contractor for East Coast Rail Link," *Straits Times*, January 22, 2019.
54. "Malaysia nearing deal with China to revive scrapped ECRL, reports Bloomberg," *The Star*, February 19, 2019.
55. Bhavan Jaipragas, "Malaysian Prime Minister Mahathir Mohamad's exclusive interview in full," *South China Morning Post*, March 8, 2019.
56. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.

Ultimately, the new ECRL deal was modified to improve the terms and transparency, lower costs, and bring local benefits in line with procedural norms. The most prominent change was in the project costs: it was cut by one-third from the original 65.5 billion ringgit, or US$16 bilion, to 44 billion ringgit (US$10.7 billion).[57] Malaysia's lead negotiator, Tun Daim Zainuddin, said at a press conference that the cost of building each kilometer of the rail line would cost 68 million ringgit, down from 98 million ringgit.[58] Under the new memorandum of agreement, the project would be a 50:50 joint venture between CCCC and its Malaysian counterpart for the management, operation, and maintenance of the ECRL, whereas Malaysia would have had to bear the full costs in the original contract.[59] This would ensure that the Chinese contractor would "have skin in the game" rather than simply being a turnkey operator.[60] Malaysia would also retain 80% of any profits.[61]

In addition, China agreed to build industrial parks near seven stations on the rail link and bring in Chinese investors, in order to ensure the viability of ECRL as a cargo operator.[62] 40% of the subcontractors would also be Malaysians.[63] In May 2019, the Malaysian operator announced an open 'Pre-Qualification' tender exercise for all qualified local contractors to participate in these civil works projects, with the evaluation committee comprising senior officials from both the Malaysian and Chinese operators.[64] In a media interview, Malaysia's lead negotiator emphasized that Malaysian companies "should not expect tenders to be delivered to them, but that they must fight for these tenders. They have to show that they are competitive in terms of pricing, and that their work is on par with international standards."[65] Although there

57. Bhavan Jaipragas, "Malaysia to go ahead with China-backed East Coast Rail link," *South China Morning Post*, April 12, 2019.

58. Bhavan Jaipragas, "Malaysia to go ahead with China-backed East Coast Rail link," *South China Morning Post*, April 12, 2019.

59. "ECRL price tag can come down even further, says Daim," *The Star*, April 18, 2019.

60. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

61. Bhavan Jaipragas, "Top Mahathir adviser Daim says Malaysia's China-backed ECRL will be loss-making for some time, reveals surprising offer from fugitive financier Jho Low," *South China Morning Post*, May 8, 2019.

62. Interview, Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019; Bhavan Jaipragas, "Top Mahathir adviser Daim says Malaysia's China-backed ECRL will be loss-making for some time, reveals surprising offer from fugitive financier Jho Low," *South China Morning Post*, May 8, 2019.

63. Beh Yuen Hui and Mazwin Nik Anis, "ECRL is up and running again," *The Star*, April 13, 2019.

64. Danial Dzulkifly, "ECRL owner to launch scheme on civil works for local firms," *Malay Mail*, May 10, 2019.

65. Yu Pei-hua, Xie Wenwen, Zhang Yiou and Jason Tan, "Exclusive: Malaysian Negotiator Reveals the Story Behind Controversial Rail Deal's Resurrection," *Caixin*, May 15, 2019.

is a debate as to whether the ECRL negotiations ended up as "paying less to get less" in terms of smaller train gauges and lower speeds,[66] others argue that a high-speed rail would not have been feasible given the increased number of stops.[67]

Moreover, part of the negotiations included a commitment from Beijing to purchase more palm oil from Malaysia as well as bring in further investments in manufacturing and high-tech industries.[68] Citing high demand from China, the PRC ambassador to Malaysia told a media roundtable that "We are keen to increase the Malaysian palm oil trade and have been encouraging our companies to buy more Malaysian palm oil and related products."[69] Senior officials from different ministries were brought into the talks, and the lead negotiator, Tun Daim Zainuddin, told the media that the ECRL would have "new commercial elements that would have a greater impact on Malaysian companies and people....a lot more (projects) will come our way and we will get more profit."[70] In a statement issued after the ECRL deal, PM Mahathir said that "we chose to go back to the negotiation table and call for a more equitable deal, whereby the needs of the Malaysian people would be protected," explaining that the government's primary objection to the previous deal was the "unjustified" manner and speed in which the contract was signed under Najib – "a hefty lump sum price which lacked clarity in terms of technical specifications, price, and, by extension, economic justification."[71] Malaysian officials were optimistic that project costs could be lowered even further given the reduced loan amount and a possible expansion of the grace and repayment periods from China Exim Bank.[72]

Soon after the new ECRL deal, the Malaysian government also agreed to revive another China-linked RM140 billion project in Kuala Lumpur, a mixed-use property development project called Bandar Malaysia, to be built by a consortium comprising a local Malaysian company and China Railway Engineering Corporation. The plan was further modified to include 10,000 'affordable' homes, a 'people's park', and

66. Interview, Thomas Daniels, Analyst, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
67. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
68. Ho Wah Foon, "ECRL deal with China to include palm oil buy," *The Star*, April 8, 2019.
69. Ho Wah Foon, "ECRL to boost China investments," *The Star*, April 19, 2019.
70. Ho Wah Foon, "ECRL deal with China to include palm oil buy," *The Star*, April 8, 2019.
71. Ho Wah Foon, "New ECRL deal may become a case study for others," *The Star*, April 16, 2019.
72. "ECRL price tag can come down even further, says Daim," *The Star*, April 18, 2019.

prioritization of local firms and suppliers in the construction process.[73] This again points to Malaysian receptiveness toward China's stakeholder cultivation and Beijing's adjustment of its economic statecraft to better adhere to domestic needs and established political processes in Malaysia.

Top Malaysian officials have continued to emphasize transparency as an important lesson from earlier Chinese investments in Malaysia, as well as the political power of public backlash in recipient countries against China's attempts at subversive carrots. As Foreign Minister Saifuddina Abdullah said, "The lesson learned is that things must be done in a certain way. Transactions must be done by the rule of law. You have to be transparent about it."[74] The Deputy MITI Minister also stated publicly that "we must learn from the lesson of past BRI projects. Recipient countries must strengthen their evaluation and institutional frameworks in approving large infrastructure projects. "The foundation of any successful project is good governance and transparent procurement."[75] Additionally, in advance of the second Belt and Road Forum in April 2019, he highlighted the role of public backlash in shaping the political outcomes of Chinese investment: "More transparency helps deal with a backlash, in case questions are raised about financing...For China, having more transparent standards will minimise the risk of local backlash if any of the projects run into financial challenges."[76]

The 2018 general election provided an impetus for more transparent mechanisms on funding and sustainability as well as broader institutional reforms in Malaysia about how contracts should be awarded.[77] The government has started political reforms to make institutions more accountable to the legislature as opposed to the Cabinet, and increase oversight – for instance, the chair of the Public Accounts committee is now occupied by the opposition instead of being controlled by the ruling party.[78] The MITI Deputy Minister further suggested ways to increase transparency by disbursing funding through the host

73. Bhavan Jaipragas, "Mahathir's government agrees to revive China-backed Bandar Malaysia project," *South China Morning Post*, April 19, 2019.

74. Bhavan Jaipragas, "'Malaysia revived China deals to boost Belt and Road Forum spirits', country's foreign minister says," *South China Morning Post*, April 22, 2019.

75. Ooi Tee Ching, "Malaysia looks to better transparency in BRI projects," *New Straits Times*, March 10, 2019.

76. Dashveenjit Kaur, "More China-Malaysia engagement after ECRL revival, says Ong," *The Malaysian Reserve*, April 17, 2019.

77. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

78. Interview, Bunn Nagara, senior fellow at Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.

country or third-party countries, such as Hong Kong or Singapore, and to use the AIIB as a benchmark for appropriate standards.[79] As described by former ambassador to China and current director of the Malaysian Investment Development Authority (MIDA), Dato Majid Khan, Malaysia's – and PM Mahathir's – response as a "correction" to "shape Chinese investment as a positive presence" – that projects should follow the rules, be on equal terms, and mutually-beneficial.[80]

Addressing Alternative Explanations

Given the fact that Malaysia remains an ethnically-divided society and there have been ethnic tensions between the Malays and Chinese, one plausible alternative explanation for public backlash is the rise of anti-Chinese sentiment. However, when explicitly asked about this, none of my interviewees and conversations in Malaysia viewed ethnic tensions or anti-Chinese sentiment as a prominent factor in the pushback against Chinese-linked investment projects. While previous concerns during the Cold War was about potential links with the Chinese Communist Party, such rhetoric is less prevalent in the present-day era. Without denying the fact that Malaysia is still a very ethnically-divided society, local analysts argue that criticisms about the ECRL – and corresponding policy responses – centered on government corruption under Najib, the lack of transparency, and unfair terms.[81]

Political observers in Malaysia point to the corruption around ECRL as the main political issue surrounding the 2018 general election and as the driver of local pushback. Despite media speculation that Mahathir was targeting all China-backed projects,[82], another mega-scale real estate project by a Chinese developer, Forest City, has not been canceled. During the election, the project was criticized as catering to wealthy Chinese investors, but was not implicated in any government corruption scandals. Politically, it is seen as a private sector rather than a BRI-linked project.[83] While the issue of Forest City may have been

79. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

80. Interview, Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

81. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.

82. Sam Reeves, "Malaysian island city in trouble as prime minister targets China-linked projects," *Hong Kong Free Press*, September 5, 2018.

83. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.

politicized during the election campaign, Mahathir's policies are constrained as his governing coalition consists of ethnic Chinese politicians and parties.[84] Compared to Indonesia, the Malaysian Chinese population is larger (around 20%) and a more politically important part of the electorate.[85] In addition, when dealing with foreign policy, Malaysian political leaders have largely put aside domestic politics, including ethnic issues.[86]

Actual policy responses along with the continued receptiveness toward Chinese investments suggest that public backlash is primarily due to procedural violations rather than a blanket rejection of China's economic statecraft or pure anti-Chinese sentiment. According to the Malaysian Finance Minister, the government sought a "rebalancing" of the Forest City project to ensure that the development would not solely benefit rich foreigners, regardless of nationality.[87] To improve its image, subsequent phases of Forest City included plans for more affordable housing units, factory investments,[88] and a diversity of international buyers.[89]

In addition, national security concerns due to China's military presence or tensions over the South China Sea remain a marginal factor in dominant elite thinking. Overwhelmingly, China is seen as a "geographical fact"[90] and an opportunity rather than a threat.[91] In fact, some political leaders arguably subscribe to a narrative in which the United States is a new type of imperialist and poses a threat to regional security.[92] While Malaysia "won't be quiet" on key national security interests or on issues that affect regional stability, its elites view delinking economics and security as a "pragmatic approach" to manage the bilateral relationship.[93]

84. Liz Lee, Reuters journalist, Kuala Lumpur, June 11, 2019.
85. Interview, Cheng-Chwee Kuik, professor at National University of Malaysia (UKM), New York, April 13, 2018.
86. Interview, Peter Chang, Vice Chancellor at Institute of China Studies, University of Malaya, Kuala Lumpur, June 12, 2019.
87. Bhavan Jaipragas, "'Nice Chinese' hamper Malaysian hard bargaining over US$20 billion East Coast Rail Link," *South China Morning Post*, September 13, 2018.
88. Interview Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.
89. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
90. Thomas Daniels, Analyst, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
91. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
92. Thomas Daniels, Analyst, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.
93. Interview, Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

Moreover, there is a high level of economic interdependence between Malaysia and China. In media interviews, Mahathir said that he regarded China as "a good neighbor...and also as a very big market...we can't quarrel with such a big market as China."[94] While acknowledging China's economic importance, he emphasized the importance of mutually beneficial arrangements: "...our workers must find jobs from Chinese investments in Malaysia. So we have to look into what benefits us. To just negate or reject foreign direct investment from any country, including China, is not going to help us grow. We have grown in Malaysia largely through foreign direct investment."[95]

As such, Malaysian elites tend to view Beijing in terms of bringing more economic benefits rather than posing a security threat. Given high economic interdependence in tandem with low security threats, Malaysia presents a hard test for the failure of China's use of subversive carrots. The presence of procedural violations in economic statecraft – whether Chinese economic investments adhere to or violate domestic political processes and institutions – is likely to be a more salient factor for the Malaysian public and elites. That pushback occurred even amidst economic interdependence with China, and a broader desire for deepening economic relations with Beijing, shows the importance of having economic inducements adhere to domestic processes and institutions.

The Success of Stakeholder Cultivation in Malaysia

What about the outcomes of China's stakeholder cultivation in Malaysia? According to the logic of procedural violation, recipient countries such as Malaysia may reject subversive carrots but remain open to stakeholder cultivation. In particular, Malaysia has sought value-added and quality investments that would be open, fair, and employ more locals in high-tech and manufacturing sectors.[96]

Indeed, Malaysian officials have continued to welcome Chinese FDI that constituted stakeholder cultivation. According to the Deputy International Trade and Industry Minister, "we are still very open

94. Exclusive interview with SCMP, July 5, 2018, see footage here https://www.scmp.com/news/asia/diplomacy/article/2153984/malaysian-prime-minister-mahathir-mohamad-plans-visit-china.

95. Bhavan Jaipragas, "Malaysian Prime Minister Mahathir Mohamad's exclusive interview in full," *South China Morning Post*, March 8, 2019.

96. Interview, Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

for business and we still want to attract good quality Chinese investment to come to Malaysia."[97] In another interview, he stated that "many of the realized [Chinese] investments in the manufacturing sector have created good jobs and helped boost Malaysian exports." Over half of approved manufacturing FDI from Chinese firms in fact came after the May 2018 general election, with a total value of RM15.62 billion between January and September 2018, compared to RM4.7 billion in 2016.[98] PM Mahathir further highlighted this awareness of welcoming the right sort of economic cooperation with China: "the countries concerned must be able to distinguish what is allowable or needed by their country and what is not...you know capital flowing into the country exerts some influence over the country. So it is up to the countries concerned to make sure that the money flowing into their country is not borrowed money, is not money for infrastructure, but maybe limited to money for investment in productive processes."[99]

Other China-backed projects that were seen to be above-board continued amidst the suspension and renegotiation over subversive carrots such as the ECRL. For example, Malaysia proceeded with a joint shipbuilding venture, purchasing four littoral mission ships from China (costing US$72 million per ship). Comparing the ECRL and shipbuilding deals, a Malaysian analyst said that the renegotiation of the ECRL was "due to apparent irregularities and high costs" whereas the ship deal brought more benefits to Malaysia.[100] In January 2019, the Transport Ministry announced that China Railway Rolling Stock Corp (CRRC) would be expanding its train manufacturing center in Malaysia – where currently 85% of workers are locals – with hopes to build up the industry through technology transfer and joint ventures with local firms.[101] In June 2019, a Malaysian company (Eco World) and a Chinese SOE (PowerChina) signed a joint venture agreement to develop a RM850 million industrial park in Selangor to attract Chinese manufacturers relocating to Southeast Asia. The deal required shareholders' approval and company leaders emphasized "mutually beneficial partnerships," "high skilled employment opportunities for the

97. Hari Raj, "Mahathir's Malaysia still 'open for business' with China despite stalled rail link: top trade official Dr Ong Kian Ming," *South China Morning Post*, February 28, 2019.

98. Wong Ee Lin, "Ong Kian Ming: M'sia strongly committed to attracting FDI from China," *The Edge Markets*, January 22, 2019.

99. Bhavan Jaipragas, "I'd side with rich China over fickle US: Malaysia's Mahathir Mohamad," *South China Morning Post*, March 8, 2019.

100. Zam Yusa, "Some Bilateral Projects Halted, but Malaysia-China Ship Deal Sails On," *Benar News*, October 23, 2018.

101. John Bunyan, "With China's help, Malaysia can build trains too, says Loke," *Malay Mail*, January 3, 2019.

people of Selangor, and the "sourcing [of] industries from China that can contribute to the technology and skillsets in Malaysia."[102]

When asked what constituted a successful case of Chinese investment, the Malaysian Deputy Minister for International Trade and Industry pointed to Huawei.[103] Huawei has a data center, an R&D facility, and a training center in Malaysia. 60% of the 2000 workers being trained at Huawei's training center in Cyberjaya are locals. Malaysian workers were also sent abroad to countries in Africa and Central Asia to implement company projects and training programs.[104]

Another example of a successful project in progress is the Malaysia-China Kuantan Industrial Park (MCKIP), a US$2 billion joint venture between IJM, Malaysia's second-largest construction company, and Guangxi Beibu Gulf International Port Group. In spring 2019, the Malaysian government announced additional investments in manufacturing plants for industrial batteries and tyres.[105] Chinese firms have apparently made efforts to address local residents' concerns regarding jobs and environmental protection. Of the 6000 construction workers employed at MCKIP, 2400 are locals.[106] Alliance Steel, which is building a US$1.4 billion steel plant, employs 80% local workers, most of whom are also ethnically Malay.[107] To minimize environmental impact, the steel plant is supposed to recycle most of its water and will not have offsite wastewater discharges. In May 2018, the Malaysian government investigated claims that Alliance Steel had built an unauthorized water supply system and stolen US$125,000 worth of state-owned water during construction, prompting the Chinese company to pay back the costs. An associated US$1 billion expansion of Kuantan port also reduced local resistance by avoiding the displacement of local communities.[108]

Beijing has realized the importance of stakeholder cultivation and working with a range of domestic

102. "EcoWorld and PowerChina to develop industrial park in Selangor," *New Straits Times*, June 14, 2019.
103. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.
104. "Investments from China expected to surge, says Ong," *The Star*, April 18, 2019.
105. "Malaysia-China Kuantan Industrial Park welcomes tyre and battery factories," *New Straits Times*, April 3, 2019.
106. Keith Schneider, "Kuantan in the spotlight as Malaysia reviews Chinese deals," *Asian Correspondent*, August 24, 2018.
107. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.
108. Keith Schneider, "Kuantan in the spotlight as Malaysia reviews Chinese deals," *Asian Correspondent*, August 24, 2018.

actors, including different political elites as well as with local communities. In the past, China appeared "so close to the ruling party that it seemed to be supporting the party, not the government...this crosses a domestic red line."[109] CCP elites now meet with leaders from the formerly-opposition Democratic Action Party (DAP), and PRC Ambassador Bai Tian (who was previously seen on the campaign trail with the Malaysian Chinese Association, a party in the former ruling coalition) subsequently had to "eat lots of humble pie," even apologizing during a meeting with the DAP party chief and current Finance Minister Lim Guan Eng.[110] While the Chinese government initially seemed unenthusiastic to renegotiate the ECRL deal during Mahathir's visit to Beijing in August 2018, it subsequently realized the renegotiation was the best path forward.[111]

The Chinese government has also ramped up its public diplomacy. During the corruption scandals, the Chinese embassy in KL actively used social media to highlight cultural and historical similarities between the two countries.[112] To mark 45 years of diplomatic relations between the two countries in 2019, the embassy released a music video performed by a Malaysian and a Chinese singer, in Mandarin and Malay, describing the strength and warmth of bilateral ties. The song, titled "Left Shoulder", described Malaysia and China as "brothers through it all", saying "My right shoulder shelters you from the wind and rain; my left shoulder is for you to lean on."[113]

Political Payoffs: Beijing's Gains and Losses

While Malaysia has by and large adopted a hedging strategy toward China, promoting positive economic and political ties in tandem with continued strong relations with the United States, Beijing's economic

109. Interview Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

110. Interview, Dr Ong Kian Ming, Malaysian Deputy Minister for International Trade and Industry, Kuala Lumpur, June 13, 2019.

111. Yu Pei-hua, Xie Wenwen, Zhang Yiou and Jason Tan, "Exclusive: Malaysian Negotiator Reveals the Story Behind Controversial Rail Deal's Resurrection," *Caixin*, May 15, 2019.

112. Interview, Liz Lee, Reuters journalist, Kuala Lumpur, June 11, 2019.

113. Tashny Sukumaran, "'You are here for me for life': Beijing releases song marking 45 years of diplomatic ties with Malaysia," *South China Morning Post*, January 28, 2019; Allison Lai, "Chinese embassy composes song to celebrate Malaysia-China ties," *The Star*, January 28, 2019, video at https://www.thestar.com.my/news/nation/2019/01/28/chinese-embassy-composes-song-to-celebrate-malaysia-china-ties/.

statecraft has incurred both political gains and losses.

Subversive carrots arguably bought over a more acquiescent Malaysia under Najib's administration. Opposition politicians expressed concern that Chinese funds through the ECRL or other projects would be used to get Malaysia "to take a more pro-China position on the South China Sea dispute."[114] Although he did not make any major compromises on the South China Sea issue, Najib was noticeably silent given an uptick in Beijing's security presence in the disputed area. He did not criticize Chinese actions even as coast guard ships sailed near features claimed by Malaysia.[115]

In contrast to more active military responses by other claimants such as Vietnam, the Malaysian government ignored reports in 2015 that Chinese Coast Guard vessels were bullying Malaysian fishermen, and downplayed Chinese naval exercises at James Shoal in 2013 and 2014. An unnamed senior Malaysian minister complained to the media that "when the Chinese entered Indonesia's waters, they were immediately chased out. When the Chinese vessels entered our waters, nothing was done."[116] In March 2016, the government denied claims that around a hundred Chinese fishing boats had been detected in the Luconia Shoals, an area in the southern Spratlys claimed by China and administered by Malaysia.[117] Neither did KL issue any statement after an international tribunal ruling against China's activities in the South China Sea in July 2016.[118] After attending the ASEAN-China summit in 2017, Najib praised China for its positive response to reduce tensions in the South China Sea and said that "their commitment to ensure peace in the region has not changed."[119]

However, backlash against subversive carrots meant that they failed at buying over Malaysia's political silence in the longer term, and in fact reduced Beijing's political influence, with the incumbent kicked out

114. Amy Chew, "What has Malaysian leader Najib Razak's China trip got to do with 1MDB?," *South China Morning Post*, October 29, 2016.

115. Ralph Jennings, "Malaysian PM Shows Signs of a Bolder Stance on South China Sea," *VOA News*, June 25, 2018.

116. Joseph Sipalan, "As Beijing flexes muscles in South China Sea, Malaysia eyes harder response," *Reuters*, May 31, 2016 https://www.reuters.com/article/us-southchinasea-malaysia-idUSKCN0YM2SV.

117. Nyshka Chandran, "Malaysia's Najib Razak in China, as 1MDB scandal, South China Sea dispute loom over talks," *CNBC*, October 30, 2016, https://www.cnbc.com/2016/10/30/malaysias-najib-razak-in-china-as-1mdb-scandal-south-china-sea-dispute-loom-over-talks.html.

118. Ho Wah Foon, "China factor in the Asean stage," *The Star*, August 28, 2016.

119. D Arul Rajoo, 'Najib: China will work to reduce tension in South China Sea," *Malaysiakini*, November 13, 2017.

of office. Coming into office after Najib, Mahathir has been more vocal and critical on the South China Sea disputes. He made public statements reiterating Malaysia's sovereignty claims in the South China Sea,[120] saying that warships should be kept out and that Malaysia was determined to continue occupying the features currently under its control.[121] Mahathir also emphasized the importance of ensuring openness to navigation in the South China Sea,[122] and called for China to more clearly define its claims.[123]

At the same time, we see the buffering political effects of stakeholder cultivation in Malaysia. Without compromising on its sovereignty claims, the Malaysian government has refrained from sticking its neck out unnecessarily. Stakeholder cultivation has contributed to broader elite and public belief in China's economic importance and the value of maintaining positve diplomatic ties with Beijing. As discussed in the previous section on potential alternative explanations and the high level of economic interdependence between the two countries, stakeholder cultivation has created an atmosphere in which economic benefits are seen as greater than potential security concerns.

Finally, going beyond the political consequences within Malaysia, the country's responses to Chinese investment projects have also been an important symbol for the BRI's political success and for China's international reputation. While public and political backlash in Malaysia soured domestic and international attitudes on China's Belt and Road Initiative, Beijing's willingness to renegotiate the ECRL project and to adopt a more stakeholder cultivation approach bolstered its standing in the run up to the second BRI forum.

Conclusion

Examining the case of Malaysia, this chapter has argued that China's subversive carrots incited public and political backlash, whereas other Chinese investments that took a stakeholder cultivation approach were more successful. Evidence from field interviews and primary source documents underscores my theoret-

120. Ralph Jennings, "Malaysian PM Shows Signs of a Bolder Stance on South China Sea," *VOA News*, June 25, 2018.
121. Bhavan Jaipragas, "Forget the warships: Malaysian PM Mahathir's peace formula for South China Sea," *South China Morning Post*, June 19, 2018.
122. "Malaysia's Mahathir: South China Sea must be open to navigation," *ABS-CBN News*, March 7, 2019.
123. Jim Gomez, "Mahathir: China should define claims in South China Sea," *AP*, March 7, 2019, https://www.apnews.com/43df5211a5ec40c488261cbd53790ec5.

ical arguments that the manner in which economic statecraft is carried out – whether or not it adheres to domestic institutions and processes – was a major determining factor of the economic and political outcomes. While the presence of corruption, unfair terms, and the lack of transparency triggered pushback, the same project renegotiated (a la the East Coast Rail Link) proved to be politically palatable. Dissatisfaction with subversive carrots drove the public to vote the former prime minister out of office, and drove the nature of renegotiations and demands that the new Malaysian government exerted on China. As Andrew Polk, an economist and founder of a Beijing-based consulting firm, said of Beijing, "They've come in throwing around their weight in these places and not taking stock of local politics, and it's blown up in their face."[124]

The resilience of domestic institutions and processes remains key. Political observers point to the quality of governance in recipient countries (including Malaysia) as the source of problems, arguing that "we need to get our house in order."[125] In the words of former Malaysian ambassador to China Dato Majid Khan, "it depends on domestic institutions. If we're weak, China will take advantage. We internally need to be strong."[126] At the same time, instead of merely blaming host countries, Beijing should impose higher standards and requirements on its own companies, otherwise developments will be counterproductive for China's own image.[127]

The Malaysia case has also proved informative for China's conduct of economic statecraft, given Beijing's tendency to employ subversive carrots. The political shock from Malaysia's 2018 general election and the resulting pushback against subversive carrots has pushed Beijing to adopt stakeholder cultivation. While Beijing was insensitive in the past, the ECRL experience has compelled China to be more aware of recipient country needs, including transparency, environmental protection, and using local workers and

124. Alexandra Stevenson, "China Yields on Malaysia Rail Project as Global Infrastructure Program Is Re-Examined," *New York Times*, April 12, 2019.

125. Interview, Dr Peter Chang, Deputy Vice Chancellor, Institute of China Studies, University of Malaya, Kuala Lumpur, June 12, 2019.

126. Interview, Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

127. Interview, Dr Peter Chang, Deputy Vice Chancellor, Institute of China Studies, University of Malaya, Kuala Lumpur, June 12, 2019.

suppliers.[128] China is learning lessons and getting more sophisticated in its foreign policy. It has realized the importance of having a more politically-balanced approach, even in developing countries in Southeast Asia and Africa.[129] As Prime Minister Mahathir put it, "...we have put ourselves in a position where China has strong influence on our economy and maybe even our politics. But it is all up to us... we have to be on the lookout whether the influence of China over Malaysia would be detrimental to Malaysia's future."[130]

This chapter compared the outcomes of subversive carrots and stakeholder cultivation in one country, Malaysia. In the following chapter (Chapter 5), I again contrast the differing political outcomes of these two inducement strategies, but at the individual level. Using a survey experiment in the Philippines, I examine the effects of procedural violation on public attitudes and policy demands in a high accountability country, in order to test the microfoundations of my theoretical framework.

128. Interview, Bunn Nagara, Senior Fellow, Institute for Strategic and International Studies, Kuala Lumpur, June 13, 2019.

129. Interview, Dato Majid Khan, former Malaysian ambassador to China, director of the Malaysian Investment Development Authority, and chairman of the Malaysia-China Friendship Association, Kuala Lumpur, June 10, 2019.

130. Bhavan Jaipragas, "Malaysian Prime Minister Mahathir Mohamad's exclusive interview in full," *South China Morning Post*, March 8, 2019.

Chapter 5

Economic Inducements and Public Opinion: Survey Experimental Evidence

To complement the case study work presented above, I present results from a survey experiment designed to test the theoretical mechanisms of public accountability. My theory predicts that subversive carrots backfire in target countries with high levels of public accountability, whereas stakeholder cultivation is likely to be more successful. Public opinion plays an important role in a high accountability system. Transparency allows the public to acquire information on economic inducements offered to political leaders, and the public can also exercise oversight by imposing domestic political costs on elites (or potentially rewarding elites), thus constraining elite behavior and influencing policy cooperation with China.

Given the important mechanism of public opinion, a survey experiment helps to test my theoretical arguments by providing evidence of individual-level responses to different types of economic inducements within a target country. I examine effects on attitudes toward the sender state as well as policy preferences. In line with previous cases in this book, the survey experiment focuses on China as the sender state. An online survey experiment was conducted in the Philippines in June 2018. Before launching the survey, a pre-analysis plan was pre-registered at the Evidence in Governance and Politics (EGAP) website

(ID 20180607AA).[1] The experiment was designed based on my fieldwork experience in the Philippines, with the goal of maximizing external validity and ensuring the real-world relevance of my chosen outcome measures.

My results validate the mechanism of public opinion backlash in altering public views of China and related policy demands, and show how different inducement strategies – subversive carrots versus stakeholder cultivation – produce differing outcomes. These findings further emphasize the importance of public accountability in constraining the behavior of political leaders in target countries. In particular, subversive carrots have limited political effectiveness because they elicit public criticism and blowback, and reduce support for policy cooperation with China. On the other hand, stakeholder cultivation produces more positive public attitudes and greater support for policy cooperation with China.

Experimental Context

The Philippines is an active dispute claimant against China in the South China Sea, and a country where the nature and extent of China's influence has been a salient topic of debate among the public and political leaders. As such, the Philippines presents an important context in which to test the individual-level mechanisms of public accountability. The design of a survey experiment in the Philippines builds on my fieldwork experience in the country. The Philippines serves as a case of high public accountability, given the presence of free media, active political opposition, and open public debate. At the same time, the Philippines is classified as a lower middle income country by the World Bank, and marked by relatively poor infrastructure development, providing an opportunity for China to step in. China's growing economic presence and its use of economic inducements have received a mixed reception in the Philippines, including negative sentiment over project scandals in the mid-2000s, as documented in Chapter 2. Renewed enticement efforts under President Duterte, however, means that the political and economic implications of Chinese investment and aid projects are still frequently discussed in the public sphere. This salience makes the Philippines an ideal place to test the theoretical mechanisms of public account-

1. More details can be found at: http://egap.org/registration/4531

ability.

My field interviews and conversations in Manila with a range of academics, journalists, and diplomats over the past two years reveal fundamental tensions in public attitudes toward China and Beijing's economic inducements. On the one hand, many people are eager for Chinese investment and financing, seeing Beijing as a source of economic growth and development. On the other hand, there is a continued suspicion of Beijing's intentions, as well as a fear of being indebted to Beijing (a common phrase in Tagalog for this deep indebtedness is 'utang na loob'), particularly because of tensions over sovereignty disputes in the South China Sea. This suggests that there has not yet been a coalescing of public sentiment regarding China. At the same time, Duterte's current popularity and his publicly pro-China rhetoric would make respondents more likely to display positive attitudes toward Beijing, providing a hard test for my theory of public accountability and its mechanism of public opinion backlash.

Hypotheses

In line with my theoretical framework, focusing on the type of inducement strategy and the level of public accountability, I tested the following sets of hypotheses on the conditions under which economic inducements create a backfire effect:

(H1a) Inducements that subvert established political processes and institutions worsen public attitudes toward China.

(H1b) Inducements that subvert established political processes and institutions reduce public support for cooperative foreign policy toward China.

(H2a) Inducements that adhere to established political processes and institutions improve public attitudes toward China.

(H2b) Inducements that adhere to established political processes and institutions increase public support for cooperative foreign policy toward China.

Data Collection

A sample of N=925 was drawn using a Qualtrics online panel. Qualtrics panel providers email respondents with a link to take the survey. Aside from legal age restrictions (over 18), consent to participate, Filipino citizenship, and a gender quota, no other eligibility based on demographic factors was considered. More details on data collection and data quality can be found in Appendix Section 5.

The Qualtrics sample is not nationally representative, and tends to be more urban, educated, and middle-class. However, this middle class population represents an important, vocal constituency in Philippine electoral politics. I also use a key outcome measure on baseline attitudes toward China that is identical to a question from a nationally-representative survey conducted in the Philippines. The distribution of responses for my control population is similar to that from previous nationally-representative surveys, suggesting that my sample is similar on the most important baseline dimension to the overall Philippine population.

Experimental Design

The survey contained a total of 3 treatment populations: (i) T0, the control population, received a neutral, factual description of China's investment projects in the Philippines; (ii) T1 received a subversive prime in addition to the control vignette, discussing how China's inducements undermine established political processes and institutions in the Philippines; and (iii) T2 received a stakeholder prime in addition to the control vignette, discussing how China's inducements adhere to established political processes and institutions in the Philippines. Respondents were randomly assigned across the three treatment populations. Balance tables are presented in Appendix Section 5, Tables 5.4, 5.5, and 5.6, and show that the randomization is well-balanced on observed covariates. Summary statistics are presented in Appendix Section 5.

The three treatments, T0-T2, are presented in Table 5.1 below. T0, the control, describes a number of infrastructure projects agreed upon by the Philippine and Chinese government, to be financed by Chinese

banks and constructed by Chinese state-owned enterprises. Information on these projects, such as bridges in Manila, railways, and agricultural irrigation projects, are based on actual ongoing and proposed projects supported by Beijing. T1 (subversive carrots) and T2 (stakeholder cultivation) both include the same neutral information presented in T0 as well as an additional paragraph of four sentences describing the nature of these economic inducements from China. I explicitly design this paragraph to be structurally identical in T1 and T2, but with opposing content. This ensures that only the variable of interest – *the type of inducement strategy*, i.e. whether the economic inducements undermine or follow established political processes and regulatory procedures – changes across my treatments, and that this change can be clearly linked to any changes in the outcomes of interest.

The first sentence of this treatment paragraph states whether the infrastructure projects did or did not follow the proper processes of approval. The second sentence explains how these Chinese-funded projects were approved, either by top Philippine politicians who directly signed the deals with China and skipped the required regulatory procedures (T1), or through the submission of competitive project proposals in accordance with required regulatory procedures (T2). The third sentence then discusses the presence or absence of corruption: whether the Chinese government and Chinese companies offered bribes and kickbacks to Philippine politicians (T1), or no bribes and kickbacks were offered (T2). The final sentence of the paragraph describes public debate on the projects and the reactions of politicians and journalists: whether there has been criticism of these inducements as being non-transparent and circumventing established political procedures and rules (T1), or whether there has been praise for these inducements as transparent and in line with established political procedures and rules (T2).

The survey also included factual questions to verify that respondents had successfully taken up the given treatment. These questions were based on information provided in the treatment vignettes, and asked respondents to base their answers on that information. For T0, the question asked if the Chinese government is involved in infrastructure projects in the Philippines. T1 and T2 populations both received two uptake questions: whether Chinese-financed infrastructure projects follow proper government procedures, and whether they involve bribes and kickbacks to Philippine politicians. A respondent

T0: Control	Please read the following information carefully, which discusses some recent developments in the Philippines. In order to complete the survey, you will be asked questions based on the information provided below. The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enterprises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects.
T1: Subversive	Please read the following information carefully, which discusses some recent developments in the Philippines. In order to complete the survey, you will be asked questions based on the information provided below. The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enterprises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects. According to media reports, these projects did not follow the proper processes and rules of approval from government agencies. Instead, a group of top Philippine politicians directly signed the deals with the Chinese government and a few Chinese companies, skipping over the required regulatory procedures. Media reports suggest that the Chinese government and Chinese companies offered bribes and kickbacks to the Philippine politicians involved in the deal. Several politicians and journalists have criticized these agreements as being non-transparent and not following established political procedures and rules.
T2: Stakeholder	Please read the following information carefully, which discusses some recent developments in the Philippines. In order to complete the survey, you will be asked questions based on the information provided below. The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enterprises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects. According to media reports, these projects followed the proper processes and rules of approval from government agencies. The Chinese government and a few Chinese companies submitted competitive project proposals to the Philippine government, in accordance with required regulatory procedures. Media reports suggest that no bribes or kickbacks were offered to Philippine politicians as part of the deal. Several politicians and journalists have praised these agreements for being transparent and following established political procedures and rules.

Table 5.1: Survey primes for the three treatment populations T0-T2

was only considered to have fully taken up the treatment if he or she answered both questions correctly. The exact question wording can be found in the chapter appendix, Section 5, which includes the full text of the survey instrument.

Outcome Measures

My theory of public accountability predicts that public opinion imposes domestic political costs on leaders for accepting subversive carrots, which produce a backfiring effect. Negative public sentiment toward subversive carrots leads to negative perceptions of the sender state and its influence in the target country. In addition, the public will be less supportive of policy cooperation with the sender, less receptive to the sender's economic inducements, and will be more likely to punish politicians that favor closer cooperation with the sender state. Because political leaders are constrained by domestic public opinion in a high accountability country, they will make efforts to distance themselves from the sender, causing subversive carrots to fail in achieving desired political outcomes.

On the other hand, public opinion will respond more positively toward stakeholder cultivation, which creates positive perceptions of the sender state. The public will then be more likely to support policy cooperation with the sender state, be receptive to further economic inducements, and will support politicians who favor closer cooperation with the sender. In response to positive public opinion, political leaders will be more inclined to build closer ties with the sender state and align more closely with the sender's foreign policy preferences.

To test my theoretical framework, in the survey, I selected five outcome measures that serve as observable indicators for the mechanism of public opinion outlined above. These five outcome measures fall into two main categories: (i) attitudes toward China, and (ii) attitudes on policy cooperation with China. To assess public attitudes toward China, respondents were asked to evaluate how positive or negative Chinese influence in their country is, and how much the Philippines should trust China. To determine attitudes on foreign policy toward and cooperation with China, respondents were asked their level of support for a joint resource exploration agreement with China in the South China Sea, their level of support for local politicians in favor of investment projects with China, and their preferred foreign country

investor for an upcoming national railway project.

The wording of these five main survey questions is presented in Table 5.2. The two outcome measures for assessing respondents' attitudes toward China are taken from major, nationally-representative surveys conducted in the Philippines. The question on attitudes toward Chinese influence is taken from the nationally-representative Asian Barometer Survey, a regular series of cross-national surveys across several countries in Asia. The question on levels of trust in China is taken from the Social Weather Station survey, a prominent domestic public opinion polling organization in the Philippines.

In addition, the outcome measures were designed whenever possible to reflect the real-world context of policy issues in the Philippines, in order to increase the external validity of the survey experiment. In particular, the content of Indicator 3 (support for foreign policy cooperation in the form of a joint resource exploration agreement) is based on ongoing, politically-contentious discussions in the Philippines about whether to sign such an agreement with China. Indicator 5 (the choice of investor for a national railway project) also reflects the Philippines' actual policy priorities of developing large-scale infrastructure, and China's prominent role in many of these projects.

Results

Figure 5.1 shows the treatment effects for T1 and T2, each measured against the control, T0, as the baseline. I present results for both the full population and a subsetted population conditional on treatment uptake.[2] Appendix Sections 5 and 5 present the regression results for both the full and uptake T1 and T2 populations. Results remain robust with ordered logit models, presented in Appendix Sections 5 and 5.

Subversive carrots had a strong adverse effect – both substantively and statistically – on public attitudes toward China and public preferences for cooperative foreign policy toward China. When stakeholder engagement was used, respondents were moderately more positive, although the results were not as strong. The results became even more substantively and statistically significant when analysis was restricted to respondents who successfully uptook the treatments. As specified in the pre-analysis plan, all

2. 96.8% of T0 respondents, 69.4% of T1 respondents, and 75.5% of T2 respondents fully uptook the given treatment.

Outcome	Indicator	Question
Public attitudes	*1. Perceptions of Influence*	"Generally speaking, the influence China has on your country is?" (1-6 Likert Scale + additional option "Decline to answer")
	2. Levels of Trust	"Generally speaking, how much do you think the Philippines can trust China?" (1-4 Likert Scale)
Policy preferences	*3. Support for Foreign Policy Cooperation*	"The Philippine government is conducting talks with the Chinese government about signing a joint resource exploration agreement, which would allow Philippine and Chinese companies to explore for oil and gas in the South China Sea. This would include areas off the coast of Palawan where the Philippines has economic rights and where China has also disputed Philippine claims. The agreement would likely lead to future joint development of natural resources in those areas involving China and the Philippines. How much do you support or oppose this agreement?" (1-4 Likert Scale)
	4. Support for Pro-China Politicians	"How much would you support or oppose your congressional district representative if he or she is involved in promoting the Chinese-financed infrastructure projects discussed earlier?" (1-4 Likert Scale)
	5. Receptiveness to Economic Inducements	"The Philippine government has recently proposed a national railway project in the Philippines, and is looking to partner with an outside investor. This investor will help to build and finance the project. Which of the following countries would you prefer to be the project investor?" (order of options is randomized among four countries: China, Japan, United States, South Korea)

Table 5.2: Question wording for outcome measures

models controlled for age, gender, education, income, employment status, and support for Duterte.

When presented with information on how China's economic inducements undermined political processes and institutions in the Philippines, respondents' perceptions of China's influence in the Philippines became significantly more negative, decreasing by 0.86 points on a 1-6 scale, or just over 17%. Similarly, trust in China decreased by 0.30 points on a 1-4 scale, or 10%. Respondents also grew more skeptical of economic and political cooperation with China. Support for Philippine politicians who favored greater Chinese economic presence dropped by 0.35 points (also on a 1-4 scale), or just under 12%. Respondents also became 10% less supportive of a joint resource exploration agreement with China in the South China Sea, and were 3% less receptive to China as an investor relative to other countries. These results provide strong evidence for the mechanism of public backlash and for a major backfiring effect when China uses subversive carrots that undermine political institutions and processes in high accountability countries.

On the other hand, China's use of stakeholder cultivation was able to improve respondents' attitudes toward China, improving perceptions of China's influence by 0.24 points (on a 1-6 scale, or about 5%) and the degree of trust in China by 0.20 points (on a 1-4 scale, or 7%). Effects on policy demands and politician support were somewhat positive but less significant. I identify two potential explanations. First, the information provided to the control population, while factual, may dampen the treatment effect for T2, as the notion of incoming investment projects is possibly seen as a positive change in itself, not least in the Philippines, where infrastructure development is poor. Second, survey respondents are likely to have previously been exposed to information on past scandals involving Chinese investments in the Philippines, suggesting that it is much harder to positively alter public mindsets about the sender state once its reputation has been adversely affected. This result holds important lessons for the importance of choosing the appropriate economic inducements, as subversive carrots can have long-term, negative implications on public opinion.

Finally, as a secondary analysis, I also directly compare the difference in public attitudes and policy preferences between the use of subversive carrots and stakeholder cultivation. This comparison reflects the real-world policy choice between the two types of inducement strategies, Figure 5.2 presents the treat-

ment effects of T1 (subversive) versus T2 (stakeholder). The large, significant effects again underline how subversive carrots and stakeholder cultivation produces very different political outcomes in a high accountability country, not just in terms of attitudes toward the sender state, but also in terms of major spillover effects on policy preferences regarding the sender, including the degree of support for closer foreign policy cooperation as well as support for political leaders seen to be closely aligned with the sender.

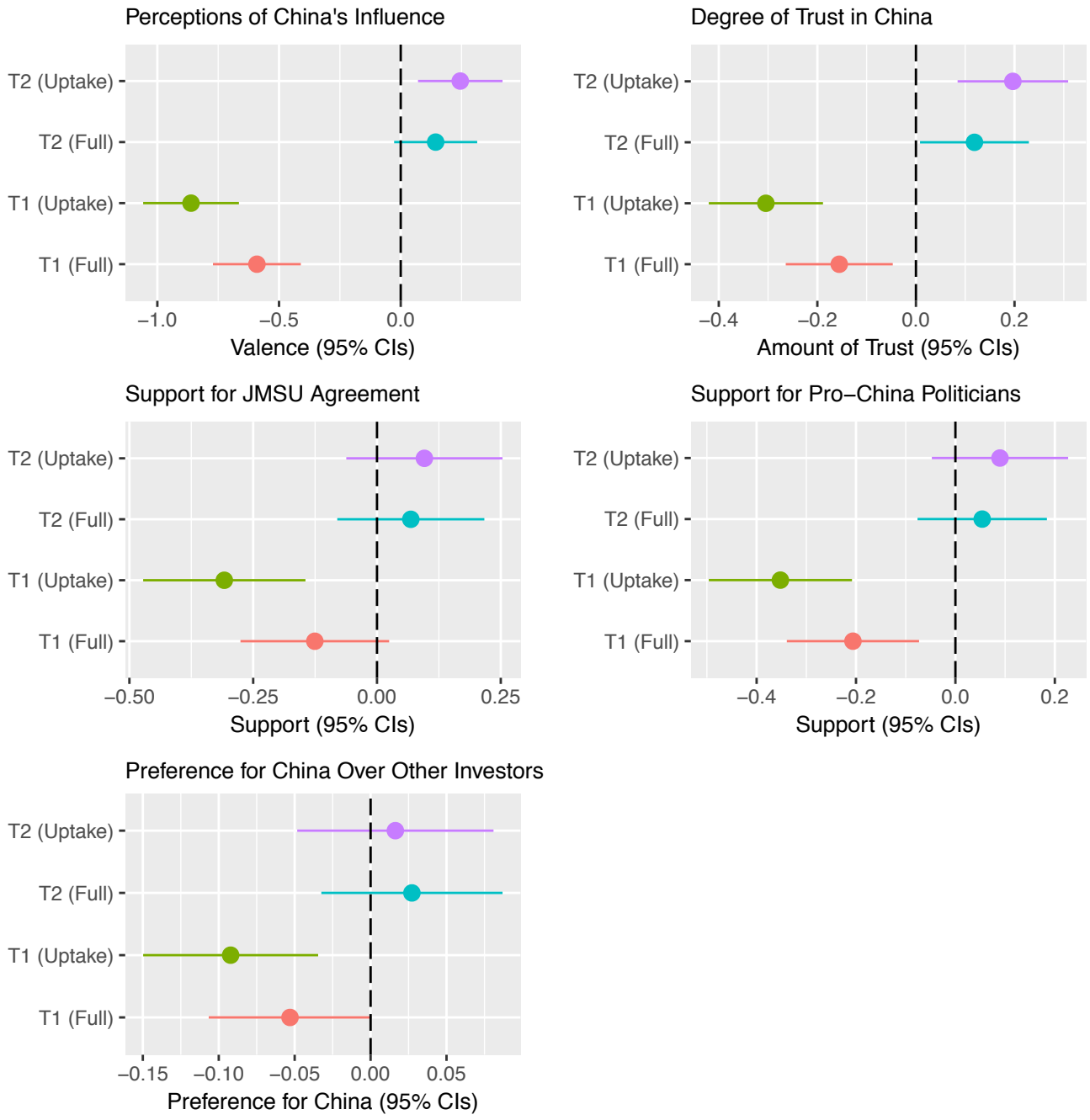

Figure 5.1: Treatment effects for T1 (subversive carrots) and T2 (stakeholder cultivation) on Philippine public attitudes and policy demands toward China. Both treatment effects are measured against the pure control, T0.

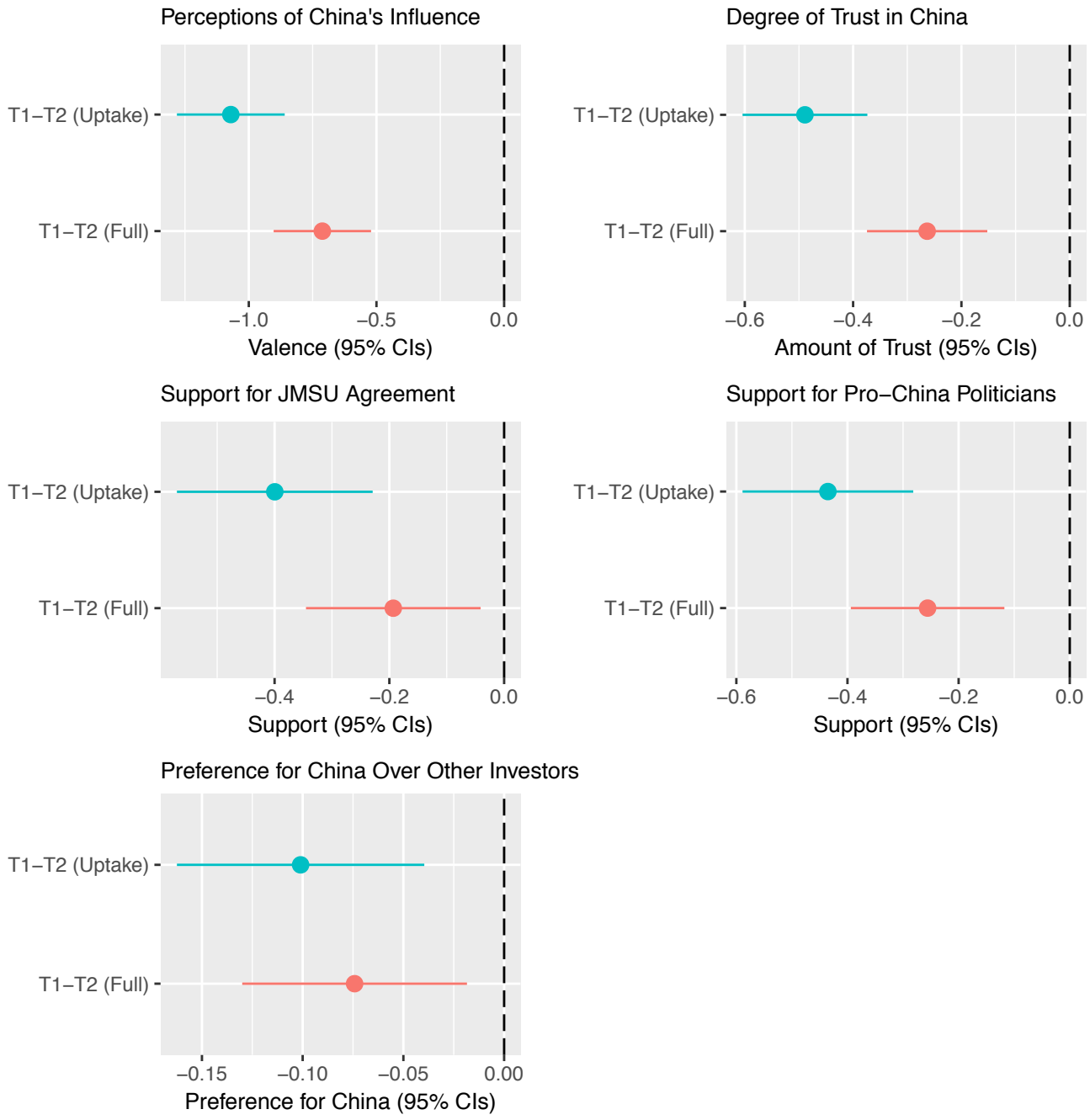

Figure 5.2: Treatment effects for T1 (subversive carrots) against T2 (stakeholder cultivation) on Philippine public attitudes and policy demands toward China. Population consists of T1 and T2 only.

Conclusion

This chapter provides evidence for the microfoundations of public accountability. In a country where political leaders are held accountable - in which the public has information on economic inducements and elites have to respond to public opinion - the choice of inducement strategy leads to very different outcomes. Subversive carrots that undermined established political and institutional processes, such as regulatory review, and operated via the use of corruption, elicited very strong public backlash. Public attitudes toward China worsened significantly, along with reduced public support for policy cooperation with China.

In contrast, the use of stakeholder cultivation had more positive effects on public perceptions of China, and laid some groundwork for greater policy cooperation with China, although it appeared less able to overcome previous negative reputations. Public accountability and the mechanism of public opinion thus serves as an important constraint on elite behavior, and an important condition for the success or failure of economic inducements. Moreover, the negative reputation acquired through the use of subversive carrots can be long-lasting and difficult to alter. In the next chapter, I further evaluate the differing results of subversive carrots and stakeholder cultivation using a paired case comparison of two high accountability cases - Australia and Japan.

Appendix

Data Quality

In line with the pre-analysis plan, data quality was ensured through several steps. First Qualtrics automatically blocks repeat IP addresses, ensuring that each respondent is unique. Additionally, the survey includes an "attention filter" question: "In which month of the year are you taking this survey?" This question was worded inconspicuously as a regular survey question, to avoid subsequent respondent complacency (knowing that they had passed the attention filter) and to minimize respondent dissatisfaction at being given a test.' All respondents who did not pass the filter were automatically dropped from the survey. Finally, at the data cleaning stage, all respondents who answered the survey at a total speed averaging less than 3.5 minutes or longer than 25 minutes were dropped. These last two steps were designed to ensure respondent quality and done before before analysis. All reported results include the above data cleaning steps.

Summary Statistics

	Obs.	Means	Median	Min	Max
Age	922	30.30	29.00	18.00	67
Gender (F/M)	922	0.50	0.00	0.00	1
Education (1-11 level)	925	8.12	9.00	2.00	11
Annual Income (10,000 PHP)	925	4.05	2.00	0.00	190
2016 Vote for Duterte	925	0.60	1.00	0.00	1

Table 5.3: Summary Statistics.

Balance Tables

	Control Means	Subversive Means	Difference	P-val
Age	30.23	30.21	-0.02	0.98
Gender (F/M)	0.51	0.51	-0.01	0.84
Education (1-11 level))	8.14	8.15	0.01	0.94
Annual Income(10,000 PHP)	3.91	4.29	0.38	0.56
Duterte Voter? (0 No/ 1 Yes)	0.64	0.62	-0.02	0.57

Table 5.4: Balance Table for T0 (Control) and T1 (Subversive).

	Control Means	Stakeholder Means	Difference	P-val
Age	30.23	30.47	0.23	0.75
Gender (F/M)	0.51	0.47	-0.04	0.29
Education (1-11 level))	8.14	8.08	-0.07	0.61
Annual Income(10,000 PHP)	3.91	3.97	0.07	0.93
Duterte Voter? (0 No/ 1 Yes)	0.64	0.56	-0.08	0.04

Table 5.5: Balance Table for T0 (Control) and T2 (Stakeholder).

	Subversive Means	Stakeholder Means	Difference	P-val
Age	30.21	30.47	0.26	0.74
Gender (F/M)	0.51	0.47	-0.03	0.40
Education (1-11 level))	8.15	8.08	-0.07	0.56
Annual Income(10,000 PHP)	4.29	3.97	-0.31	0.70
Duterte Voter? (0 No/ 1 Yes)	0.62	0.56	-0.06	0.13

Table 5.6: Balance Table for T1 (Subversive) and T2 (Stakeholder).

OLS Regression Results for Full T1 and T2 Populations

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T1	−0.5909****	−0.1556***	−0.1256	−0.2061***	−0.0531*
	(0.0921)	(0.0554)	(0.0766)	(0.0679)	(0.0273)
Age	−0.0062	−0.0015	0.0005	−0.0090**	−0.0035*
	(0.0060)	(0.0036)	(0.0050)	(0.0044)	(0.0018)
Gender	−0.0045	−0.0365	−0.0959	−0.1965***	−0.0234
	(0.0950)	(0.0571)	(0.0790)	(0.0700)	(0.0282)
Education	−0.0611*	−0.0165	−0.0647**	−0.0224	−0.0273***
	(0.0338)	(0.0196)	(0.0271)	(0.0240)	(0.0097)
Income	0.0042	−0.0030	−0.0002	0.0023	−0.0002
	(0.0058)	(0.0036)	(0.0049)	(0.0044)	(0.0018)
Voted for Duterte	0.3647****	0.2129****	0.3696****	0.2921****	0.0325
	(0.0983)	(0.0589)	(0.0814)	(0.0722)	(0.0290)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	593	616	616	616	616

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.7: OLS regression results for the effects of T1 (subversive carrots). N includes full T1 and T0 populations.

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T2	0.1437*	0.1187**	0.0683	0.0539	0.0272
	(0.0871)	(0.0564)	(0.0758)	(0.0664)	(0.0304)
Age	−0.0050	0.0015	0.0078	0.0050	−0.0037*
	(0.0057)	(0.0037)	(0.0049)	(0.0043)	(0.0020)
Gender	0.1274	0.0536	−0.0376	−0.0234	−0.0609*
	(0.0897)	(0.0581)	(0.0781)	(0.0685)	(0.0314)
Education	−0.0057	0.0066	−0.0542**	−0.0293	−0.0201*
	(0.0296)	(0.0193)	(0.0259)	(0.0227)	(0.0104)
Income	−0.0112**	−0.0037	0.0031	−0.0044	−0.0006
	(0.0044)	(0.0029)	(0.0039)	(0.0034)	(0.0016)
Voted for Duterte	0.4377****	0.2973****	0.3588****	0.3069****	0.0815**
	(0.0908)	(0.0587)	(0.0789)	(0.0691)	(0.0317)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	600	613	613	613	613

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.8: OLS regression results for the effects of T2 (stakeholder cultivation). *N* includes full T2 and T0 populations.

OLS Regression Results for Uptake T1 and T2 Populations

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T1	−0.8616****	−0.3044****	−0.3083****	−0.3521****	−0.0922***
	(0.1004)	(0.0591)	(0.0836)	(0.0735)	(0.0294)
Age	−0.0099	−0.0073*	−0.0024	−0.0143***	−0.0051***
	(0.0065)	(0.0038)	(0.0054)	(0.0048)	(0.0019)
Gender	0.0808	0.0517	0.0481	−0.0743	−0.0061
	(0.1021)	(0.0604)	(0.0854)	(0.0751)	(0.0300)
Education	−0.0468	−0.0273	−0.0674**	−0.0182	−0.0303***
	(0.0383)	(0.0221)	(0.0312)	(0.0274)	(0.0110)
Income	0.0049	−0.0023	0.0007	0.0025	0.00003
	(0.0060)	(0.0036)	(0.0051)	(0.0044)	(0.0018)
Voted for Duterte	0.2935***	0.1975***	0.3417****	0.2540****	0.0473
	(0.1039)	(0.0612)	(0.0866)	(0.0762)	(0.0305)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	497	512	512	512	512

Notes:
****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.9: OLS regression results for the effects of T1 (subversive carrots). *N* includes T1 and T0 populations that uptook treatments.

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T2	0.2447***	0.1967****	0.0958	0.0897	0.0163
	(0.0886)	(0.0572)	(0.0805)	(0.0700)	(0.0330)
Age	−0.0023	0.0020	0.0055	0.0025	−0.0037*
	(0.0058)	(0.0037)	(0.0052)	(0.0045)	(0.0021)
Gender	0.0942	0.0277	−0.0395	−0.0483	−0.0628*
	(0.0908)	(0.0587)	(0.0825)	(0.0717)	(0.0338)
Education	−0.0016	−0.0003	−0.0537*	−0.0147	−0.0229**
	(0.0306)	(0.0199)	(0.0280)	(0.0243)	(0.0115)
Income	−0.0127***	−0.0045*	0.0029	−0.0027	−0.0008
	(0.0042)	(0.0027)	(0.0038)	(0.0033)	(0.0016)
Voted for Duterte	0.3753****	0.2879****	0.3313****	0.2486****	0.0830**
	(0.0925)	(0.0597)	(0.0839)	(0.0730)	(0.0344)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	522	529	529	529	529

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.10: OLS regression results for the effects of T2 (stakeholder). *N* includes T2 and T0 populations that uptook treatments.

Ordered Logit Regression Results for Full T1 and T2 Populations

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T1	−1.0283***	−0.4728***	−0.2449*	−0.4442***	−0.0531*
	(0.1564)	(0.1569)	(0.1477)	(0.1512)	(0.0273)
Age	−0.0103	−0.0036	0.0011	−0.0188*	−0.0035*
	(0.0097)	(0.0103)	(0.0096)	(0.0098)	(0.0018)
Gender	−0.0817	−0.0860	−0.2110	−0.4702***	−0.0234
	(0.1546)	(0.1607)	(0.1517)	(0.1558)	(0.0282)
Education	−0.0904*	−0.0382	−0.1337**	−0.0522	−0.0273***
	(0.0546)	(0.0548)	(0.0534)	(0.0550)	(0.0097)
Income	0.0071	−0.0085	−0.0004	0.0056	−0.0002
	(0.0092)	(0.0096)	(0.0092)	(0.0095)	(0.0018)
Voted for Duterte	0.6294***	0.5940***	0.7086***	0.6270***	0.0325
	(0.1594)	(0.1655)	(0.1569)	(0.1597)	(0.0290)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	593	616	616	616	616

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.11: Ordered logit regression results for the effects of T1 (subversive carrots); binary logit used for "Investor" variable. *N* includes full T1 and T0 populations.

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T2	0.2941*	0.3513**	0.1284	0.1144	0.0272
	(0.1514)	(0.1600)	(0.1489)	(0.1533)	(0.0304)
Age	−0.0070	0.0097	0.0177*	0.0162	−0.0037*
	(0.0099)	(0.0105)	(0.0097)	(0.0102)	(0.0020)
Gender	0.1440	0.1748	−0.1178	−0.0842	−0.0609*
	(0.1570)	(0.1646)	(0.1531)	(0.1584)	(0.0314)
Education	−0.0454	0.0269	−0.1196**	−0.0609	−0.0201*
	(0.0522)	(0.0545)	(0.0528)	(0.0532)	(0.0104)
Income	−0.0181**	−0.0111	0.0081	−0.0093	−0.0006
	(0.0092)	(0.0073)	(0.0081)	(0.0069)	(0.0016)
Voted for Duterte	0.7340****	0.8691****	0.7193****	0.6852****	0.0815**
	(0.1606)	(0.1688)	(0.1572)	(0.1613)	(0.0317)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	600	613	613	613	613

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.12: Ordered logit regression results for the effects of T2 (stakeholder cultivation); binary logit used for "Investor" variable. *N* includes full T2 and T0 populations.

Ordered Logit Regression Results for Uptake T1 and T2 Populations

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T1	−1.5684****	−0.9547****	−0.6109****	−0.7943****	−0.0922***
	(0.1846)	(0.1794)	(0.1664)	(0.1715)	(0.0294)
Age	−0.0161	−0.0206*	−0.0035	−0.0288***	−0.0051***
	(0.0110)	(0.0116)	(0.0106)	(0.0110)	(0.0019)
Gender	0.0924	0.1832	0.0617	−0.1828	−0.0061
	(0.1718)	(0.1817)	(0.1681)	(0.1729)	(0.0300)
Education	−0.0847	−0.0769	−0.1397**	−0.0390	−0.0303***
	(0.0633)	(0.0659)	(0.0632)	(0.0656)	(0.0110)
Income	0.0080	−0.0081	0.0012	0.0054	0.00003
	(0.0099)	(0.0105)	(0.0096)	(0.0101)	(0.0018)
Voted for Duterte	0.5176***	0.5879***	0.6726****	0.5690***	0.0473
	(0.1730)	(0.1834)	(0.1715)	(0.1753)	(0.0305)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	497	512	512	512	512

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.13: Ordered logit regression results for the effects of T1 (subversive carrots); binary logit used for "Investor" variable. *N* includes T1 and T0 populations that uptook treatments.

	Influence	Trust	JMSU	Politician	Investor
	(1)	(2)	(3)	(4)	(5)
T2	0.4546***	0.5934****	0.1722	0.1865	0.0163
	(0.1658)	(0.1793)	(0.1623)	(0.1679)	(0.0330)
Age	−0.0022	0.0113	0.0136	0.0109	−0.0037*
	(0.0108)	(0.0116)	(0.0106)	(0.0112)	(0.0021)
Gender	0.0834	0.1121	−0.1293	−0.1340	−0.0628*
	(0.1707)	(0.1822)	(0.1662)	(0.1728)	(0.0338)
Education	−0.0411	0.0180	−0.1173**	−0.0249	−0.0229**
	(0.0577)	(0.0614)	(0.0588)	(0.0594)	(0.0115)
Income	−0.0224**	−0.0139*	0.0082	−0.0065	−0.0008
	(0.0090)	(0.0076)	(0.0083)	(0.0072)	(0.0016)
Voted for Duterte	0.6960****	0.9190****	0.6800****	0.5608***	0.0830**
	(0.1746)	(0.1883)	(0.1706)	(0.1762)	(0.0344)
Emp. Stat FE?	Yes	Yes	Yes	Yes	Yes
N	522	529	529	529	529

Notes:

****Significant at the 0.1 percent level
***Significant at the 1 percent level
**Significant at the 5 percent level
*Significant at the 10 percent level

Table 5.14: Ordered logit regression results for the effects of T2 (stakeholder cultivation); binary logit used for "Investor" variable. *N* includes T2 and T0 populations that uptook treatments.

Full Text of Survey Instrument

Consent to Participate in Survey

This survey is about your attitudes towards different contemporary issues. It is part of an academic research project. Academic researchers are conducting the survey and they will be the only people who see your anonymous results.

Your participation is completely voluntary. If you agree to participate, you will answer some questions about yourself and your attitudes towards different policies. The questions should take about 10 minutes to answer. If you complete the survey, you will receive a small payment.

Your participation in this study will be confidential. Your personal identity will never be linked to your survey responses, so please answer as honestly as you can.

By clicking on the arrow below, you are agreeing to participate.

-I consent to participate.

-I do not consent to participate.

[If consent is given]

Thank you for participating in this survey. If you have any questions or concerns regarding your participation you may contact: aywresearch[at]yahoo.com

A. Demographics

First, please answer some questions about your personal background.

What year were you born in?

(open-ended variable)

Where do you currently live?

National Capital Region 1 City of Manila 2 City of Mandaluyong 3 City of Marikina 4 City of Pasig 5 Quezon City 6 City of San Juan 7 Caloocan City 8 City of Malabon 9 City of Navotas 10 City of Valenzuela 11 City of Las Pinas 12 City of Makati 13 City of Muntinlupa 14 City of Paranaque 15 Pasay City 16 Taguig City 17 Municipality of Pateros Cordillera Administrative Region 18 Abra 19 Apayao 20 Benguet 21 Baguio City 22 Ifugao 23 Kalinga 24 Mountain Province Ilocos Region 25 Ilocos Norte 26 Ilocos Sur 27 La Union 28 Pangasinan Cagayan Valley 29 Batanes 30 Cagayan 31 Isabela 32 Nueva Vizcaya 33 Quirino Central Luzon 34 Aurora 35 Bataan 36 Bulacan 37 Nueva Ecija 38 Pampanga 39 Angeles City 40 Tarlac 41 Zambales 42 Olongapo City Calabarzon 43 Batangas 44 Cavite 45 Laguna 46 Quezon 47 Lucena City 48 Rizal Mimaropa 49 Marinduque 50 Occidental Mindoro 51 Oriental Mindoro 52 Palawan 53 Puerto Princesa City 54 Romblon Bicol Region 55 Albay 56 Camarines Norte 57 Camarines Sur 58 Catanduanes 59 Masbate 60 Sorsogon Western Visayas 61 Aklan 62 Antique 63 Capiz 64 Guimaras 65 Iloilo 66 Iloilo City (Capital) 67 Negros Occidental 68 Bacolod City (Capital) Central Visayas 69 Bohol 70 Cebu 71 Cebu City (Capital) 72 Lapu-Lapu City (Opon) 73 Mandaue City 74 Siquijor 75 Negros Oriental Eastern Visayas 76 Biliran 77 Eastern Samar 78 Leyte 79 Tacloban City 80 Northern Samar 81 Samar (Western) 82 Southern Leyte Zamboanga Peninsula 83 Zamboanga del Norte 84 Zamboanga del Sur 85 Zamboanga City 86 Zamboanga Sibugay 87 City of Isabela Northern Mindanao 88 Bukidnon 89 Camiguin 90 Lanao del Norte 91 Iligan City 92 Misamis Occidental 93 Misamis Orietnal 94 Cagayan de Oro City Davao Region 95 Compostela Velley 96 Davao del Norte (Davao) 97 Davao del Sur 98 Davao City 99 Davao Oriental SOCCSKSARGEN 100 Cotabato 101 Sarangani 102 South Cotabato 103 General Santos City (Dadiangas) 104 Sultan Kudarat 105 Cotabato City Caraga 106 Agusan del Norte 107 Butuan City 108 Agusan del Sur 109 Dinagat Islands 110 Surigao del Norte 111 Surigao del Sur Autonomous Region in Muslim Mindanao (ARMM) 112 Basilan 113 Lanao del Sur 114 Maguindanao 115 Sulu 116 Tawi-tawi

What gender do you identify with?

1 Male

2 Female

3 Other

What is your marital status?

1 Single/Never married

2 Married

3 Living-in as married

4 Widowed

5 Separated / Married but separated /not living with legal spouse

6 Divorced

Do you have children?

1 Yes

2 No

Are you a Filipino citizen?

1 Yes

2 No

Which ethnic group do you identify with?

1 Filipino (Pinoy)

2 Chinese Filipino (Tsinoy)

3 Other

What is your highest level of education?

1 No formal education

2 Incomplete primary/elementary

3 Complete primary/elementary

4 Incomplete secondary/high school: technical/vocational type

5 Complete secondary/high school: technical/vocational type

6 Incomplete secondary/high school

7 Complete secondary/high school

8 Some university education

9 University education completed

10 Masters degree

11 Doctoral or professional degree

What is your current employment status? Choose one:

1 Employed

2 Self-employed

3 Currently unemployed

4 Student

5 Retired

6 Homemaker

What industry sector do/did you work in?

Agriculture 1 Agriculture, hunting, and forestry 2 Fishing Industry 3 Mining and quarrying 4 Manufacturing 5 Electricity, gas, steam and air-conditioning supply 6 Water supply. sewerage, waste management and remediation activities 7 Construction Services 8 Wholesale and retail trade; repair of motor vehicles and motorcycles 9 Transportation and storage 10 Accommodation and food service activities 11 Information and communication 12 Financial and insurance activities 13 Real estate activities 14 Professional, scientific and technical activities 15 Administrative and support service activities 16 Public administration and defense; compulsory social security 17 Education 18 Human health and social work activities

19 Arts, entertainment and recreation 20 Other service activities 21 Homemaker 22 Activities of extraterritorial organizations and bodies 23 Unemployed / student / retired

How much, in pesos, (approximately) was your household income last month?

(insert blank) pesos

Which candidate did you vote for in the 2016 presidential election?

1 Rodrigo Duterte

2 Mar Roxas

3 Grace Poe

4 Jejomar Binay

5 Miriam Defensor Santiago

6 Other / Did not Vote

(Attention filter)

In which month of the year are you taking this survey?

1 March

2 April

3 May

4 June

5 July

Randomized Vignettes

[All respondents randomly receive one of the following four vignettes.]

T0: Please read the following information carefully, which discusses some recent developments in the

Philippines. In order to complete the survey, you will be asked questions based on the information provided below.

The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enterprises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects.

T1: Please read the following information carefully, which discusses some recent developments in the Philippines. In order to complete the survey, you will be asked questions based on the information provided below.

The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enterprises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects.

According to media reports, these projects did not follow the proper processes and rules of approval from government agencies. Instead, a group of top Philippine politicians directly signed the deals with the Chinese government and a few Chinese companies, skipping over the required regulatory procedures. Media reports suggest that the Chinese government and Chinese companies offered bribes and kickbacks to the Philippine politicians involved in the deal. Several politicians and journalists have criticized these agreements as being non-transparent and not following established political procedures and rules.

T2: Please read the following information carefully, which discusses some recent developments in the Philippines. In order to complete the survey, you will be asked questions based on the information provided below.

The Chinese government and the Philippine government have agreed to start work on several new infrastructure projects that will be financed by Chinese banks and constructed by Chinese state-owned enter-

prises. These projects include new bridges to reduce traffic congestion in Metro Manila, national railway projects, and agricultural irrigation projects.

According to media reports, these projects followed the proper processes and rules of approval from government agencies. The Chinese government and a few Chinese companies submitted competitive project proposals to the Philippine government, in accordance with required regulatory procedures. Media reports suggest that no bribes or kickbacks were offered to Philippine politicians as part of the deal. Several politicians and journalists have praised these agreements for being transparent and following established political procedures and rules.

Uptake check

[for T0]:

Based on the information above, is the Chinese government involved in infrastructure projects in the Philippines?

1 Yes

2 No

[for T1 and T2]:

Based on the information above, did the Chinese-financed infrastructure projects follow the proper processes and rules of approval from government agencies?

1 Yes

2 No

Based on the information above, did the Chinese-financed infrastructure projects involve bribes and kickbacks to Philippine politicians?

1 Yes

2 No

Outcome variables

[For each question, a random 50% of respondents view the answer choices in order of increasing negativity, and the remaining 50% of respondents view the answer choices in order of increasing positivity.]

Generally speaking, the influence China has on your country is?

1 Very positive

2 Positive

3 Somewhat positive

4 Somewhat Negative

5 Negative

6 Very negative

9 Decline to answer

Generally speaking, how much do you think the Philippines can trust China? 1 A great deal of trust

2 A fair amount of trust

3 Not too much trust

4 No trust at all

The Philippine government is conducting talks with the Chinese government about signing a joint resource exploration agreement, which would allow Philippine and Chinese companies to explore for oil and gas in the South China Sea. This would include areas off the coast of Palawan where the Philippines has economic rights and where China has also disputed Philippine claims. The agreement would likely lead to future joint development of natural resources in those areas involving China and the Philippines. How much do you support or oppose this agreement?

1 Strongly support

2 Somewhat support

3 Somewhat oppose

4 Strongly oppose

How much would you support or oppose your congressional district representative if he or she is involved in promoting the Chinese-financed infrastructure projects discussed earlier?

1 Strongly support

2 Somewhat support

3 Somewhat oppose

4 Strongly oppose

The Philippine government has recently proposed a national railway project in the Philippines, and is looking to partner with an outside investor. This investor will help to build and finance the project. Which of the following countries would you prefer to be the project investor? [country order randomized]

1 China

2 Japan

3 United States

4 South Korea

In your opinion, what are the advantages and/or disadvantages of Chinese investment and financing of infrastructure projects in the Philippines?

(open-ended response)

How would you evaluate the Philippine government's foreign policy toward China?

(open-ended response)

Baseline question [for T0 only]

Based on your knowledge, do Chinese-financed infrastructure projects, like those discussed earlier, follow the proper processes and rules of approval from government agencies?

1 Yes

2 No

Based on your knowledge, do Chinese-financed infrastructure projects, like those discussed earlier, involve bribes and kickbacks to Philippine politicians?

1 Yes

2 No

Concluding note for survey

Thank you for your participation.

The information, events, and people described in the survey are fictional and not meant to represent any specific case of Chinese aid or investment project in the Philippines. Any resemblance to events or people in real life is purely coincidental.

Chapter 6

Winds of Change? Statecraft in Myanmar and Cambodia

In this chapter, I use *within-country variation in the type of inducement strategy used* – in Cambodia – as well as another case of *within-country variation in public accountability over time* – Myanmar – to demonstrate the explanatory role of the two variables in my theoretical framework. I show how China's subversive carrots in Cambodia succeeded in achieving Beijing's foreign policy goals in the South China Sea, while stakeholder cultivation used by Japan and the United States did not produce meaningful political outcomes in Cambodia's low accountability system. In addition, I examine how subversive carrots became less effective in Myanmar with changes that led to greater public accountability.

First, I investigate Cambodia as a case of low accountability and the correspondingly high efficacy of China's subversive carrots. Beijing used subversive carrots that worked through crony state-business linkages in Cambodia and brought direct benefits to Cambodian elites, including the powerful prime minister. This has directly translated into desired political payoffs for Beijing. Data shows evidence of a spike in Chinese aid at opportune moments, resulting in Cambodia's willingness to support China's position on the South China Sea in defiance of other Southeast Asian countries, particularly when Cambodia held the ASEAN[1] chairmanship in 2012. An absence of public accountability mechanisms have prevented public and societal actors from punishing Cambodian leaders for their policy behavior.

1. Association for Southeast Asian Nations, a regional organization composed of ten Southeast Asian countries.

Additionally, I discuss the failure of stakeholder cultivation, also in Cambodia. Years of foreign aid from donors that adhered to institutional standards and procedures – Japan and the United States – produced negligible political outcomes. Because stakeholder cultivation did not provide rents directly to elites, it failed to induce attitudinal or policy changes in key constituencies with the pivotal political influence. To the contrary, the Cambodian government undertook no meaningful governance or political reforms, aid donors continue to carry little clout, and Japan failed in its attempts to leverage its economic presence for its policy objectives in the South China Sea.

Finally, I examine the political transition in Myanmar from the military junta to a more democratically-elected (albeit imperfect) government, to show how within-country changes in public accountability affect the success of China's subversive carrots. Under the previous military junta, subversive carrots served to benefit military cronies directly via non-transparent economic deals. However, the transition to a government that was more responsive to negative public opinion toward China reduced the efficacy of subversive carrots and led to changes in Myanmar's public management of its South China Sea position. Moreover, Beijing was pressured under conditions of higher accountability to change its strategy to a more stakeholder cultivation approach, pointing to a learning curve for China.

Cash for Comment: Success of Subversive Carrots in Cambodia

Cambodia, a country with low public accountability, presents a case of how Beijing has used subversive carrots to further its foreign policy goals in Southeast Asia. While Cambodia may be a relatively small and impoverished country, even relative to its neighbors, ASEAN's institutional norm of consensus allows Phnom Penh – with Chinese backing – to effectively wield veto power over the organization's statements and positions.

The current Sino-Cambodian relationship has grown from instrumental rather than ideological or historical foundations. China was the patron of the Pol Pot regime and Khmer Rouge, in opposition to Hun Sen's origins as part of the Vietnam-backed People's Republic of Kampuchea (PRK). However, as Hun Sen rose in prominence and eventually seized power in a coup, which led to international sanctions,

Beijing exploited the opportunity and became Cambodia's primary source of economic and military assistance.[2]

There is little transparency and little oversight in Cambodia's political system. Prime Minister Hun Sen and his cronies maintain tight control over lucrative sectors of Cambodia's economy, from natural resources and trading to construction and industrial parks. Apart from the private sector, Hun Sen and his extensive web of relatives – by blood and marriage – also control key components of the domestic political machinery and state apparatus, from the military and police to the media and civil society.[3] Both politics and business operate through personalized patronage networks. Business elites get concessional benefits and licenses as well as government positions, and they in turn channel funds to the ruling coalition and security forces. Funds flow to officials through bribes and kickbacks, and as patronage in advance of elections.[4]

Ruling Cambodia elites also face few domestic political costs for their actions. Hun Sen has brutally suppressed political opposition figures and intimidated voters, preventing fair and competitive elections.[5] Ahead of local and national elections in 2017 and 2018, the Cambodian government slammed opposition figures with numerous lawsuits and passed measures that could dissolve the main opposition party, causing the top opposition leader, Sam Rainsy, to preemptively resign.[6] The majority of the domestic (Khmer-language) press are controlled by ruling party interests, reducing the need for overt censorship. Because of low literacy and limited distribution, television is an important medium but also under firmer government control. Political coverage is essentially government propaganda, and opposition parties are denied broadcasting licenses and airtime. Journalists critical of the government are silenced through intimidation and violence.[7] While there appears on the surface to be a large and vibrant civil society, including many local and international NGOs, it is a "purposefully selective freedom" in which activities

2. John D. Ciorciari, "A Chinese model for patron-client relations? The Sino-Cambodian partnership," *International Relations of the Asia-Pacific* 15 (2015): 245–278.

3. For a detailed investigation, see "Hostile Takeover: The Corporate Empire of Cambodia's Ruling Family," Global Witness, July 2016.

4. Ciorciari, "A Chinese model for patron-client relations? The Sino-Cambodian partnership."

5. Duncan McCargo, "Cambodia: Getting Away with Authoritarianism?," *Journal of Democracy* 16, no. 4 (2005): 98–112.

6. Julia Wallace, "Top Opposition Leader in Cambodia Resigns as Election Nears," *New York Times*, February 12, 2017.

7. Sebastian Strangio, *Hun Sen's Cambodia* (Yale University Press, 2014), 195-198.

are circumscribed to non-sensitive areas such as the provision of public goods.[8]

Large-scale Chinese investment projects, in sectors such as natural resources, energy, transportation, and textiles, are subject to few institutional checks. Contracts are non-transparent and directly involve dealings between Chinese businesses and Cambodian political elites. Land grabs, human displacement, and environmental degradation have generated discontent, but opposition activists have often faced violent and life-threatening responses by the state.[9][10] White elephant projects are common, and foreign aid and development loans are often siphoned off as "plain brown paper bags full of cash."[11] The public and other societal actors have little ability to enforce oversight over China's subversive carrots or impose political costs on Hun Sen despite widespread dissatisfaction. Observers have argued that the Cambodian government has been skilful at creating "a mirage of freedom" rather than simply seeking to get rid of opposing voices, with ups and downs in freedom often linked to electoral cycles.[12]

How Chinese Cash Produced Cambodian Comment

Cambodia's low accountability environment has facilitated Beijing's use of subversive carrots to buy political support for China's foreign policy interests. In late 2009, 22 Uighur refugees entered Cambodia seeking asylum. The UNHCR issued letters identifying them as "Persons of Concern" under the agency's protection and was highly optimistic that the Cambodian government would grant them refugee status in line with legal obligations. However, in a reversal from government statements that Cambodia would be processing their asylum claims, the Uighurs were abruptly sent back to China on December 18 – the day before President Xi Jinping arrived in Phnom Penh for a state visit, along with US$1.2 billion in promised grants and loans.[13]

Arguably the most notorious incident, with implications for regional security, was Cambodia's behavior in ASEAN in 2012. Data on aid inflows into Cambodia show significant spikes in Chinese official

8. Strangio, *Hun Sen's Cambodia*, 191-194.
9. See also "How China bought its way into Cambodia," *Financial Times*, September 8, 2016.
10. Ciorciari, "A Chinese model for patron-client relations? The Sino-Cambodian partnership."
11. Strangio, *Hun Sen's Cambodia*, 221.
12. Ibid., 207.
13. Ibid., 211-213.

development aid (ODA) to Cambodia in 2011 and 2012 (Figures 6.1 and 6.2). Not coincidentally, in 2012, Cambodia assumed the chairmanship of ASEAN, the regional organization comprising the ten Southeast Asian countries.

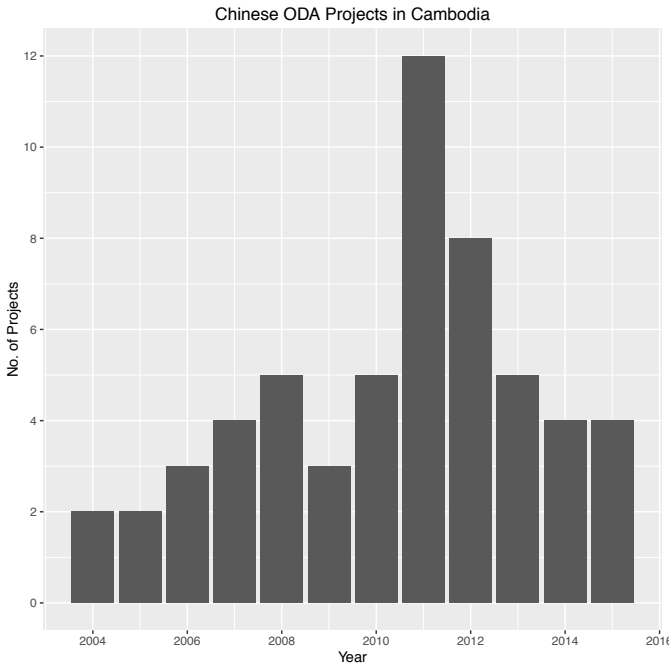

Figure 6.1: No. of Chinese ODA projects in Cambodia. Data source: odacambodia.com

Evidence shows a strong relationship between Chinese money and Cambodia's policy stance during the ASEAN Annual Ministerial Meeting (AMM) in July 2012. That meeting marked the first time in ASEAN's history that a joint communique was not issued. This unprecedented failure was attributed to consistent Cambodian opposition to any mention of sovereignty disputes in the South China Sea, in line with Beijing's foreign policy goals. During my interview with a senior U.S. diplomat based in a Southeast Asian country, he described a "straight up monetary" deal to provide economic benefits to Cambodia in exchange for not accepting specific language on the South China Sea.[14]

Based on field interviews and leaked media reports, the consensus among foreign and even Chinese observers was that Beijing had bought Cambodia over. China's goals were to prevent a joint ASEAN position and advocate bilateral management of the South China Sea disputes. In a serious breach of protocol,

14. Interview, senior U.S. diplomat based in Southeast Asia, January 2017.

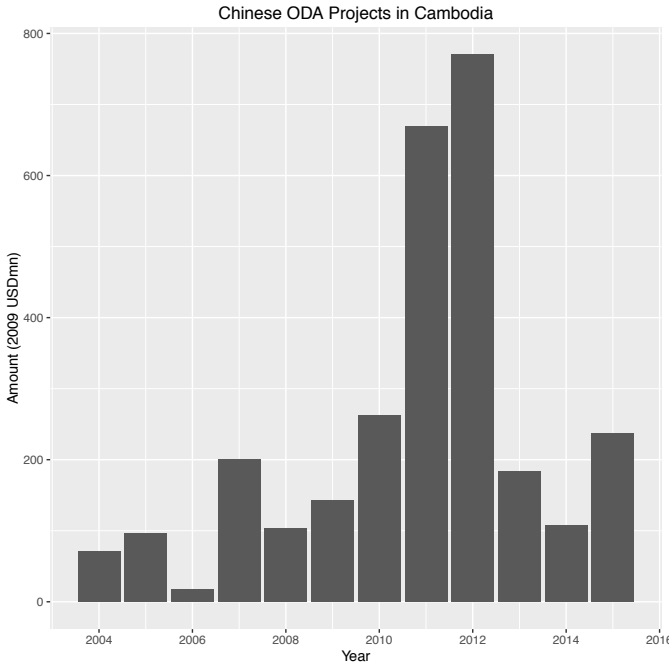

Figure 6.2: Amount of Chinese ODA flows to Cambodia. Data source: odacambodia.com

Cambodian delegates consulted with their Chinese counterparts during internal ASEAN discussions over the wording of the joint communique. China had demanded that any references to the South China Sea disputes be removed.[15] The Cambodian Foreign Minister said that he would be scolded by his superiors if he agreed to the joint statement, while Hun Sen falsely claimed that he had secured agreement from both Xi Jinping and Philippine president Aquino on the SCS issue.[16]

A parallel incident occurred during the July 2016 ASEAN summit, when Cambodia blocked any mention of the recent international tribunal ruling that had criticized China's position. Beijing pledged $600 million in aid to Phnom Penh just before the summit, and announced soon after the ASEAN meeting that it would build a $16 million National Assembly Hall in the Cambodian capital.[17] The low public accountability environment in Cambodia has allowed ruling elites to accept subversive carrots without facing domestic political costs. Despite local resentment against China's economic presence, Cambodian citizens

15. For a detailed analysis of what occurred at the meeting, see Carlyle Thayer, "ASEAN's Code of Conduct in the South China Sea: A Litmus Test for Community-Building?," *Asia-Pacific Journal* 10, no. 34 (2012)

16. Interview, former senior member of Presidential Management Staff under Aquino, July 29, 2016.

17. "How China bought its way into Cambodia," *Financial Times*, September 8, 2016.

have consistently lacked oversight mechanisms to punish the prime minister for his policy choices.[18]

China's subversive carrots and Cambodia's actions have had major implications for foreign policy issues in the region. Although Cambodia is not a dispute claimant in the South China Sea, its actions are not costless. Its foreign policy behavior has damaged relations with Southeast Asian neighbors and severely harmed its reputation in the region. While ASEAN used to be seen as a way for Southeast Asian countries to jointly amplify their policy voice vis-a-vis Beijing, the organization has suffered deepening divisions and greater incoherence since 2012, particularly on managing the South China Sea disputes. This has strengthened Beijing's position, enabling a consolidation of its presence in the South China Sea and preventing a resolution of the disputes counter to its foreign policy interests. Thus, the Cambodia case – exemplifying low public accountability – shows how the use of subversive carrots can efficiently produce political payoffs for Beijing.

The Failures of Stakeholder Cultivation in Cambodia

In contrast to Beijing's use of subversive carrots, stakeholder cultivation through aid programs and foreign investment from OECD countries such as Japan and the United States – which operate by established rules and procedures – have failed at gaining any sort of political traction with Prime Minister Hun Sen.

Since the 1990s, Japan has long been a leading provider of aid and investment in Cambodia (and the Mekong region more broadly), particularly in infrastructure development as well as the development of special economic zones.[19] Between 1993 and 2018, the United States provided around US$235 million in aid relating to governance, democracy, and civil society.[20] One major political goal of U.S. aid efforts were to strengthen democratic institutions and the rule of law.[21] International aid has added up to several billions of dollars since 1993.

18. Andrew Nachemson, "Chinese investment in Cambodia is bringing Phnom Penh closer to Beijing – and further from the EU," *South China Morning Post*, May 1, 2019, https://www.scmp.com/news/asia/southeast-asia/article/3008451/chinese-investment-cambodia-bringing-phnom-penh-closer.

19. Francoise Nicolas, "Catching Up or Staying Ahead? Japanese Investment in Mekong Region and the China Factor," *Asie. Visions* 99 (2018).

20. CRS2019.

21. CRS2019.

However, corruption remains rampant, as do human rights abuses (many ending in violence). There remains a strong culture of impunity in Cambodia, and analysts have described a move toward a one-party authoritarian state under Hun Sen's control.[22] Although Japan is generally well-regarded in Cambodia as an honest broker and an important source of aid, and has attempted to work with both the ruling and opposition parties,[23] its efforts to improve political governance and democratic reforms have been largely ineffective.

Certainly, a stakeholder cultivation approach was far less appealing to the Cambodian elites than subversive carrots. If OECD donors attempted to pressure Hun Sen on reforms and governance, he could turn to China for loans and investments without facing similar demands[24] Given that Hun Sen's cozy relationship with Beijing grew from instrumental reasons rather than historical or ideological affinities – in fact, Hun Sen had aligned with Vietnam against the Chinese-backed Khmer Rouge during the Cambodian-Vietnamese War – this points to the contrasting appeal of subversive carrots versus stakeholder cultivation for elites in a low accountability system.

Low public accountability meant that Hun Sen was able to manipulate stakeholder cultivation to serve his political legitimacy and crony needs of the elite. At annual donor meetings, he would grandly and repeatedly espouse the correct aid ideals and promise to undertake improved governance reforms, without delivering on this rhetoric.[25] Ruling elites in Cambodia have skilfully paid lip service to aid commitments while retaining political power, aided by their ability to manipulate and control national resources.[26] Scholars have even argued that foreign aid has reduced government's dependence on taxes, thus decreasing domestic public pressure for accountability and undermining democracy/rule of law. Because Cambodians have never paid taxes to the government, they "don't have that concept of the civil servant owing you something."[27]

22. Ronald Bruce St John, "Democracy in Cambodia—One Decade, US $5 Billion Later: What Went Wrong?," *Contemporary Southeast Asia*, 2005, 406–428.
23. Sek Sophal and Yoichiro Sato, "Reinvigorating Japan's twin-track diplomacy in Cambodia," *The Japan Times*, April 8, 2019.
24. Strangio, *Hun Sen's Cambodia*.
25. Ibid., 219-220.
26. St John, "Democracy in Cambodia—One Decade, US $5 Billion Later: What Went Wrong?"
27. Strangio, *Hun Sen's Cambodia*, 225.

In order to continue working with Cambodian leaders, aid donors have been forced to adjust their strategy to better accommodate government preferences.[28] Many projects have shifted to achieving low-level, short-term quantifiable outcomes to get the biggest bang for their buck. By and large, efforts have narrowed to focus on 'technical support' while putting aside fundamental political challenges and the prevalent issue of corruption and patronage. Individuals who criticize Cambodian elites are declared persona non grata or otherwise pressured to leave. This has allowed elites to continue with their parallel patronage system without facing political costs. According to an aid worker who has lived in Cambodia since 1995, many people have said that "this is the most difficult country I have ever worked in. There are very few places where you can go and meet with the government, who will blatantly say yes, yes, yes to everything and do absolutely nothing, take [your] $3 million, produce absolutely nothing, and then get another $3 million."[29]

The contrasting outcomes of stakeholder cultivation and subversive carrots can be seen through the apparent competition between Japan and China over infrastructure development (and geopolitical influence) in Cambodia. While Japan built a Cambodia-Japan Friendship Bridge in the 1990s, China has built eight Cambodia-China Friendship Bridges in recent years.[30] Japan recently renovated its Friendship Bridge for over a year and reopened it in April 2019, at a cost of US$30 million.[31]

Japan has been criticized for continuing its aid and investment in an attempt to woo PM Hun Sen, despite his numerous actions backpedaling democracy and violating human rights, in order to compete with China for political influence in Cambodia. For example, Japan donated 10,000 ballot boxes at a cost of US$7.5 million (China donated US$20 million worth of polling booths, computers, and other equipment) for Cambodia's general election in July 2018, even though the election was regarded as a sham given crackdowns on the opposition party.[32] According to observers at the Human Rights Watch, "Japan is fighting a losing battle for Hun Sen's support. Japan can't outspend China or deliver sweetheart con-

28. Strangio, *Hun Sen's Cambodia*, 259-261.
29. Ibid., 232-233.
30. "Cambodia builds 8th Cambodia-China Friendship Bridge," *Xinhua*, February 9, 2018.
31. Khouth Sophak Chakrya, "Chroy Changvar bridge is reopened," *The Phnom Penh Post*, April 4, 2019.
32. Nyshka Chandran, "The Japan-China rivalry is playing out in Cambodia's election," *CNBC*, July 19, 2018.

tracts to Cambodia, yet its overt and clumsy attempts to ingratiate itslef have led to a backlash among Cambodian activists, who see Tokyo selling out democracy and human rights to maintain a friendship with a dictator."[33]

Tokyo even attempted recently to leverage its aid and investment in Cambodia for more explicit geopolitical purposes. When agreeing to provide a concessional loan of 17 billion yen for improving a major road during a bilateral summit in November 2015, Japanese prime minister Abe told Hun Sen that Japan is 'deeply concerned about unilateral changes to the status quo such as large-scale land reclamation, the building of outposts, and its use for military purposes' in the South China Sea, and that 'Japan is focusing on a peaceful resolution to the situation based on the principle of the rule of law at sea.' During the Asia-Europe Meeting in July 2016, soon after the UN tribunal ruling on the South China Sea dispute, Abe chose Cambodia as one of six partners (out of the 50 attending the meeting) to have a bilateral summit. He highlighted specific progress in Japan's aid and infrastructure development to Cambodia, before stating that the tribunal ruling was final and legally binding for both parties as a matter of rule of law. However, these attempts to build on stakeholder cultivation have not produced any shifts in Cambodia's position on the South China Sea or its alignment with Beijing.[34]

Comparing the political outcomes of stakeholder cultivation versus subversive carrots, it is clear that investors and donors, including Japan and the United States, that sought to operate in accordance with institutional norms and standards failed in gaining political influence in Cambodia. Stakeholder cultivation did not provide rents directly to elites and thus were shunned in favor of subversive carrots (provided by China). Under conditions of low accountability, stakeholder cultivation was sometimes compelled to retreat to less ambitious (or even contrary) goals in order to be able to continue operating in Cambodia.

33. Brad Adams and Teppei Kasai, "Japan Should Stop Acting Like China in Cambodia," *The Diplomat*, March 22, 2019.

34. Hidetaka Yoshimatsu, "Japan's Export of Infrastructure Systems: Pursuing Twin Goals Through Developmental Means," *The Pacific Review* 30, no. 4 (2017): 494–512; Hong Zhao, "China–Japan Compete for Infrastructure Investment in Southeast Asia: Geopolitical Rivalry or Healthy Competition?," *Journal of Contemporary China*, 2018, 1–17; Nicolas, "Catching Up or Staying Ahead? Japanese Investment in Mekong Region and the China Factor."

Uprooted Carrots: Political Transition in Myanmar

During military junta rule in Myanmar, China was widely seen as the country's major backer. Political ties were intertwined with the large amounts of Chinese aid and investment flowing into Myanmar's underdeveloped economy. However, the unexpected political transition to a more democratic form of government has increased the role of public accountability, amplified public backlash against subversive carrots, and made Myanmar a less steadfast political ally, including on issues such as the South China Sea.

Although Myanmar is still far from being a fully accountable system, domestic political changes have altered the payoffs of economic statecraft. While Beijing could previously push through economic deals to its benefit by rewarding corrupt, crony actors, such non-transparent arrangements have now become less feasible, and (negative) public opinion has become a more important constraint on elites. As a result, China's use of subversive carrots has been less successful in achieving desired political outcomes.

Subversive carrots amidst changing accountability

Myanmar faced international censure and isolation after the 1990 general election, when the military government (officially known as the State Peace and Development Council/State Law and Order Restoration Council) seized power and refused to acknowledge the National League for Democracy (NLD) victory, led by Aung San Suu Kyi. Years of economic sanctions left China as the dominant source of trade, investment, and technical assistance. A long, complicated history of political ups-and-downs meant that the junta had no intention of turning Myanmar into a client or satellite state of China, but the lack of alternate strategic options greatly limited their ability to pursue a non-aligned, neutral foreign policy. This created an 'implicit bargain' in which China provided much-needed economic and political support, in exchange for favorable access to Myanmar's natural resources and strategic location.[35]

Under the military junta, major Chinese investment projects were geared toward benefiting Chinese

35. Jonathan T. Chow and Leif-Eric Easley, "Persuading Pariahs: Myanmar's Strategic Decision to Pursue Reform and Opening," *Pacific Affairs* 89, no. 3 (2016): 521–542; Evelyn Goh and David I. Steinberg, "Myanmar's Management of China's Influence:From Mutual Benefit to Mutual Dependence," in *Rising China's Influence in Developing Asia*, ed. Evelyn Goh (Oxford University Press, 2016).

interests and corrupt Burmese elites. These projects did not bring socioeconomic or developmental benefits to local populations, and often led to human displacement, violent land grabs, and environmental degradation.[36] Crony ties were particularly rampant in resource extractive industries such as jade, mining, and logging, primarily driven by Chinese actors.[37] As a result, Beijing and Chinese firms believed that they could ignore negative public opinion, relying instead on bribes and "government relations" as the main "lubricant" for Chinese economic projects.[38] Combined with widespread unethical practices of Chinese individuals, and the poor quality of Chinese-made products, this has created a broad, deep-rooted dislike for China in Myanmar society.[39] A recent survey experiment in Myanmar found strongly negative public perceptions of, and bias against, Chinese investments compared to Japanese investments, even when firms displayed similar behavior.[40] A retired Burmese diplomat observed that China has acted mostly for itself and suggested that it have a more generous aid policy modeled after that of Japan.[41]

Myanmar's domestic political transition altered the economic and political landscape for China. The Chinese "thought they had sewn it [political influence] up" using their traditional methods of bribing cronies,[42] but the use of such subversive carrots became less effective under a government that was more responsive to public opinion. A transition government came into power in 2010, and the NLD participated in parliamentary elections in 2012, subsequently winning office in the 2015 general elections. While the military remains a powerful actor, the NLD became the pivotal group in power, and its leader Aung San Suu Kyi is not as favorable toward China as her military predecessors.[43]

The government's greater attention to public opinion and transparent review, in response to widespread

36. Lee Jones, "The Political Economy of Myanmar's Transition," *Journal of Contemporary Asia* 44, no. 1 (2014): 144–170; Yizheng Zou and Lee Jones, "China's Response to Threats to Its Overseas Economic Interests: Softening Non-Interference and Cultivating Hegemony," *Journal of Contemporary China*, 2019,

37. See e.g. "Jade: Myanmar's 'Big State Secret,"' Global Witness, October 2015.

38. Yun Sun, "China's Strategic Misjudgement on Myanmar," *Journal of Current Southeast Asian Affairs* 31, no. 1 (2012): 73–96.

39. Interview, Yangon University professor, Yangon, January 13, 2017.

40. Ying Yao and Youyi Zhang, "Public perception of Chinese investment in Myanmar and its political consequences: A survey experimental approach," *International Growth Centre Policy Brief*, no. 53421 (2018).

41. Interview, retired senior Burmese diplomat, Yangon, January 13, 2017.

42. Interview, U.S. diplomat based in Yangon, January 3, 2017.

43. Interviews in Yangon, Australian businessman with ties to NLD central executive committee, January 4, 2017; senior manager at KBZ bank, January 14, 2017.

anti-Chinese sentiment, suggests that Chinese investment projects must meet higher standards. For example, the controversial $3.6 billion Myitsone dam has been suspended since 2011. This was attributed to effective mobilization by civil society actors under a more accountable government that proved sensitive to domestic political pressure.[44] Public pressure has continued to constrain elite actions in Myanmar. A range of societal actors have become more vocal, including NGOs, trade unions, and religious organizations (namely Buddhist monks), and labor strikes and local protests are not uncommon.[45] In the run-up to the second Belt and Road Forum in April 2019, hundreds of civil society leaders gathered in Yangon to announce a "one dollar campaign" that would raise funds to compensate China for canceling the Myitsone dam project by collecting $1 from every citizen.[46]

Reduced political payoffs: the South China Sea issue

In tandem with the increased public accountability was a shift in Myanmar's approach to the South China Sea issue. Traditionally, the Burmese government maintained strategic silence over the issue, facilitating Beijing's strategy of dividing ASEAN and preventing a multilateral consensus on handling disputes in the South China Sea. China's consistent financial and political support for the military regime – as Myanmar's main shield from international opprobrium – created pressure on the junta government to accord with Chinese interests, both domestically and internationally.[47][48] Beijing expected Myanmar to "reciprocate" and support Chinese positions in ASEAN, including China's bilateral negotiations formula for resolving the South China Sea disputes – as directly told to Myanmar officials prior to the 2011 ASEAN Regional Forum.[49]

However, the situation changed with Myanmar's political transition. According to observers, the Chi-

44. Debby Sze Wan Chan, "Asymmetric bargaining between Myanmar and China in the Myitsone Dam controversy: social opposition akin to David's stone against Goliath," *The Pacific Review* 30, no. 5 (2017): 674–691.

45. Zou and Jones, "China's Response to Threats to Its Overseas Economic Interests: Softening Non-Interference and Cultivating Hegemony."

46. Thomas Kean, "Belt and Road forum marks subtle shift in China-Myanmar ties," *Frontier Myanmar*, May 8, 2019, https://frontiermyanmar.net/en/belt-and-road-forum-marks-subtle-shift-in-china-myanmar-ties.

47. Yun Sun, "China and the Changing Myanmar," *Journal of Current Southeast Asian Affairs* 31, no. 4 (2012): 51–77.

48. Interviews with retired senior Burmese diplomat and Yangon University academic, January 13, 2017.

49. Sun, "China's Strategic Misjudgement on Myanmar," 82.

nese government exerted aggressive diplomatic pressure and made strong demarches in the run-up to the May 2014 ASEAN summit, suggesting that bilateral relations would be harmed (with an implicit threat of economic repercussions in the background) if the joint statement did not accord with Chinese interests.[50] However, Myanmar's leaders successfully resisted Chinese pressure, and handled the SCS issue in a neutral and balanced manner.[51] Under Myanmar's chairmanship, the organization issued a statement expressing "serious concerns" over ongoing tensions in the South China Sea.[52] This shows that the political payoffs of China's subversive carrots decreased after Myanmar saw an increase in public accountability.

In a significant shift from its traditional silence on SCS issues, when an international arbitration tribunal announced its ruling on the Philippine's South China Sea case in July 2016, Myanmar issued a public statement that expressed support for "rule of law," calling for all parties to "exercise restraint...and to refrain from threats or use of force."[53] In an interview, a former senior Burmese diplomat remarked that the Myanmar government's behavior was especially notable, given that not every ASEAN country issued an individual statement.[54]

Of course, the NLD government is far from being fully democratic and accountable. Ethnic violence, weak governance institutions, and oppressive laws remain. And Myanmar has not become completely antagonistic in its foreign policy toward China. Aung San Suu Kyi faces a hard balancing act in managing bilateral relations. While eager to broaden ties with other countries and conscious of widespread anti-Chinese public sentiment, the Burmese government needs help from China on the peace process and border issues, which are key policy priorities.[55] To maintain domestic legitimacy, Naypyidaw will have to spur greater economic growth, which likely requires cooperation with Beijing.[56] As a retired senior

50. Interview, Australian diplomat based in Yangon, January 5, 2017.

51. Interviews, U.S. and Australian diplomats based in Yangon, January 3 and 5, 2017.

52. "At Myanmar's first ASEAN Summit, alarm over China sea spat," AFP, May 12, 2014, accessed February 4, 2017 at http://www.mmtimes.com/index.php/national-news/nay-pyi-taw/10325-at-myanmar-s-first-asean-summit-alarm-over-china-sea-spat.html

53. "Myanmar's statement on the Award of the Arbitral Tribunal on the South China Sea under Annexure VII of UNCLOS," Ministry of Foreign Affairs, Nay Pyi Taw, July 13, 2016, accessed February 4, 2017 at http://www.president-office.gov.mm/en/?q=issues/foreign-policy/id-6479; see also Nyan Lynn Aung, "Myanmar wades in to South China Sea ruling with a balancing act," *Myanmar Times*, July 19, 2016.

54. Interview, retired senior Burmese diplomat, Yangon, January 13, 2017.

55. Interview, retired senior Burmese diplomat, Yangon, January 13, 2017.

56. Interview, Australian diplomat based in Yangon, January 5, 2017.

Burmese diplomat put it, "we are neighbors and cannot run away from each other; China is a big country, so we must be friendly and cooperative."[57] Facing international isolation due to the Rohingya crisis, the Myanmar government also has fewer foreign policy options.

Toward stakeholder cultivation? China's learning under pressure

Nonetheless, subversive carrots from China, such as explicit government-to-government favors or direct agreements with government ministers, are no longer par for the course.[58] Chinese firms have had to compete with commercial actors from other countries – including Japan, South Korea, and Singapore – especially for major infrastructure projects. After being caught flat-footed by the domestic political transition in Myanmar, Beijing has shifted away from purely using subversive carrots and started to engage with a broader range of political and societal actors in Myanmar, echoing a stakeholder cultivation strategy.

The Chinese government aggressively courted the new NLD government, with the Chinese foreign minister being the first to visit. It has reached out to NGOs and democracy activists, while continuing to maintain contacts with former military government figures.[59] Even politicians and activists critical of China and Chinese investments have been invited to Beijing for high-level meetings. The Chinese embassy as well as the Yunnan government and Yunnan University[60] has provided training courses for government bureaucrats, NLD leaders, and local businesses. Through a mix of government and NGO cooperation, Beijing has donated laptops to schools, sponsored scholarships, donated medical equipment, upgraded hospitals, and provided free healthcare services.[61] Chinese officials have even courted opposition politicians from ethnic minrotiy parties.[62]

57. Interview, retired senior Burmese diplomat, Yangon, January 13, 2017.
58. Interview, professor at Yangon University, January 13, 2017.
59. Interviews, U.S. and Australian diplomats based in Yangon, January 3 and 5, 2017.
60. Yunnan is a Chinese province neighboring Myanmar, and often plays a role in foreign relations with Myanmar Wong, "More than Peripheral: How Provinces Influence China's Foreign Policy."
61. Zou and Jones, "China's Response to Threats to Its Overseas Economic Interests: Softening Non-Interference and Cultivating Hegemony."
62. Sui-Lee Wee, "China courts hardline Buddhist party ahead of Myanmar poll," *Reuters*, October 15, 2015, https://www.reuters.com/article/us-myanmar-election-china/china-courts-hardline-buddhist-party-ahead-of-myanmar-poll-idUSKCN0S900520151015.

Chinese firms have also taken steps toward social responsibility and public relations initiatives.[63] In implementing investment projects, some Chinese companies have proactively sought to cultivate broader popular support and work with local political leaders.[64] For example, a Chinese state-owned enterprise involved in building two hydropower projects in the northern part of Myanmar preemptively sought out NGOs and CSOs, offering them shares in the project, and hired foreign environmental agencies for project approval.[65]

The greater role of public opinion in constraining elite behavior in Myanmar has decreased the effectiveness of China's subversive carrots, increased the demand for stakeholder cultivation, and pushed Beijing to adhere to domestic political processes and institutions. In August 2018, the Myanmar government announced that the Chinese-financed Kyaukpyu deepwater port had been scaled down to US$1.3 billion from original estimates of US$7.3 billion.[66] In embarking on this renegotiation process, the Myanmar government apparently requested technical assistance and advice from the U.S. government and other Western countries to examine the fine print of contracts and ensure greater viability and transparency – according to someone familiar with the negotiations, the latter "were very much Burmese-led but armed with the advice of the Americans and others as well. We were able to go to the Chinese [and say], 'This part is OK, this part is problematic in terms of debt.'"[67]

Subsequently, the Myanmar government spelled out conditions for signing a memorandum of understanding on China's BRI: that Myanmar would be allowed to seek financing from international financial institutions, invite international tenders, and to select proposed projects on the basis of mutual benefits. A top government official at the Planning and Finance Ministry emphasized that the minister had "scrutinized every setnence and word" of the MoU, and that Myanmar had approved only nine of the thirty-eight projects proposed by China.[68] Political observers continue to call for greater transparency and more

63. Sun, "China and the Changing Myanmar."
64. Zou and Jones, "China's Response to Threats to Its Overseas Economic Interests: Softening Non-Interference and Cultivating Hegemony."
65. Interview, senior manager at KBZ Bank, Yangon, January 14, 2017.
66. "Myanmar scales back Chinese-backed port project over debt fears," *Reuters*, August 2, 2018; "Port project scaled back amid debt concerns," *Economist Intelligence Unit*, August 3, 2018;
67. "U.S. Goes on the Offensive Against China's Empire-Building Funding Plan," *Wall Street Journal*, April 9, 2019.
68. Nan Lwin, "Gov't Spells Out Conditions for Signing BRI Deals with China," *The Irrawaddy*, May 30, 2019.

robust regulations to ensure that Myanmar benefits.[69] While in Beijing for the Belt and Road Forum in April 2019, Aung San Suu Kyi stressed that BRI projects should be in line with Myanmar's national development plans, should be economically viable as well as socially and environmentally responsible, and "most importantly, the projects must win the confidence and support of local people."[70]

Conclusion

The level of public accountability in the target country is an important constraint in the success of different inducement strategies. As seen across a range of countries in Southeast Asia, Beijing has overwhelmingly focused on providing economic benefits to top political leaders and elites in the target country in ways that circumvent political processes. Such a strategy of subversive carrots was able to yield quick political dividends in countries with low public accountability, where elites have greater incentive and ability to translate that into political outcomes. This is evident in Cambodia, seen to be firmly in China's pocket. In contrast, stakeholder cultivation by other foreign powers, such as Japan and the United States, failed to gain political traction or influence among Cambodian elites.

Moreover, the case of Myanmar underlines how subversive carrots have limited sustainability and are vulnerable to domestic political shifts in target countries. An increase in public accountability meant that the government was more responsive to public opinion and was more reluctant to accept subversive carrots. In fact, Beijing's efforts to shift toward a stakeholder cultivation strategy underscore the importance of institutional resilience and accountability mechanisms in recipient countries to pressure China to operate in line with domestic political processes and institutions.

69. Nan Lwin, "Wariness Over BRI as State Counselor Prepares for Beijing Forum," *The Irrawaddy*, April 3, 2019.

70. Thomas Kean, "Belt and Road forum marks subtle shift in China-Myanmar ties," *Frontier Myanmar*, May 8, 2019, https://frontiermyanmar.net/en/belt-and-road-forum-marks-subtle-shift-in-china-myanmar-ties.

Chapter 7

Peddling or Persuading: China's Economic Statecraft in Australia

Over the next two chapters, I test my theory in the context of two liberal democracies who are both U.S. allies in the Asia-Pacific region, comparing the effectiveness of subversive carrots versus stakeholder cultivation in two high accountability cases. In this chapter, I focus on the case of Australia.

Australia is an economically developed country with a very high public accountability system. This makes it an ideal case study to examine the political outcomes of China's economic statecraft under conditions of high public accountability. Moreover, Australia is seen as a canary in a coal mine, at the forefront of liberal democracies realizing the reach of CCP interference and manipulation efforts. This underscores the far-reaching attempts by China to exercise economic statecraft, not just on developing but also developed countries.

I analyze how China has attempted to use subversive carrots to influence Australia's foreign policy, in particular through political donations and academic funding, with the aim of coopting public voices and shaping the direction of intellectual discourse about China. However, Australia's high level of public accountability soon generated a strong public backlash against China. The presence of a free media, active political opposition, and robust institutional mechanisms enabled open debate and transparent reporting on politicians linked to Beijing's payroll, pressured politicians to backtrack, and facilitated fur-

ther institutionalization to increase resilience against foreign interference. This underlines the important role of public accountability institutions in circumscribing the success of China's subversive carrots.

In addition, I examine the broader context of Australia's economic interdependence with China, and the buffering effects of stakeholder cultivation, through which important domestic constituencies in Australia have become more aligned with China's foreign policy interests and have been strong advocates of cooperative relations. While Canberra continues to seek a positive bilateral relationship with Beijing, this has not stopped it from pursuing a firmer stance against China's subversive carrots and perceived foreign interference efforts. In fact, the use of carrots has created longer-term reputational costs, deepened politicization, and heightend suspicions of Chinese-Australian individuals and China's economic activities more generally, even absent apparent political motivations.

Peddling in Australia: Canary in the Coal Mine?

Given the relatively transparent and accountable nature of democratic politics in Australia (particularly as compared to other frequent targets of China's economic statecraft such as Cambodia), the Chinese government dangled inducements by exploiting Australia's relatively lax campaign financing laws, which do not require donors to be Australian nationals. While Beijing has commonly used aid and infrastructure projects (often with accompanying corruption) as inducements in developing countries, the more advanced nature of Australia's economy called for a different type of subversive carrot – political donations and financing. At the same time, there are strong parallels in the targeting of individual elites and the circumventing and undermining of democratic political processes.

In particular, Australia's intel agency flagged two major political donors, Huang Xiangmo and Chau Chak Wing, as having close connections to the Chinese Communist Party and warned the leaders of Australian political parties that their donations might come with strings attached. For example, Chau is an Australian national and billionaire property developer who owns a CCP-linked newspaper in Guangdong and is a member of a provincial-level Chinese People's Political Consultative Conference (CPPCC), suggesting close governmental ties. From 2006 to 2016, he gave over AUD$4 million to the three major

political parties in Australia - Liberal, Labor, and Nationals. [1] Chau has access to high-level politicians on both sides of the political aisle. During a trip to Europe as Foreign Minister, Kevin Rudd made a stopover in Guangdong (bypassing Beijing), leaving by the back door of his hotel to meet Chau in a limo sent by the Chinese businessman.[2]

Huang Xiangmo similarly donated almost A$2.7 million across political parties between 2012 and 2016. Until recently, he was president of the Australian Council for the Promotion of Peaceful Reunification of China (ACPPRC), a prominent instrument of China's United Front work, which aims to advance CCP interests by winning over friends and silencing perceived enemies of the Chinese state. Huang's donations meant that he often rubbed shoulders with top-level politicians in Australia. He was also a prominent figure in the Chinese-Australian community who was well-connected with the Chinese embassy, and could often be seen seated next to the PRC ambassador at events.[3] In an editorial for the *Global Times*, Huang wrote that the Australian Chinese community needed to learn "how to have a more efficient combination between political requests and political donations."[4] He also publicly stated that "overseas Chinese realize that they need to make their voices heard in politics, to safeguard Chinese interests, and let Australian society pay more attention to the Chinese."[5]

In the most publicized scandal, in fall 2016 a New South Wales (NSW) state senator, Sam Dastyari, was found to have very close ties with Huang Xiangmo. As the Australian Labor Party's NSW General Secretary and subsequently Senator, Dastyari was closely involved in fundraising, and Huang was an important donor. Huang and associated donors also helped Dastyari cover several thousand dollars of legal fees and travel bills.[6] In June 2016, the Chinese businessman had canceled a promised $400,000 donation to the Labor Party after its defense spokesperson criticized the sitting government's "ambiguous" policy

1. Nick McKenzie, Chris Uhlmann, Richard Baker., Daniel Flitton, and Sashka Koloff, "China's Operation Australia: Payments, Power and Our Politicians," *Sydney Morning Herald*, 2017.

2. Interview, Nick McKenzie, journalist, Melbourne, March 16, 2018.

3. Interview, Tim Watts, Labor Party MP, Melbourne, March 15, 2018.

4. Primrose Riordan, "China's local emperor Huang Xiangmo says politics just like sport," *Australian Financial Review*, September 1, 2016.

5. Nick McKenzie and Sarah Ferguson, "Power and Influence: The Hard Edge of China's Soft Power," *ABC Four Corners*, June 5, 2017.

6. Nick McKenzie and Sarah Ferguson, "Power and Influence: The Hard Edge of China's Soft Power," *ABC Four Corners*, June 5, 2017.

on the South China Sea and called for the Australian military to conduct freedom of navigation operations. At a press conference the day after, standing next to Huang, Dastyari called for Canberra to refrain from involvement in the South China Sea disputes and respect Beijing's position, saying that "the Chinese integrity of its borders is a matter for China...As a supporter, and a friend of China, the Australian Labor party needs to play an important role in maintaining that relationship and the best way of maintaining that relationship is knowing when it is and isn't our place to be involved."[7] This was very much in line with China's desired policy position and, if followed through, would have been a major diplomatic victory for Beijing. In addition, Dastyari made calls to expedite Huang's citizenship application, and provided counter-surveillance advice to Huang during a face-to-face meeting at the latter's mansion in October of the same year, telling him to leave his phone and have their conversation outside, as Australian security agencies were monitoring him.[8]

Huang was also able to parachute his allies (with similar links to the ACPPRC) into political positions. Six months after Huang and his associates made a $500,000 donation to the New South Wales Labor Party in November 2012, Ernest Wong was placed into the Upper House seat formerly held by Eric Roozenthal, who then went on to work for Huang. Similarly, a month after making a $60,000 donation, fellow ACPPRC member Simon Zhou was given a place on the Labor Party's senate ticket for the 2016 election.[9] Observers note that the insertion of CCP proxies into political circles is still significant, even at the local and state levels, given the face time and networking connections with senior and federal-level politicians and party operatives.[10] The Australian Security Intelligence Organization (ASIO) has thus far identified about ten candidates at state and local government elections who were closely linked with Chinese intelligence services.[11] While Chinese-Australians have the right to get involved in politics, the fact that any sufficiently prominent individual or successful businessperson would likely need to have politi-

7. "Dastyari caught defying Labor on China," *Sky News*, November 29, 2017.

8. Nick McKenzie, James Massola, and Richard Baker, "Sam Dastyari warned big Chinese donor to go outside, his phone was bugged," *Sydney Morning Herald*, November 29, 2017.

9. Nick McKenzie and Sarah Ferguson, "Power and Influence: The Hard Edge of China's Soft Power," *ABC Four Corners*, June 5, 2017.

10. Interview, Nick McKenzie, journalist, Melbourne, March 16, 2018.

11. Christopher Knaus and Tom Phillips, "Turnbull says Australia will 'stand up' to China as foreign influence row heats up," *Guardian*, December 8, 2017.

cal connections in China and community organizational support in Australia (now often controlled by CCP United Front organizations) makes it harder to disentangle the reach of the Chinese government.

As Australian politicians seek to engage with the growing Chinese-Australian communities, the need for campaign financing and grassroots machinery have given CCP-linked individuals more opportunities to influence political advocacy. The Chinese government's strategy has been to make financial contributions to anyone who has a reasonable chance of winning office, seeking to make them more sympathetic to issues of interest to China [12] – and make public statements reflecting those positions. For example, a Sydney MP, Craig Laundy, participated in CCP-organized protests against Abe's visit to the Yasukuni Shrine, and apparently condemned Tibetan-led protest in Sydney as "thugs who attacked the Chinese consulate."[13]

The Dastyari case was also a clear example of how subversive carrots in the form of political donations through CCP proxies were able to yield (temporary) political dividends for Beijing. Sam Dastyari had been previously quoted in PRC media saying that getting involved in territorial disputes in Asia was against Australia's national security interests, and he appeared at a Chinese community event in Sydney protesting then-Prime Minister Tony Abbott's meeting with Japanese PM Shinzo Abe and praise of Japanese soldiers.[14] In 2015, Dastyari also reportedly pressured a deputy Labor leader not to meet with a political activist during her visit to Hong Kong.[15] During Senate committee hearings, Dastyari's intensive line of questioning toward senior foreign and defense policy officials reflected China's concerns.[16]

Top-ranking political figures have also been implicated. Former Trade Minister Andrew Robb pushed strongly for the China-Australian Free Trade Agreement (ChAFTA) to be sealed, despite criticisms about the potential benefits and concerns over the Australian labor market; Huang's company donated A$100,000 to Robb's fundraising vehicle, including A$50,000 on the day ChAFTA was signed. Even before officially

12. Interview, Richard Rigby, Richard Rigby, retired diplomat and former consul general in Shanghai, Canberra, March 7, 2018.

13. Clive Hamilton and Alex Joske, "Political networking the Chinese way - a Sydney MP and his 'community adviser'," *Sydney Morning Herald*, June 22, 2017.

14. Andrew Bolt, "Dastyari, Carr: took China's cash, took China's side," *Herald Sun*, September 7, 2016.

15. Paul Karp and agencies, "Sam Dastyari told Tanya Plibersek not to meet a Hong Kong democracy activist – report," *Guardian*, December 10, 2017.

16. John Fitzgerald, "Australia," Asan Special Forum on China's Sharp Power and Foreign Interference, April 24, 2018.

leaving his job, Robb took on an unspecified consulting position for A$880,000 a year with Landbridge, a Chinese firm with links to the PRC government and that acquired the lease of Darwin Port in 2015.[17][18] This lease was highly controversial given the presence of a nearby military base that also included expanded US Marine Corps deployments and rotations.[19]

CCP-linked money has also reached into universities and academic circles in Australia. Chau Chak Wing gave A$20 million to University of Technology Sydney's business school. Huang also donated A$1.8 million to UTS, to set up the Australia-China Relations Institute (ACRI), replacing the now-defunct China Research Institute. Huang served as chairman of ACRI's board, and personally named former Foreign Minister Bob Carr to be ACRI's executive director. Carr has stated that ACRI " take[s] an unabashedly positive and optimistic view of the Australia-China relationship."[20] Feng Chongyi, a professor at the same university and vocal CCP critic, has said that ACRI repeatedly dismissed his attempts to get involved.[21] According to a senior Labor source, Carr has been "pushing for an aggressive pro-China position" among NSW Labor MPs.[22] Through ACRI, Carr has brought Australian journalists on study tours around China, resulting in puff pieces presenting a gleaming image of China and repeating Party lines on the economic benefits of a peaceful bilateral relationship and ominous warnings should Canberra anger Beijing over the South China Sea and other issues.[23]

Other Australian China experts have expressed concerns over ACRI's academic independence and criticized the institute for being a "propaganda vehicle" for the Chinese government, with limited transparency on its financial budget and activities (including meetings with CCP officials), and a preference for one-sided opinion pieces and fact sheets. One prominent academic has described the "monotony of

17. Peter Dixon and Maureen Rimmer, "Free trade agreement: What's really at stake if China deal falls through?" *The Conversation*, September 7, 2015.

18. Clive Hamilton, *Silent Invasion: China's Influence in Australia* (Hardie Grant Books, 2018), 71-72,116-118.

19. Others have argued that it did not compromise national security because anyone could easily observe activities at the Darwin base from publicly-accessible areas.

20. Nick O'Malley, Philip Wen, and Michael Koziol, "Donations, Dastyari and Chinese soft power," *Sydney Morning Herald*, September 9, 2017.

21. Damien Cave and Jacqueline Williams, "Australian Politics Is Open to Foreign Cash, and China Has Much to Gain," *New York Times*, June 6, 2017.

22. Sarah Martin, "Bob Carr's think tank 'operating as a China propaganda arm'," *The Australian*, September 9, 2016.

23. Hamilton, *Silent Invasion: China's Influence in Australia*, 104-108.

Carr's China-Whatever comments."[24] Carr described Huang Xiangmo as being "well-informed on Chinese politics" and "unfairly victimized" by an ongoing "China panic" in Australia. He criticized current political leaders for "loose talk" and anti-PRC statements, and argued that there was no evidence of a coordinated CCP strategy to swamp Australia with Chinese money.[25]

The accountability backlash

However, Australia's high level of public accountability soon generated a strong public backlash against China, involving open debate and extensive reporting on politicians linked to Beijing's payroll. Political, media, and public criticism pressured politicians to resign and backtrack from ties with China, as well as sparked a review process of Chinese donor influence and new foreign interference laws.[26]

First, information transparency, facilitated by the presence of a free press, has allowed greater awareness of 'cash for comment' instances and broader knowledge of CCP influence in Australia. There is an ongoing, public (if fairly polarized) debate over the issue. Journalists have played significant and instrumental roles in uncovering details of the Dastyari scandal, Huang's and Chau's activities, the status of ACRI, and other United Front-related work about overseas Chinese students and Chinese-language media in Australia.[27] Established institutional structures mean that journalists are also able to access and publish information about where political donations are coming from and which politicians are implicated.[28] Scholars and former government officials have further chimed in through written analysis and media interviews.[29] Criticism has centered on how the CCP has been undermining parliamentary sovereignty and

24. Matthew Knott and Heath Aston, "Don't become 'propaganda vehicles' for China: universities warned over donations," *Sydney Morning Herald*, September 8, 2016; James Leibold, "The Australia-China Relations Institute doesn't belong at UTS," *The Conversation*, June 4, 2017; John Fitzgerald, "Business as usual: Accommodating China's interests in Australia," *The Australian*, September 9, 2016.

25. Interview, Bob Carr, Sydney, March 13, 2018.

26. Peter Hartcher, "Riding the red dragon express not a good look," Sydney Morning Herald, September 3, 2016; Editorial, "China's Influence-Peddling in Australia," *Wall Street Journal*, September 14, 2016; "Sam Dastyari-linked political donor resigns from Bob Carr institute after major review," Australian Financial Review, September 21, 2016.

27. For a helpful overview, see Kelsey Munro, "A free press is a magic weapon against China's influence peddling," *Lowy Interpreter*, December 18, 2017.

28. Chris Uhlmann and Andrew Greene, "Chinese donors to Australian political parties: who gave how much?" *Australian Broadcasting Corporation*, August 21, 2016.

29. See e.g. John Garnaut, "How China Interferes in Australia and How Democracies Can Push Back," *Foreign Affairs*, March 9, 2018; Peter Jennings, "At last, we're awake to China's predatory meddling," *The Weekend Australian*, December

interfering in Australian electoral processes through the use of financial inducements.[30]

Second, oversight exercised by the presence of robust institutional mechanisms and open political competition creates domestic consequences for political figures ensnared in Beijing's influence peddling. After Sam Dastyari's comments on the South China Sea were reported, the senator quickly ducked the issue and backtracked, saying that he supported the Labor Party position and international rule of law.[31] Politicians across political parties have openly criticized the situation (albeit with a tendency to attack individuals from the opposite side of the aisle).[32] Facing political pressures, including from some voices within the Labor Party, Sam Dastyari resigned in December 2017.[33] Ernest Wong, a local politician linked with Huang, also publicly cut institutional links to the businessman.[34] Top leaders have lost respect and been discounted within their political party; politicians themselves are now wary of accepting PRC-linked money, and decline invites to dinners and events with CCP-linked individuals that they might have gone to a few years ago.[35] Huang Xiangmo resigned as chairman ACRI's board, and the institute has made an effort to clarify its budget, stating that Huang's donation ran out in 2016 and that UTS has been responsible for operating costs since then.[36] All of these developments highlight how subversive carrots backfired for Beijing.

The Australian government has also taken a strong stance in criticizing China's political interference efforts, with Prime Minister Malcolm Turnbull controversially paraphrasing a famous Mao Zedong quote (although its authenticity has been questioned) to declare in Mandarin that "the Australian people

16, 2017; Nick McKenzie and Sarah Ferguson, "Power and Influence: The Hard Edge of China's Soft Power," *ABC Four Corners*, June 5, 2017; "An open letter from concerned scholars of China and the Chinese diaspora," *Policy Forum*, March 19, 2018; Fergus Hunter, "Leading China scholars sign open letter saying Beijing influence debate is not racist," *Sydney Morning Herald*, March 27, 2018.

30. See e.g. John Fitzgerald, "China influence: in defence of parliamentary sovereignty," *Lowy Interpreter*, April 19, 2018.

31. Nick McKenzie and Sarah Ferguson, "Power and Influence: The Hard Edge of China's Soft Power," *ABC Four Corners*, June 5, 2017.

32. See e.g. Primrose Riordan, "Robb under fire for China policy push," *Australian Financial Review*, November 1, 2016; Amy Remeikis, "Sam Dastyari quits as Labor senator over China connections, *Guardian*, December 11, 2017.

33. Jacqueline Williams, "Australian Lawmaker Quits Amid Questions Over China Ties," *New York Times*, December 12, 2017; Amy Remeikis, "Sam Dastyari quits as Labor senator over China connections, *Guardian*, December 11, 2017.

34. Primrose Riordan, "MP severs ties with Chinese billionaire," *The Australian*, December 1, 2017.

35. Interview, Tim Watts, Labor Party MP for Gellibrand, Melbourne, March 15, 2018.

36. Interview, James Laurenceson, Deputy Director at ACRI, Sydney, March 12, 2018.

[will] stand up" to China.[37] In August 2016, the government commissioned a classified investigation on foreign interference in Australia, which found widespread political interference by the CCP.[38] In December 2017, Canberra introduced a new set of foreign interference legislation, titled the National Security Legislative Amendment (Espionage and Foreign Interference) Bill 2017 and the Foreign Influence Transparency Scheme Bill 2017. These laws would ban foreign political donations, require those in Australian politics to declare links with foreign entities, and make it a crime to covertly act on behalf of a foreign principal to influence Australian political processes or against Australian national interests.[39] These bills were reviewed by the Parliamentary Joint Committee on Intelligence and Security (PJCIS), and members of the public (from academics to civil society to community organizations) have made several submissions in response to the proposed legislation, which has also stirred debate over freedom of press concerns.[40] The law on covert foreign interference and espionage was passed in June 2018 (the law on banning foreign political donations was still being drafted).[41]

As seen above, the formalized, institutional process of implementing new laws has allowed the solicitation of diverse viewpoints and promoted a vigorous debate over how Australia should respond to CCP attempts at political influence. Observers have expressed confidence in the Australian political system, including the healthy response of media and governing institutions.[42] Others have discussed the importance of media reporting, transparency, and democratic institutions in making Australia more resilient to Beijing's political interference efforts, and the necessity of clear legal frameworks.[43] In a testimony hearing

37. Christopher Knaus and Tom Phillips, "Turnbull says Australia will 'stand up' to China as foreign influence row heats up," *Guardian*, December 8, 2017.

38. John Garnaut, "How China Interferes in Australia and How Democracies Can Push Back," *Foreign Affairs*, March 9, 2018; "Australia to ban covert foreign interference in politics," Associated Press, June 27, 2018.

39. "Protecting Australian from Foreign Interference: Media Release," Prime Minister, Attorney-General, Minister of Finance, December 5, 2017, https://www.pm.gov.au/media/protecting-australia-foreign-interference; Henry Belot, "Explainer: Here's what you need to know about the Government's foreign interference laws," *ABC*, February 7, 2018.

40. See "Review of the National Security Legislation Amendment (Espionage and Foreign Interference) Bill 2017," accessed April 2, 2018 at https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Intelligence_and_Security/EspionageFInterference; David Wroe, "Freedom of press concerns prompt changes to foreign interference laws," *Sydney Morning Herald*, March 5, 2018.

41. "Australia to ban covert foreign interference in politics," Associated Press, June 27, 2018.

42. Interviews with senior diplomat working on Asia-Pacific issues at Department of Foreign Affairs and Trade, Canberra, March 8, 2018; Allan Gyngell, former director-general of the Australian Office of National Assessments, Canberra, March 9, 2018.

43. Interview, John Garnaut, former journalist and member of Prime Minister's Office, March 14, 2018; John Garnaut,

to the PJCIS on March 16, 2018, Australia's spy chief Duncan Lewis emphasized how strengthened legislative regimes and prosecutions of foreign interference activities would provide strong deterrence against both Australian individuals and foreign entities.[44] This underscores the importance of public accountability in circumscribing the effects of China's subversive carrots and as a condition for the effectiveness of China's economic statecraft.

Long-term costs: politicization, spillover, and reputational costs

The public and political backlash against China's subversive carrots in Australia has created significant longer-term costs. Debates on CCP influence and China's economic statecraft have become highly politicized, with additional adverse implications for the Chinese-Australian community as debates take on an ethno-nationalist tone. The nature of the backlash in Australia highlights the negative reputation and spillover costs for China's foreign policy and economic statecraft in the long run. Beijing's attempts to exploit weak campaign finance laws and channel political donations via CCP-linked individuals backfired significantly. Not only did implicated Australian politicians suffer political costs for making statements favorable toward the Chinese government's foreign policy interests, any activities related to Chinese capital and ethnically-Chinese individuals are regarded under a deeper cloud of suspicion.

Part of the backlash in Australia has involved broader suspicion of the ethnic Chinese communities in Australia, and a common assumption that any ethnic Chinese actors are likely to be acting on behalf of the Chinese government. This is despite the fact that most of the top political actors implicated in accepting Beijing's carrots have been non-Chinese Australians. Beijing's attempts to cultivate support from Chinese diaspora communities have certainly contributed to this perception. Top Chinese leaders have publicly called for overseas Chinese to unite in support of the "China dream,"[45] and the Chinese government has encouraged foreign citizens with Chinese heritage to apply for special residency visas.[46]

"How China Interferes in Australia and How Democracies Can Push Back," *Foreign Affairs*, March 9, 2018; John Fitzgerald, "Australia," Asan Special Forum on China's Sharp Power and Foreign Interference, April 24, 2018.

44. "National Security Legislation Amendment (Espionage and Foreign Interference) Bill 2017," Parliamentary Joint Committee on Intelligence and Security, Melbourne, March 16, 2018.

45. See e.g. Timothy Heath, "Beijing's Influence Operations Target Chinese Diaspora," *War on the Rocks*, March 1, 2018.

46. Jieh-Yung Lo, "Beijing's welcome mat for overseas Chinese," *The Lowy Interpreter*, March 6, 2018.

The use of ethnic Chinese diaspora as a 'magic weapon' for CCP interests to circumvent and undermine democratic political processes has entrenched concerns over Beijing's subversive carrots.

Some voices in Australia have expressed concerns over broad racism and suspicion of the Chinese-Australian community as part of an unproductive policy and political response.[47] Public debate has been so polarized that Chinese-Australians or those who expouse a more moderate view are often labeled as "CCP stooges."[48] Far right political parties in Australia have seized on the furor to promote a white nationalistic agenda, painting Chinese investment as an imperialistic strategy to acquire Australian wealth and sovereignty.[49]

Certainly, individuals from Mainland China can be susceptible to being coopted into Beijing's political agenda, for example through economic incentives or psychological pressure. They can also more effectively serve as intermediaries between the Chinese embassy and Australian politicians. As seen in the recent scandals, Chinese individuals can be important sources of political donations. The revelation of certain individuals as CCP proxies has also been caught up in a broader debate over the role of the Chinese government in controlling – through local United Front organizations – Chinese-language media, Chinese students, and Chinese-Australian community organizations in Australia.[50] Many Chinese community associations have been stacked with individuals associated with the Chinese embassy and other United Front organizations, and have been mobilized to become more politically active.

Yet, there are also major cleavages within the Chinese diaspora community, particularly between recent migrants from Mainland China and those who have been living in Australia for several generations (and who may also hail from places other than Mainland China). Ethnic Chinese politicians have be-

47. David Brophy, "David Brophy reviews 'Silent Invasion: China's Influence in Australia' by Clive Hamilton," *Australian Book Review*, March 21, 2018; "An open letter from concerned scholars of China and the Chinese diaspora," *Policy Forum*, March 19, 2018.

48. Jieh-Yung Lo, "Just because I have a moderate view on China doesn't make me a Beijing stooge," *The Guardian*, April 5, 2018.

49. See e.g. John Hood AC, "China's One Belt One Road imperialist designs upon Australia - traitor class in Darwin grab their yuan cut," Australia First Party, July 10, 2018, https://australiafirstparty.net/chinas-one-belt-one-road-imperialist-designs-upon-australia-traitor-class-in-darwin-grab-their-yuan-cu

50. Clive Hamilton and Alex Joske, "Submission to the Parliamentary Joint Committee on Intelligence and Security: United Front Activities in Australia," February 2018.

come more cautious in their political and social activities, for fear of being associated with the CCP.[51] In addition, many Chinese-Australians participate in United Front-linked community organizations as a pragmatic way of getting business and social connections rather than because of an explicit ideological motivation to serve CCP interests.[52] There have been reports from the Chinese-Australian community over unhappiness that societal discussion has not "put a face" on individuals, alongside increased feelings of marginalization, pushing some to more actively seek out the Chinese embassy's embrace.[53]

Furthermore, Chinese investment and financing has started to meet with greater scrutiny. In 2018, the Australian government issued a ban on 5G technology from Huawei and ZTE, two major Chinese companies, over potential espionage concerns.[54] A bid by a leading Hong Kong infrastructure company (Cheung Kong Infrastrcuture Holdings, CKI) to buy APA Group, a key Australian gas pipeline operator, was blocked on national security grounds.[55]

In addition, Canberra has become far more concerned over inflows of Chinese capital into the South Pacific. The Australian government launched a fund of over US$2 billion in infrastructure loans and grants to counter China's economic activities in the South Pacific.[56] While the Solomon Islands government had signed a deal with Huawei in 2016 to lay an undersea internet cable, Canberra jumped in offering to cover construction costs for the Solomon Islands as well as Papua New Guinea.[57] Australia also outbid China to fund a military base in Fiji,[58] This underscores how subversive carrots have had major negative spillover costs for Beijing's foreign policy across national borders.

Policy responses to China's political financing activities have been framed under a narrative of a generational struggle to protect Australian democracy against the rise of authoritarian governments such as

51. Damien Cave, "Espionage Bills in Australia Stir Fears of Anti-Chinese Backlash," *New York Times*, December 19, 2017.
52. Interview, Tim Watts, Labor Party MP for Gellibrand, Melbourne, March 15, 2018.
53. Interviews with Richard Rigby, retired diplomat and former consul general in Shanghai, Canberra, March 7, 2018; Heidi Han, journalist, Sydney, March 13, 2018.
54. "Huawei and ZTE handed 5G network ban in Australia," *BBC*, August 23, 2018; Saheli Roy Choudhury, "Former Australian PM Turnbull explains why his government banned Huawei, ZTE from selling 5G equipment," *CNBC*, March 28, 2019.
55. Simon Segal, "Blocking Chinese gas takeover won't damage Australia's foreign investment pipeline," *The Conversation*, November 22, 2018.
56. "China shuns rivalry in Pacific as Australia says 'this is our patch'," *Reuters*, November 7, 2018.
57. Liam Fox, "Australia, Solomon Islands, PNG sign undersea cable deal amid criticism from China," *ABC*, July 11, 2018.
58. Christopher Mudaliar, "Australia outbids China to fund Fiji military base," *Lowy Interpreter*, October 4, 2018.

China. Andrew Hastie, an Australian legislator and the chair of the Parliamentary Joint Committee on Intelligence and Security described China as"a state that uses the whole of society to advance its national objectives. We are less organised because we believe in individual liberty. That's a good thing for Australia but it does make us vulnerable to authoritarian states."[59]

This suggests that backlash against China's subversive carrots and perceived Chinese political interference is also exacerbated by China's image as an authoritarian regime operating under a model of state-led capitalism. While research has shown that China's overseas economic activities and foreign policy initiatives are often a reflection of diverging domestic actors and interests,[60] the opaque nature of the CCP regime and the difficulty in separating commercial from strategic actors leads to assumptions that most activities have the state's hand in them.

Thus, the Australia case shows how backlash and spillover reputational costs from the use of subversive carrots, further entrenching wariness of Chinese capital as being directed by the Chinese Communist Party, will continue to pose challenges for Beijing's ability to use economic statecraft for political influence. Given that most Australians are against subversive carrots and Chinese government interference in their political system, Australian political leaders will have little room to back away from its current policy positions.[61] This phenomenon further underlines the short- and longer-term risks of using carrots in a high public accountability system. Such subversive carrots create a fierce public backlash that fundamentally detracts from the image of China and Chinese diaspora (often seen by Beijing as an useful instrument of its foreign policy) in target countries, Australia included. This makes current and any future efforts at economic statecraft or political influence even more challenging.

59. David Wroe, "Defending democracy a generational struggle, Australian MPs warn," *Sydney Morning Herald*, July 10, 2018.

60. Wong, "More than Peripheral: How Provinces Influence China's Foreign Policy"; Baogang He, "The Domestic Politics of the Belt and Road Initiative and its Implications," *Journal of Contemporary China* 28, no. 116 (2019): 180–195; Min Ye, "Fragmentation and Mobilization: Domestic Politics of the Belt and Road in China," *Journal of Contemporary China*, 2019,

61. Interview, senior diplomat working on Asia-Pacific issues at Department of Foreign Affairs and Trade, Canberra, March 8, 2018.

Persuading Australia: Buffering Effects of Economic Interdependence

In this section, I situate the backfiring of subversive carrots against the broader context of Australia-China economic relations and stakeholder cultivation efforts. In juxtaposing the effects of subversive carrots and stakeholder cultivation, the analysis draws out some implications of using multiple economic statecraft strategies, as is plausible in a country's foreign policy. This discussion also sheds light on the mechanisms by which the Chinese government has sought to increase its economic and political influence, and which domestic actors constitute Beijing's preferred targets. An important part of analyzing the effectiveness of China's economic statecraft rests on understanding who receives inducements and how this may translate into political outcomes. I conclude by discussing the resulting implications for the resilience of public accountability institutions and the outcomes of subversive carrots versus stakeholder cultivation.

Even as there has been political pushback in Australia against China's use of subversive carrots, continued economic interdependence and the cultivation of domestic stakeholders has served as a buffering force. The policy debate is often polarized between the national security community (such as the defense and intel establishments) and other societal actors more concerned with broader economic benefits. Certain domestic groups benefiting from a strong Australia-China economic relationship tend to advocate for peaceful and cooperative relations with Beijing. Despite the backlash over subversive PRC-linked political donations, Chinese investment largely remains welcome and Canberra has continued to seek cooperative economic and political relations with Beijing.

Chinese Investment in Australia

China accounts for a small but rapidly growing proportion of foreign investment in Australia. While the United States and United Kingdom remain the largest investors in Australia, together adding up to over 40% of total investment at the end of 2017, Chinese investment remains in the single percentage digits. However, Chinese investment has grown significantly over the past decade. Investment from the PRC, currently ranked as the ninth-largest investor (2% of total investment), grew 21.6% between 2012 and 2017 (and also accounted for almost 25% of all proposed investment in 2016-17). Investment from Hong Kong

(fifth-largest investor) stands at 3.6% of the total and grew 17% over the five year period ending in 2017.[62]

A new dataset focusing on Chinese foreign direct investment into Australia – including investments by subsidiaries effectively controlled by a Mainland Chinese investor – found that Chinese-owned companies accounted for just over A$40.4 billion of direct investment in the four-year period of 2014 to 2017.[63] Mining and real estate were the largest destination for funds (A$9.9 and A$8.7 billion respectively), although the real estate sector saw the largest number of projects (110 versus 36). Most real estate investment went into commercial real estate. There was also considerable variability over time; for example, there were major Chinese investments in transport in 2016 but none in 2017.

While only 15% of projects fell under state-owned enterprises, these accounted for 47% of the total investment value. In addition, 87% of the total value of Chinese investments came from projects worth more than A$100 million. This suggests that Chinese investments tend to involve large projects, and that state-owned enterprises are much more likely to make large-scale investments and remain an important driving force.[64]

At the same time, Chinese FDI declined by 40% between 2016 and 2017,[65] 2017 investments by Chinese state-owned enterprises declined for the first time since 2014, particularly in infrastructure investment, although private investment remained more robust.[66] Part of this decline stemmed from Beijing's tighter control over capital outflows and broader attempts to regulate foreign investment. In addition, analysts cited growing investor wariness over bilateral ties. According to a KPMG and University of Sydney report, only 35% of Chinese firms surveyed said they felt welcome to invest in Australia, declining from 52% in 2014. 70% of respondents said that political tensions had made them more cautious about invest-

62. "Foreign investment statistics," Department of Foreign Affairs and Trade, https://dfat.gov.au/trade/resources/investment-statistics/Pages/statistics-on-who-invests-in-australia.aspx. Data includes direct, portfolio, and other investments.

63. Chinese Investment in Australia (CHIIA) Database, East Asian Bureau of Economic Research, Crawford School of Public Policy, Australian National University, released fall 2018, http://www.chiia.eaber.org/

64. Greg Jericho, "Following the money: where China's $40bn investment in Australia is going," *Guardian*, October 8, 2018; Susan Travis, "The Story of Chinese Direct Investment in Australia (2014-2017)," *EABER Working Paper Series No. 133*, October 2018.

65. Greg Jericho, "Following the money: where China's $40bn investment in Australia is going," *Guardian*, October 8, 2018.

66. Michael Heath, "Chinese Investors Grow Wary of Australia as Tensions Rise," *Bloomberg*, June 12, 2018.

ing in Australia.[67] Nonetheless, there remained a mood of cautious optimism and Chinese investment in Australia was still relatively robust compared to Chinese investment in other countries.[68]

Cultivating Domestic Stakeholders

In Australia, there remain considerable divisions among societal groups on their levels of support for Chinese capital. Surveys have found that Chinese investors view Australian business leaders, state governments, and local councils to be highly supportive compared to other actors such as the federal government, Foreign Investment Review Board (FIRB), and the media.[69] Much of these divisions stem from perceptions of and actual gains in economic benefits from China.

Unsurprisingly, business actors have a strong interest in non-provocative foreign policies toward Beijing.[70] They have often criticized government policy for being too harsh toward China. For example, the business community slammed the government's espionage and foreign interference legislation as endangering economic and political ties with Beijing.[71] The Australia China Business Council, representing major corporations doing business with China, expressed concern in a written submission to parliament over the government's "disproportionate response" and the fostering of an "atmosphere of suspicion. Mining magnate Andrew Forrest also called for a stop to the ongoing debate that "fuels distrust, paranoia and a loss of respect."[72]

Some observers have criticized a permeation in the business community on being grateful to China, including Australian businessman James Packer's previous comment that Australia should express "grat-

67. Hans Hendrischke and Wei Li, "Chinese investment in Australia falls as political debate hits confidence," *The Conversation*, June 12, 2018, https://theconversation.com/chinese-investment-in-australia-falls-as-political-debate-hits-confidence-98144.

68. "Demystifying Chinese Investment in Australia: June 2018," KPMG, June 12, 2018, https://home.kpmg/au/en/home/insights/2018/06/demystifying-chinese-investment-in-australia-june-2018.html.

69. Hans Hendrischke and Wei Li, "Chinese investment in Australia falls as political debate hits confidence," *The Conversation*, June 12, 2018, https://theconversation.com/chinese-investment-in-australia-falls-as-political-debate-hits-confidence-98144.

70. See also Bob Carr, *Diary of a Foreign Minister*, NewSouth (2014), p.182, 254.

71. Glenda Korporaal, "Politicians Endanger China Links," *The Australian*, March 7, 2018.

72. Glenda Korporaal, "Business lobby lashes China transparency bill," *The Australian*, March 6, 2018; Glenda Korporaal,"Politicians endanger China Links," *The Australian*, March 7, 2018

itude" to China.[73] In private meetings with the government, major company executives expressed fears that Beijing would impose retaliatory tariffs.[74] Australian winemakers facing delays at Chinese customs quickly lobbied for Canberra to resolve political tensions with Beijing.[75] A range of business actors, such as the head of a mining firm and a former senior politician who is now president of the Australia China Business Council, have also called for Canberra to be more supportive of China's Belt and Road Initiative (BRI), an ambitious plan to promote Chinese investment and infrastructure projects across a range of countries.[76]

In addition, the higher education sector has been a vocal advocate of maintaining positive relations with Beijing. International education is Australia's third-largest export, contributing around US$21.7 billion in 2017. Many Australian universities are now dependent on Chinese students as a major source of revenue. Around a third of foreign students in Australia are from Mainland China, constituting 125,000 students in 2018, with 60 percent at the leading Group of Eight universities in Australia.[77]

University leaders have criticized the government's tough response over CCP influence as "Sinophobic" and unwarranted. There have been a number of incidents in which universities have canceled events relating to contentious issues such as Tibet or overseas dissidents, or when Mainland Chinese students and on-campus organizations (the Chinese Students and Scholars Association) have vocally protested individual lecturer statements or actions that they perceived to undermine PRC interests, leading to university apologies.[78] Universities Australia, a coalition body, sent a delegation of vice-chancellors to Beijing in April in an effort to reassure China and forestall any cut-off of Chinese student enrollment.[79]

State governments have also been active in promoting closer economic cooperation and implement-

73. Interview, Richard McGregor, Australian journalist and senior fellow at the Lowy Institute, Sydney, March 12, 2018.
74. Interview, Australian journalist, Sydney, March 12, 2018.
75. "Australian winemakers press prime minister to end rift with China," *Reuters*, June 6, 2018.
76. David Wroe, "'How empires begin.' China has made its global move. This is Australia's response," *Sydney Morning Herald*, June 22, 2018.
77. Jordan Baker, "'A knowledge race': Australian universities set to suffer drop in students from China," *Sydney Morning Herald*, https://www.smh.com.au/education/a-knowledge-race-australian-universities-set-to-suffer-drop-in-students-from-china-20190301-p5113e.html
78. See e.g. John Ross, "Australian universities' student recruitment from China flatlines," *Times Higher Education*, March 5, 2018.
79. John Ross, "Australian universities' student recruitment from China flatlines," *Times Higher Education*, March 5, 2018.

ing policies to attract Chinese capital. This has carried on despite apparent diplomatic tensions between Australia and China. For example, in late 2018, New South Wales (which is apparently the largest state recipient of PRC investment) signed a Memorandum of Understanding (MoU) with a major Chinese airline to boost tourism.[80] Even more contentiously, the state government of Victoria signed an MoU on China's Belt and Road Initiative, to the surprise of the federal government.[81] This went against Canberra's previous decision not to formally sign onto the initiative due to strategic concerns, although it had signed a MoU on cooperating with BRI projects in third countries.[82] While the MoU is not a legally binding agreement, its political symbolism points to strong elite interest in the economic opportunities provided by Chinese capital.

A Balancing Act

While Canberra's tough rhetorical and legal response to China's political financing activities points to the limitations of such an approach for gaining influence, Australia by and large perceives closer economic and political ties with China to be in its national interests. This balancing act is reflected in both government policies as well as public attitudes.

Canberra has continued efforts to keep bilateral ties on a positive track. The foreign minister stated publicly that Australia does not see China "as posing a military threat to Australia," distancing the Australian government from the U.S. National Security Strategy released in January 2018.[83] Before he was ousted in a party leadership challenge, the Australian prime minister had announced his intention to visit Beijing to repair trade relations, particularly as Australian businesses complained of unusual Chi-

80. "NSW strikes deal with China Eastern Airlines," *ETB Travel News*, November 7, 2018, http://australia.etbtravelnews.global/371020/nsw-strikes-deal-with-china-eastern-airlines/.

81. Paul Karp, "Scott Morrison rebukes Victoria for signing up to China's Belt and Road initiative," *The Guardian*, November 5, 2018.

82. Andrew Greene and Andrew Probyn, "One Belt, One Road: Australian 'strategic' concerns over Beijing's bid for global trade dominance," *ABC*, October 22, 2017; David Wroe, "Foreign Affairs ministry opts for secrecy over China infrastructure agreement," *Sydney Morning Herald*, July 30, 2018.

83. Fergus Hunter, "'We have a different perspective': Julie Bishop distances Australia from US on China, Russia threat," *Sydney Morning Herald*, January 29, 2018, https://www.smh.com.au/politics/federal/we-have-a-different-perspective-julie-bishop-distances-australia-from-us-on-china-russia-threat-20180129-h0rbzz.html.

nese customs delays.[84] The following administration, under Scott Morrison, announced a new US$31.5 million foundation, the National Foundation for Australia-China Relations, to promote closer economic and cultural cooperation, and appointed a top China specialist as Australia's next ambassador to Beijing.[85]

Public attitudes also remain mixed regarding China, reflecting the opposing outcomes of subversive carrots and stakeholder cultivation. While a 2018 poll by the Lowy Institute found that "feelings" toward China were measured at 58 degrees (out of 100), unchanged from 2017, in the 2019 poll the "feelings" had cooled down to 40 degrees.[86] 52% of respondents in 2018 but only 32% in 2019 trusted China to act responsibly in the world. In 2018, 82% viewed China as 'more of an economic partner than a military threat', an increase of three points from 2017, and a majority of respondents regarded China as the world's leading economic power.

While these figures suggest an understanding of China's economic importance – generated through stakeholder cultivation, this comes along with wariness of China as a source of subversive carrots interfering in Australia's domestic politics. 63% of respondents in 2018 were concerned about China's foreign influence in Australia's political processes, and 41% believed that foreign interference in Australian politics was a critical threat to national security (89% of respondents believed that foreign interference was either a critical or important national security threat). In 2019, this had increased to 49% of respondents thinking that foreign interference was a critical national security threat (with 93% saying that it was either a critical or important threat). 44% felt that when considering which foreign companies should be allowed to supply new technology for important services in Australia, the government's first priority should be to protect Australians from foreign intrusion, over bringing the most advanced technology or keeping prices down, suggesting broad support for the government's decision to ban Huawei and ZTE from building 5G networks.

We also see growing suspicion of economic inducements from China. 72% of respondents in 2018 and

84. "Australian Prime Minister Malcolm Turnbull to visit China to improve trade relations," Reuters, May 19, 2018, https://www.scmp.com/news/china/diplomacy-defence/article/2146877/australian-prime-minister-malcolm-turnbull-visit-china.

85. Ben Packham and Geoff Chambers, "Morrison puts $44m into foundation to improve China ties," *The Australian*, March 28, 2019.

86. Lowy Institute Poll, http://lowyinstitutepoll.lowyinstitute.org/

68% in 2019 thought that the Australian government was allowing too much investment from China, an increase from merely 56% in 2014. In 2019, 79% agreed that China's infrastructure investment projects across Asia were part of China's plans for regional domination, 52% disagreed that these projects were good for the region, 74% felt that Australia was too economically dependent on China, and 73% agreed that Australia should try to prevent China from increasing its influence in the Pacific. 77% felt that Australia should do more to resist China's military activities in our region, even if this affected the economic relationship, an increased from 66% in 2015.

While the Australian public has been more skeptical of foreign investors in general, not just against China but also against Japan and the United States in the past.[87], and some have argued that the share of foreign ownership matters more than the investor country,[88] data from the opinion surveys above point to growing public concern over China's economic statecraft, not just within Australia but also in the Asia-Pacific region more broadly. Suspicion of infrastructure projects elsewhere underline the longer-term spillover reputational costs from using subversive carrots in a high accountability country.

Although the overall economic relationship has remained largely robust, there are fears that the Australian economy is vulnerable to Chinese government coercion. Reports of Australian coal, beef, and wine exports being held up at Chinese ports, under the guise of custom inspections but alleged by some as a political move,[89] point to the latent leverage provided by economic linkages with China. But Australia's position as a supplier of raw materials suggests that the Chinese economy is actually more dependent on Australia's.[90] The demand-driven nature of Mainland Chinese students in Australia means that it is not as easy for Beijing to turn off the tap, and PRC airline companies have also been major bene-

87. Interview, Peter Drysdale, professor emeritus and head of the East Asian Bureau of Economic Research, Australian National University, March 6, 2018. See also Lim, "Coercive Economic Diplomacy: Power, Interdependence and Statecraft in Asia."

88. James Laurenceson et al., "Chinese investment in Australian infrastructure assets: accounting for local public preferences," *China Economic Journal* 12, no. 1 (2018).

89. Jason Scott, Dan Murtaugh, and Bloomberg, "China Restricts Australian Coal Imports in Likely Retaliation to Huawei 5G Ban," *Fortune*, February 21, 2019, http://fortune.com/2019/02/21/china-australia-coal-imports/; Kirsty Needham, "China's coal industry lashes Australia for 'irresponsible comments'," *Sydney Morning Herald*, April 12, 2019.

90. Interview, Peter Drysdale, professor emeritus and head of the East Asian Bureau of Economic Research, Australian National University, March 6, 2018.

ficiaries of expanded tourist routes between China and Australia.[91] Rather, political retaliation by the Chinese government, such as canceling leader visits, has been more likely.[92] China's economic coercion could backfire by making commercial actors more wary of political costs of doing business with China. Beijing's removal of the velvet gloves by economically coercing Australia would send a strong negative signal to other countries and alter international perceptions of China.[93]

Conclusion

Overall, there remain divisions in Australia about how to manage the economic benefits alongside political risks in its relationship with China. Economic interdependence has arguably created a buffer against political tensions through the long-term cultivation and empowerment of Australian domestic actors with vested interests in positive ties with Beijing. This suggests a longer-term political payoff in cultivating stakeholders as an economic statecraft strategy.

We have seen significant domestic coalitions lobbying for more cooperative policies toward China, exerting policy pressure on Canberra. In Australia, the most vocal China advocates are in fact certain local and national politicians as well as major business actors who either have received direct economic benefits from China or have vested economic interests. The allure of economic benefits has undoubtedly induced a perception in Canberra that negative political ties with Beijing are not in its national interest, causing political (and certainly business) leaders to engage in a delicate dance to avoid 'angering' China unnecessarily.

At the same time, subversive carrots have created negative reputational costs for China's economic statecraft. Attempts to use political donations from CCP-linked individuals to shape political discourse generated quick public and political backlash, linked to perceptions of foreign interference in Australia's democratic processes. Canberra pushed forward with a tough rhetorical and legal response to China's

91. Interviews, senior diplomat working on Asia-Pacific issues at Department of Foreign Affairs and Trade, Canberra, March 8, 2018; Richard McGregor, Australian journalist and senior fellow at the Lowy Institute, Sydney, March 12, 2018.

92. Interview, senior diplomat working on Asia-Pacific issues at Department of Foreign Affairs and Trade, Canberra, March 8, 2018; "China shunned Australia's minister during recent visit: diplomat," *Reuters*, May 31, 2018.

93. Interview, Peter Jennings, executive director of the Australian Strategic Policy Institute and former senior-level government official, Canberra, March 7, 2018.

use of subversive carrots, despite protestations from some quarters. The strong public blowback against such carrots underscore the limitations of Beijing's current approach, even against the larger context of economic interdependence and stakeholder cultivation.

This has also had longer-term negative implications for China's overseas image. Chinese investment – a key aspect of Beijing's economic diplomacy – is facing greater political scrutiny overall, exacerbated by common assumptions that all economic activities have the hand of Party-state behind them. The political impacts of outbound Chinese investment are often mediated and worsened by widespread perceptions of cohesive state control over capital.

How China uses its economic capabilities when interacting with liberal democracies is an increasingly salient topic of concern. Many developed countries such as the United States and various European nations are starting to grapple with the implications of China's economic inducements, particularly as Beijing continues to expand its Belt and Road Initiative. The Australia case underlines the dilemmas faced by developed democracies in accepting Chinese capital and managing economic and political ties with Beijing.

Even high public accountability systems need to maintain vigilance about institutional, political, social, and economic vulnerabilities that can potentially be exploited. Accountable political processes and institutions promote resilience, but their openness and inclusiveness can also provide avenues to exercise influence through economic statecraft. The political access afforded to donors and individuals covertly linked to the CCP (or any other foreign government), even if the strings have not yet been pulled for a specific policy change, can pose a latent concern for national security.[94] Existing CCP and United Front-linked networks in Australia will largely remain intact even after the current public backlash dies down.[95] As Verbal said about the mysterious Keyser Soze in the movie *The Usual Suspects*, "The greatest trick the Devil ever pulled was convincing the world he didn't exist."[96]

94. Interview, Nick McKenzie, Australian journalist, Melbourne, March 16, 2018.
95. Interview, Primrose Riordan, Australian journalist, Canberra, March 8, 2018.
96. Thanks to Nick McKenzie for suggesting this quote.

Chapter 8

Reeling Japan In: Cultivating Key Stakeholders

This chapter examines how China successfully employed stakeholder cultivation in Japan, a country with high public accountability. China enticed Japan with economic benefits in the two decades leading up to Sino-Japanese normalization in 1972. Beijing's main political goal was to secure Japanese diplomatic recognition of Mainland China instead of Taiwan. The Chinese government actively targeted business leaders, pro-China politicians, and the public in Japan. This created new societal interests supporting economic and diplomatic relations with China, and these domestic groups exerted sustained political pressure on the Japanese government to pursue bilateral normalization. This case provides external validity for my theoretical framework, showing that the arguments apply across different time periods and geopolitical contexts.

Returning to the supply-side model discussed in Chapter 2 of where economic statecraft comes from, it was easier for Beijing to use stakeholder cultivation for two reasons. First, during the postwar period, China was in an earlier stage of economic development and its domestic political economy was less corrupt. Second, Beijing's goals were less instrumental and more long-term in this case. Achieving diplomatic recognition required engaging with multiple stakeholder and changing minds over time, rather than just a one-off statement or transaction for which subversive carrots lend themselves.

Stakeholder Cultivation in Sino-Japanese Normalization

China enticed Japan with economic benefits in the two decades leading up to Sino-Japanese normalization in 1972. Beijing's political goals were to secure Japanese diplomatic recognition of Mainland China instead of Taiwan, as well as to drive a wedge between Japan and the United States, including on the international trade embargo that had been imposed on China. While acknowledging that a range of Japanese individuals had inherent interests in expanding relations with China (whether motivated by economics or a sense of Asianism and war guilt),[1] and that China itself also saw Japan as a source of economic growth and industrialization,[2] in this section I focus my argument on the strategic targeting of key pivotal societal groups via Japan's political system as part of China's economic engagement strategy, effectively accelerating the process of normalization. Scholars have argued that Japan's China policy during that time involved a multiplicity of actors, rather than a coherent top-down strategy; in particular, Japanese non-governmental actors played a major initiating role in expanding economic and political relations, as well as shaping the government's policies toward China.[3] Figure 8.1 shows the increase in Japan's trade with China in the 1950s and 1960s, in both absolute value and as a proportion of Japan's economy.

In line with its stakeholder cultivation strategy, the Chinese government actively targeted business leaders and pro-China politicians in Japan. Beijing was strategic in working through Japan's domestic political system, engaging with a diverse range of political and economic figures. Top business leaders, leftist legislators (or Diet members), as well as certain figures from the ruling conservative party were often involved in the numerous rounds of bilateral talks and trade agreements. Interactions slowly shifted from a non-governmental to a quasi-governmental and eventually more formal diplomatic basis. This created new domestic coalitions supporting economic and diplomatic relations with China, and these actors exerted sustained pressure on the Japanese government to pursue improved relations with the Mainland. In the 1960s, Japan pursued expanding trade relations with China even under criticism from the

1. Yoshihide Soeya, *Japan's economic diplomacy with China, 1945-1978* (Oxford University Press, 1998).
2. Amy King, *China-Japan Relations after World War Two: Empire, Industry and War, 1949-1971* (Cambridge University Press, 2016).
3. Soeya, *Japan's economic diplomacy with China, 1945-1978*.

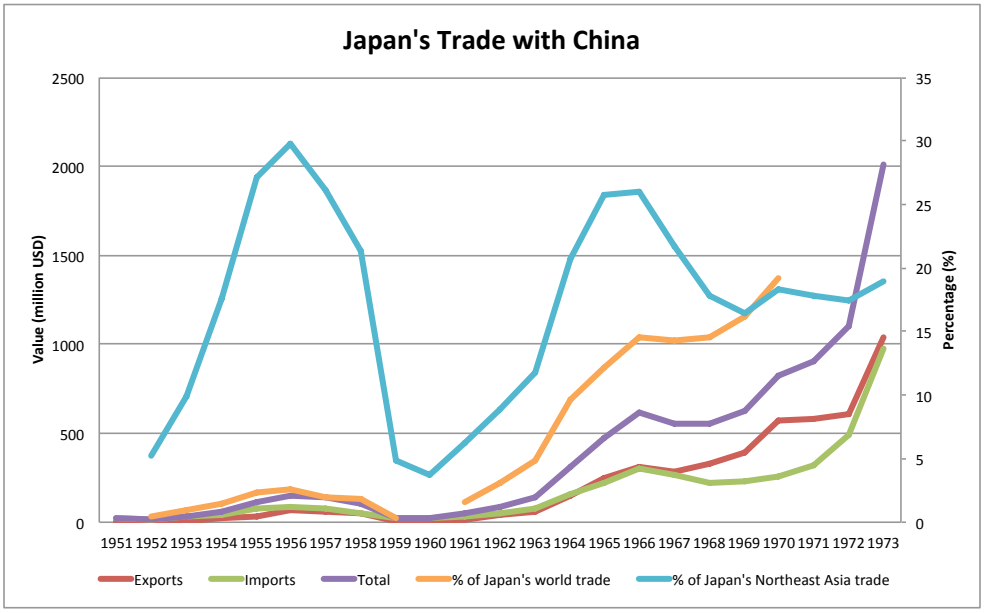

Figure 8.1: Japan's trade with China in the run up to normalization

United States. The following decade, Sino-Japanese normalization was achieved, a huge milestone in which Tokyo finally recognized the Mainland over Taiwan.

"Using the people to push the government"

The key thrust of Beijing's economic statecraft strategy was to "use the people to push the government" (*yimin cuguan*, or 以民促官).[4] In this spirit, China would focus on engaging with Japanese businessmen and Diet legislators, in order to promote non-governmental trade as well as raise public awareness of economic exchange with the Mainland. This would eventually spur more formal trade agreements and eventually official political talks leading to diplomatic normalization between the two countries' governments. Zhou Enlai, the Chinese premier, played a leading role in this process of economic and political engagement. His often-stated goal was to use non-governmental and people-to-people exchanges to "pull the Japanese government" into the picture – underlining this ultimate end goal was Zhou's phrase "depending only on the people is insufficient; without the people it is also impossible" (*zhikao minjian*

4. Interview, Takeyoshi Jiro, Japanese businessman and member of the China-Japan Trade Promotion Association during that period, July 13, 2017.

buxing, meiyou minjian ye buxing, or 只靠民间不行,没有民间也不行)[5]

In a 1954 speech to a visiting Japanese Diet members along with academic and cultural delegations, Zhou emphasized the cultural commonalities and economic complementarities between the two countries, and especially the importance of friendly relations at the people-to-people level as a "foundation" for improving Sino-Japanese ties.[6] Speaking with another Japanese business delegation in June 1956, Zhou said that the resumption of bilateral relations had to be "pushed forward" by the people of both countries. According to Zhou, the extensive interactions and exchanges between non-governmental i.e. "people's organizations" were critical in improving governmental relations and facilitating direct official contact, thus "paving the way forward" for normalization of diplomatic relations. By this time, people-based organizations had signed a total of fifteen agreements, ranging from the railway and fishing industries to science and trade.[7]

First steps: engaging with sympathetic Japanese actors

Japanese politicians and businessmen who had previously lived and worked in China proved to be critical sources of influence back home in Japan – they were instrumental in setting up civil society organizations that sponsored delegations to the Mainland and played important negotiating and signatory roles in trade agreements with China, and were prominent voices in lobbying the Japanese government to deepen ties with Beijing.[8] Key proponents of Japan-China trade in the 1950s included those linked with the Japanese Communist Party (JCP) and the progressives, as well as executives of major companies and pro-China conservative politicians. The legislators who were most keen on expanding Sino-Japanese relations often had electoral constituents and political supporters who hoped to gain economically from developments in the bilateral relationship.[9]

Some key Japanese organizations were the Japan-China Trade Promotion Association (JCTPA), the

5. Interview, Takeyoshi Jiro, Japanese businessman and member of the China-Japan Trade Promotion Association during that period, July 13, 2017.
6. Enlai Zhou, *Zhou Enlai waijiao wenxuan* (Zhongyang wenxian chuban she, 1989), 87-93.
7. Ibid., 168-171.
8. King, *China-Japan Relations after World War Two: Empire, Industry and War, 1949-1971*.
9. Ryosei Kokubun et al., *Japan-China Relations in the Modern Era* (London and New York: Routledge, 2017), 44, 65.

Japan Association for the Promotion of International Trade (JAPIT), and the Diet Members' League for the Promotion of China-Japan Trade. The JCTPA was closely tied to the Japanese Communist Party and had a greater ideological affinity with the PRC, while the JAPIT was formed by top business executives interested in deeper economic relations with China and had a more internationalist approach to the Mainland. The Diet Members' League, on the other hand, was composed of legislators from a range of political parties.

Japanese businessmen who had spent considerable time doing business in China were major drivers of closer relations with the Mainland. There was a widespread belief that the Japanese economy would benefit from greater access to the Chinese market,[10] although in the postwar era the U.S. market became more important.[11] Particularly in the 1960s, there was a huge gap between the business community and the government, with the business sector pushing for rapprochement with Beijing and the Japanese Cabinet following Washington.[12] There were also differences between the business community. While the manufacturing sector had stronger economic linkages to Taiwan, the steel industry regarded Mainland China as a priority because of its natural resources. However, the steel sector constituted a powerful lobbying force because it was an important donor to the ruling LDP, and the sector comprised many firms and labor organizations, employed many workers, and had the ability to activate people and votes.[13] The Ministry of International Trade and Industry (MITI) was also positively inclined toward building closer ties with the PRC. The presence of favorable domestic actors within Japan allowed Beijing to capitalize on Japanese economic intentions. From the PRC's perspective, Japanese firms served as its vocal friends.[14]

The first two Japan-China Private Trade Agreements, concluded in June 1952 and October 1953, were driven largely by left-leaning, pro-China figures. At the 1952 Moscow International Economic Conference, the Chinese delegation invited Japanese attendees (who were a mix of Diet League and JCTPA members to negotiate a six-month barter trade agreement with a two-way value of 30 million pounds

10. Interview, Matsuda Yasuhiro, professor at the University of Tokyo, Tokyo, May 31, 2018.
11. Interview, Sugiura Yasuyuki, National Graduate Institute for Policy Studies, Tokyo, May 30, 2018.
12. Interview, Matsuda Yasuhiro, professor at University of Tokyo, Tokyo, May 31, 2018.
13. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.
14. Interview, Takeyoshi Jiro, former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, May 30, 2018.

sterling. The second year-long agreement involved pro-China Diet members and the China Council for the Promotion of International Trade (CCPIT). At the same time, the Yoshida government refused to sell China items covered by the U.S.-led embargo, so only 5% and 38% of the agreed value was traded for the two respective trade agreements.[15]

Although some Japanese were interested in promoting economic ties with the Mainland, official bureaucrats such as in the Ministry of Foreign Affairs (MOFA) were far more reluctant and tended to be pro-U.S. (and hence pro-Taiwan) in their views. When Takasaki Tatsunosuke was given permission to lead a Japanese delegation to the Bandung Conference in April 1955, MOFA sent three senior officials as "monitors." While Takasaki was able to have a secret meeting with Zhou Enlai during the conference, a second planned meeting was canceled by the Japanese side, likely due to intervention from the MOFA officials present.[16]

The third agreement, between CCPIT, JAPIT, and the Diet Members' League, also included trade exhibitions for both countries' products in Tokyo and Osaka, held in December 1955.[17] Negotiations for the Fourth Japan-China Private Trade Agreement in 1958 were concluded between a Nippon Steel delegation on the Japanese side and the China Metals Import Corporation and China Minerals Corporation on the PRC side. This agreement increased its political demands on the Japanese government, even amidst Prime Minister Kishi's actions to strengthen political ties with Taiwan. Apart from an expansion of the agreement to five years and 100 million pound sterling, an accompanying memorandum established trade representative offices that were allowed to fly the national flag and had the equivalent of diplomatic treatment, which sparked protests from the U.S. and ROC governments. In addition, both sides promised to push their governments to conclude a governmental trade agreement.[18][19] Negotiations had dragged due to PRC insistence on these political demands. The Japanese side expressed support for the trade agreement but did not officially acknowledge the PRC flag, leading to disappointment on the Chinese side.[20]

15. Mayumi Itoh, *Pioneers of Sino-Japanese Relations: Liao and Takasaki* (Palgrave Macmillan, 2012), 97.
16. Ibid., 99-103.
17. Kokubun et al., *Japan-China Relations in the Modern Era*, 44-45, 49.
18. Ibid., 54.
19. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 38.
20. Itoh, *Pioneers of Sino-Japanese Relations: Liao and Takasaki*, 108.

The insertion of political outcomes and the involvement of the Diet Members' League reflected Beijing's desire to use economic ties in pursuit of political normalization.

During the 1950s, trade agreements often benefited Japanese companies more than Chinese, as was the case for a fishery agreement giving fishing rights to Japanese fishermen in the East and Yellow Seas. Large-scale and highly-publicized trade exhibitions and other activities also generated growing public interest and support.[21] Building up contacts with PRC officials, Japanese individuals traveled to the Mainland for trade fairs, as part of trade delegations (e.g. the Diet Members' League visited in September 1953), and political delegations (including the Parliamentary Delegation in October 1954). A PRC trade delegation led by the vice-minister for foreign trade visited Japan for six weeks in 1955 and met with over 4500 Japanese individuals. They were instructed by Beijing to "put economic trade at the center of discussions" and "pay special attention" to influential actors such as the conglomerates, big capitalists, and top officials.[22]

Broadening stakeholder cultivation

Realizing that openly supporting JCP revolutionary activities was counterproductive for its goals, after 1952 the Chinese government shifted its strategy to building 'peaceful' links with various groups in Japan that could favorably influence public opinion on China as well as increase political divisions.[23] Beijing targeted its lobbying efforts toward Japanese businessmen and leftist elements to push Tokyo for expanded economic ties. According to PRC Foreign Ministry documents, the goal was to "make the Japanese people and those enthusiastic about Japanese trade increase their resentment of the Hatoyama government on the Sino-Japanese trade issue, and increase their hatred of, and opposition to, US imperialism."[24] Through speeches to visiting Japanese delegations and *People's Daily* editorials, Beijing emphasized how Tokyo's relationship with the United States was detrimental to Japan's economy, while China could bring many benefits.[25] From the mid 1950s, Beijing started to strengthen ties with the Japanese Socialist Party

21. Zhang, *Beijing's Economic Statecraft During the Cold War, 1949-1991*.
22. King, *China-Japan Relations after World War Two: Empire, Industry and War, 1949-1971*, 104-105.
23. Kurt Werner Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi* (Manchester University Press, 1990), 103.
24. King, *China-Japan Relations after World War Two: Empire, Industry and War, 1949-1971*, 119-120.
25. Ibid., 120-121.

(JSP), which aligned itself with PRC policy. JSP members frequently met with Zhou and other Chinese officials, and in January 1957 the party officially declared its opposition to 'two Chinas' and called for the Japanese government to normalize relations with the Mainland.[26] Moreover, Zhou asked the JSP to"courageously undertake the task" of pushing Tokyo to de-recognize Taiwan and normalize relations with the Mainland.[27] China also provided funds to labor organizations in Japan, who tended to view the Mainland in a positive light.[28]

During the 1959 election cycle in Japan, foreign policy toward the PRC was an important (and divisive) issue, and the Chinese government also looked to capitalize on these political divisions, including through closer links with the JSP and selective economic inducements to amenable Japanese businesses. During a visit to China, JSP leader Asanuma Inejiro made extensive anti-U.S. statements, causing debate even within his party. In addition, Beijing agreed to small-scale "consideration trade" with a leftist trade union in Japan, that would bring together a select group of Japanese firms willing to accept the PRC's political conditions – while intentionally excluding the LDP from such benefits.[29] This again demonstrates how the Chinese government sought to use economic inducements to empower pro-China elements and achieve policy changes in the Japanese political system.

At the same time, China worked to establish pivotal contacts in Japan's political system, cultivating relations with individuals in the ruling party who could lobby on behalf of PRC interests. Beijing had found that working on with the leftists and the JSP, which constituted a minority, was insufficient, and so it turned its efforts toward politicians from the LDP.[30] Exchanges with the LDP, the ruling conservative party, would naturally have a more direct impact on the government's policies.[31]

In an effort to entice more moderate LDP politicians and split them away from the Kishi administration, Liao Chengzhi, the PRC's leading Japan hand, was deliberate in his attempts to build closer ties with

26. Zhou, *Zhou Enlai waijiao wenxuan*, 225-227.
27. Ibid., 229.
28. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.
29. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 126-127.
30. Interview, Matsuda Yasuhiro, professor at University of Tokyo, Tokyo, May 31, 2018.
31. Interview, Takeyoshi Jiro, Japanese businessman and former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, May 30, 2018.

LDP politicians, seeking meetings during a 1957 visit with prominent figures such as Ishibashi Tanzan (the former prime minister) and Matsumura Kenzo.[32] The Chinese were far more conciliatory during closed-door meetings with these two figures. Both Liao and Zhou emphasized the importance of economic ties and said that diplomatic relations were not a pre-requisite.[33] Even when political relations worsened, including after the Nagasaki flag incident in May 1958 under the Kishi administration, Beijing continued exchanges with pro-China groups in Japan while cutting ties with supposed 'reactionary' forces.[34]

As part of stakeholder cultivation, Chinese officials placed high priority on building and maintaining good personal relations with these key Japanese politicians. Zhou Enlai 'always made time to meet', while JAPIT delegations were able to skip customs on their visits to China.[35] When Matsumura passed away in 1971, Beijing sent high-level figures to attend his funeral.

In the fall of 1959, Ishibashi made several preparatory visits to Beijing, then followed by Matsumura, who was also accompanied by other LDP politicians and major news journalists. At this time, Zhou no longer insisted on preconditions of diplomatic ties before trade exchanges. These visits accentuated the split between the pro-China and more mainstream factions in the LDP, causing dissent within the Kishi administration that also shaped the domestic political crisis over the revision of the U.S.-Japan Security Treaty.[36] China's softer, enticing approach in the 1950s would later evolve to more explicit political conditions once the Japanese business community had grown heavily invested in economic exchanges with China, with the support of key political figures in Japan.

Increasing politicization: Friendship Trade and LT Trade

In August 1960, Zhou Enlai presented three trade principles, namely intergovernmental agreements, private contracts, and "individual considerations."[37] Under the framework of Friendship Trade, Japanese

32. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 23.
33. King, *China-Japan Relations after World War Two: Empire, Industry and War, 1949-1971*, 50-153.
34. Kokubun et al., *Japan-China Relations in the Modern Era*, 55.
35. Interview, Takeyoshi Jiro, Japanese businessman and former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, May 30, 2018.
36. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 128-130.
37. Zhou, *Zhou Enlai waijiao wenxuan*, 289-291.

companies certified as 'friendly' by the Chinese side – e.g. supporting Zhou's Three Political Principles (non-adversarial policy toward China; non-support for Two China's; non-obstruction of diplomatic normalization) – were able to trade with China and participate in the biannual Canton Trade Fair.[38] Both JCTPA and JAPIT became increasingly influential in selecting 'friendly firms' that accepted Beijing's three principles as well as the principle of inseparability of economics and politics. Most of the roughly 300 friendly firms were small, with fewer than 10 employees, but dominated trade exchanges between the two countries.[39]

At the same time, with growing Sino-Soviet tensions as well as perceptions that a governmental trade agreement was still far from reality under the Ikeda administration, Beijing adjusted its goals to focus on cultivating sympathetic stakeholders in Japan and building private trade relations (that would gradually lead to governmental involvement). Speaking with a JSP delegation in January 1961, Mao Zedong described "the anti-mainstream [LDP] politicians Matsumura, Miki, Ishibashi, Takasaki and Kono as indirect allies."[40] Through Friendship Trade, the Chinese government also broadened its economic outreach beyond just the smaller China-specialized trading firms affiliated with JCTPA, to also draw in the major trading corporations (and their dummy companies).[41] Zhou expressed interest in welcoming a Japanese delegation comprising those who were influential in 'big business'.[42] Although the zaibatsu only officially reached out to the PRC in 1970, amidst the changing international environment, well before that it had established secret dummy companies to participate in Friendship Trade.[43]

In 1962, Beijing's intensified contacts with conservative Japanese politicians as well as big business leaders paved the way for a new semi-governmental trade agreement to supplement Friendship Trade. Although this marginalized the JSP's role in bilateral economic relations, the Chinese government wanted to broaden its base of support in Japanese domestic politics. Zhou subsequently described China's strat-

38. Kokubun et al., *Japan-China Relations in the Modern Era*, 67.
39. Sadako Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," in *The Foreign Policy of Modern Japan*, ed. Robert Scalapino (1977), 175–204.
40. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 135.
41. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 64-68.
42. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 135.
43. Interview, Inoue Masaya, professor at Seikei University, Tokyo, May 28, 2018.

egy of engaging with former prime ministers (both socialist and conservative) who were supportive of the PRC as an "indirect," "cumulative," and "gradual" way to achieve bilateral normalization.[44]

As a result of these efforts, in 1963 another trade channel was launched called LT Trade (named after the two representatives who signed the memorandum, Liao Chengzhi and Takasaki Tatsunosuke). Although the Japanese government was involved in the negotiations process, much of the initiative was driven by business actors and LDP politicians.[45] The Japanese individuals involved in laying the groundwork for LT Trade were top business leaders such as Okazaki Kaheita, the president of ANA who was affiliated with JAPIT; Takasaki himself was formerly president of Manchuria Heavy Industries and had been a member of the Kishi cabinet. Another key negotiator, Matsumura Kenzo, was also a senior LDP politician with whom Beijing had established links a few years back. Responding to Japanese reservations about accepting the 'inseparability of politics and economics,' Zhou did not insist on political relations as a pre-condition for economic ties, instead emphasizing gradual measures toward political and economic normalization.[46] But in an interview, Okazaki said that Beijing always treated LT trade officials as government representatives.[47]

From the Japanese perspective, Matsumura and his team sought to establish a new trade system without explicit political conditions attached. The Ministry of International Trade and Industry was also supportive of this move, given its interest in developing more markets, while the Foreign Ministry did not make any formal objections.[48] Okazaki believed in the importance of developing a new trade system that would achieve the critical objective of normalizing diplomatic ties with China, by including more mainstream governmental figures as well as larger industrial manufacturers.[49]

While then-prime minister Ikeda publicly maintained a hardline position, in private he supported the Matsumura faction's moves to promote trade and even sent his chief adviser as part of a 1962 Japanese

44. Zhou, *Zhou Enlai waijiao wenxuan*, 340-341.
45. Soeya, *Japan's economic diplomacy with China, 1945-1978*, Ch. 5.
46. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 142.
47. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China."
48. Interview, Inoue Masaya, professor at Seikei University, Tokyo, May 28, 2018.
49. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China."

delegation to China.[50] Ikeda and Matsumura were on good terms; the prime minister had given Matsumura his backing, telling him that "I have to face toward the United States, but you should face toward China."[51] MITI was also in close contact with the LT trade office. Even though the ministry was not officially involved in the negotiations, it provided funds and appointed some officials in support of the LT trade office in Beijing, and also sent two officials to participate in a 1963 trade delegation.[52][53]

Under the LT Trade framework, Japan was to export steel, chemical fertilizer, and industrial plant, while China was to export items such as coal, iron ore, soybeans. In particular, Takasaki agreed to export an industrial plant and allowed China to finance payments with the Japan Export-Import Bank (JEXIM), which went against Tokyo's indicated policy of avoiding Japanese government involvement. This decision subsequently led to a diplomatic spat with Taiwan.[54] In addition, Takasaki agreed to export high quality ammonium sulphate, although the ammonium sulphate industry had initially been hesitant to participate because of its reliance on the Taiwan market. Rewarding his decision, China quickly purchased 200,000 tons in 1963 (four times the agreed amount), and became the top importer of Japanese ammonium sulphate in 1964.[55]

Although LT Trade provided a short-term boost in bilateral economic exchanges and promoted more extensive interactions with Japanese individuals and organizations (including the elevation of contacts to a semi-government level), the framework was also vulnerable to politicization, particularly under the Sato government (which was seen as being anti-PRC). Political and economic relations deteriorated when the Japanese government decided not to issue Exim bank credits for exporting the promised industrial plant to China.[56] Another leading Chinese figure, Nan Hanchen, threatened to cut down trade exchanges; Liao also expressed unhappiness that no current Japanese government member had visited China.[57]

50. Chalmers Johnson, "The Patterns of Japanese Relations with China, 1952-1982," *Pacific Affairs* 59, no. 3 (1986): 402–428.
51. Interview, Takeyoshi Jiro, Japanese businessman and former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, May 30, 2018.
52. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China."
53. Interview, Inoue Masaya, professor at Seikei University, Tokyo, May 28, 2018.
54. Kokubun et al., *Japan-China Relations in the Modern Era*, 67-70.
55. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 88-90.
56. Radtke, *China's relations with Japan, 1945-83: the role of Liao Chengzhi*, 163-165.
57. Ibid., 165-166.

Friendship Trade, which was based on Japanese assent to PRC political preferences, was able to survive deteriorating political ties in the 1960s. These friendly elements ensured relative stability in economic exchanges, and also provided a channel for the Chinese side to communicate their political preferences.[58] Political relations worsened publicly in the 1960s with the Cultural Revolution in China and reduced support from the Sato administration for LT Trade, which made it a difficult environment for Matsumura to operate.[59] However, key Japanese officials kept bilateral trade going through "*fumie* diplomacy" – "placidly agreeing to any and all of Zhou's demands for gestures of Japanese obsequiousness" in order to maintain channels and connections between the two countries.[60] The term "*fumie* diplomacy" as coined by Chalmers Johnson refers to a loyalty test taken under coercion; it has its origins in a tablet with a crucifix (*fumie*) that the Tokugawa military government forced people to stomp on to prove they were not Christians.

Under conditions of stakeholder cultivation, the behavior of domestic Japanese actors invested in maintaining positive ties with the PRC often reflected Beijing's preferences. With the Sino-Soviet split, a rift also developed between the JCP and CCP in the 1960s, with JCTPA and the Japan-China Friendship Association caught in the crosshairs. Other Japanese firms then banded together to remove their representatives from positions of power and to purge JCP members, in order to prevent loss of trade opportunities with China. This consolidated the influence of the JSP and the pro-China LDP politicians.[61] JAPIT took on the leading role in Friendship Trade, adopting the radical language of the Cultural Revolution. To maintain friendly firm status, businesses complied with PRC political demands, attacking Japanese "reactionaries" as well as U.S. "imperialists" and Soviet "revisionists." According to reports, around 300 of these firms mobilized 1500 people for political demonstrations against Prime Minister Sato's visit to Tai-

58. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 129.

59. Interview, Inoue Masaya, professor at Seikei University, Tokyo, May 28, 2018; Interview, Takeyoshi Jiro, Japanese businessman and former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, May 30, 2018.

60. Johnson, "The Patterns of Japanese Relations with China, 1952-1982."

61. Soeya, *Japan's economic diplomacy with China, 1945-1978*; Sadako Ogata, *Normalization with China: A Comparative Study of U.S. and Japanese Processes*, Research Papers and Policy Studies (Institute of East Asian Studies, University of California-Berkeley, 1988).

wan in August 1967.[62] Interestingly enough, 1960s saw a wave of Japanese intellectual romanticization of China and justification of Chinese actions. When Beijing agreed to allow Japanese journalists into China, they soon fell in line with China's political conditions for reporting news (and those who did not were eventually expelled).[63]

Zhou capitalized on the decline in LT trade to rachet up the political pressure on Japanese economic actors in late 1967 and early 1968. The Chinese side criticized their Japanese counterparts for not taking a stronger stance on Sato's pro-Taiwan, anti-PRC behavior, and expressed that further trade negotiations would require political pre-conditions. In response, the LT Trade office issued a statement blaming the Sato administration for worsening the bilateral relationship and calling for the elimination of political obstacles in order to expand economic ties. This marked the first time such actors had publicly gone against official Japanese government policy. The resulting memorandum signed in March 1968 and subsequent trade agreements signed in 1969 and 1970 all stipulated that both sides would uphold the inseparability of politics and economics, and trade relations would be based on China's three political principles – thus making political conditions a basis of the continued economic relationship.[64] As such, the Japanese negotiators of this Memorandum Trade often yielded to Chinese demands and political conditions, further blurring the lines between economics and politics.[65] China's use of stakeholder cultivation was paying off.

In April 1970, Zhou proposed four conditions for Sino-Japanese trade, in which China would not trade with firms that (i) aided Chiang Kai-shek or Park Chung Hee; (ii) had major investments in Taiwan or South Korea; (iii) provided military equipment for U.S. actions in Vietnam, Laos, and Cambodia; (iv) were U.S.-Japanese joint ventures or U.S. subsidiary companies. Japan then expressed a commitment to these four conditions in a quasi-governmental memorandum signed in March 1971 (which also criticized the Sato government's policies toward China). Both JAPIT and Memorandum Trade officials suggested that dummy companies would have to cut ties with their parent companies, or that the parent companies

62. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 73-78.
63. Johnson, "The Patterns of Japanese Relations with China, 1952-1982."
64. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 101-105.
65. Ogata, *Normalization with China: A Comparative Study of U.S. and Japanese Processes*.

would have to clarify their position on China.[66]

While these were challenging terms, many Japanese firms, including major corporations, agreed to follow these conditions, even surpassing the expectations of the pro-China trade promotion associations in Japan.[67] The smaller 'friendly firms' certainly felt the need to demonstrate loyalty because of their reliance on the Chinese market.[68] The steel and fertilizer industries, now heavily dependent on the Mainland market, readily accepted Zhou's conditions, in contrast to their initial reluctance in the 1960s.[69] For example, Sumitomo Kagaku, which had also been singled out by Beijing, quickly accepted the four conditions and agreed that its chairman would no longer participate in the Japan-ROC Cooperation Committee. This was driven by a desire to protect its chemical fertilizer and steel industrial interests in China – its president emphasized the value of the PRC market in the longer run, especially compared to the limitations of the Taiwan market.[70]

Four of Japan's five major steel firms also readily announced the acceptance of Beijing's conditions.[71] The textile and industrial machinery sectors as well as trading firms based in the Kansai area, all with greater business interests in the Mainland market, were also at the forefront.[72] Kansai business leaders in particular had a history of close economic interactions with China and saw the China market as a means to regain commercial growth; top figures had been active in shipbuilding contracts and industrial plant exports in the 1960s. In fact, surveys showed that Kansai business actors were far more eager to establish diplomatic relations with Beijing sooner and even before Washington did.[73] These developments underscored how China's gradual provision of economic benefits were able to sway the political inclinations of

66. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China."
67. Interview, Takeyoshi Jiro, Japanese businessman and former representative in Beijing for the Japan Association for the Promotion of International Trade, Tokyo, July 13, 2017.
68. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China."
69. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 114.
70. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 186.
71. Ibid., 187.
72. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China"; Ogata, *Normalization with China: A Comparative Study of U.S. and Japanese Processes*.
73. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 190-191.

key economic sectors.

Moreover, Zhou's political conditions were also able to lure in the four major trading corporations who still had significant trade ties with Taiwan – Mitsubishi, Mitsui, Mraubeni-Iida, and Itochu. When China refused to trade with their dummy companies, three of the four severed management and financial ties with their parent companies in order to be designated as friendly to China.[74] Marubeni's dummy company, Wako Koeki, sent a public letter of protest to its parent firm, and severed its capital and personnel links and even its office location.[75] In a press interview, Wako Koeki's president said that he would seek to change the positions of the four major trading firms and to "fight for the resignation of the Sato government in order to improve Japan-China relations."[76] In advance of July 1970 general meeting of the Japan-ROC Cooperation Committee, JAPIT issued a statement criticizing the committee and slamming the four major trading firms for acting as the "economic nucleus of revived Japanese militarism." This was followed by a similar joint statement from 134 friendly firms, and a statement by seven business organizations that those who attended the general meeting would be in violation of the basic principle of Japan-China trade and would be excluded from the PRC market.[77]

Within the next two years, the four parent companies had agreed to accept the four conditions.[78] This was aided by international and domestic political momentum in favor of recognizing the PRC. For example, Itochu, one of the largest trading firms in Japan, had been active in establishing trade and investment relations with the Mainland, including through a dummy company (Shin Nihon Tsusho) in 1960s. Despite existing political constraints, Itochu "took the first step" to build ties with China, with the involvement of key leadership including the president, CEO, and managing director. In an interview, Itochu's then-managing director, who had also been based in Beijing as chief representative of China affairs for the corporation, told me that he was sent to Hong Kong from March to June 1971 to investigate and confirm news of impending U.S.-China rapprochement (President Nixon later announced his

74. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 116-118.
75. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 188.
76. Ibid.
77. Ibid., 189.
78. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 116-118.

planned visit to China in July 1971).[79] Beijing subsequently requested that Itochu's president visit China, which he did in March 1972.

As China emerged from the Cultural Revolution, it embarked on a more activist and moderate foreign policy, leading to diplomatic recognition by countries such as Canada (in 1970) as well as the 1971 UN General Assembly resolution to recognize the PRC as the official government of China. This provided the final push for a growing number of Japanese firms to reach out to Beijing. Companies with minimal business holdings in the Mainland began to seek out opportunities. In early 1971, Toyota announced its intention to start exporting to the China market. Soon after a meeting with Chinese officials, it requested to participate in the spring 1971 Canton Trade Fair, and issued a statement that it would not make direct investments in Taiwan and South Korea. Other automobile manufacturers soon followed in Toyota's footsteps.[80] Moreover, Beijing became more flexible on applying the four conditions, with the purpose of promoting the surge of Japanese business actors seeking to enter Mainland China.[81]

Stakeholder cultivation induced proactive efforts by Japanese business actors to reach out to the Mainland, and their "pro-China tilt" was crucial in creatin a domestic atmosphere conducive to normalization with Mainland China.[82] In spring of 1971, big business leaders (the *zaikai* community) from Kansai and Tokyo had made plans to visit China, even before the Nixon Shock occurred (suggesting Japan's desire for normalization grew independently from U.S. actions). In April that year, both groups of business leaders had also met with the deputy head of the PRC national table tennis team during his visit to Japan.

The point of the business delegations was to lay the foundation for diplomatic normalization. During their visit in September 1971, the Kansai delegation stated recognition of Beijing as the legitimate government of China, that Taiwan was part of China, and that diplomatic normalization was a pre-condition for expanded economic exchanges. Although Tokyo business leaders were more cautious, the president of Nippon Steel (the remaining holdout among the five major steel companies) also announced – again

79. Interview, Fujino Fumiaki, former managing director and chief representative of China affairs for Itochu, Tokyo, May 30, 2018.

80. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 192.

81. Ibid., 193.

82. Kokubun et al., *Japan-China Relations in the Modern Era*, 92-93.

prior to knowledge of Nixon's visit – that he would accept Zhou's four conditions and recognize 'one China.'[83] These trends again highlight the effectiveness of China's economic inducements in altering the political preferences of Japanese firms in favor of China's foreign policy positions and diplomatic normalization.

Amidst a growing China fever, domestic public opinion in Japan was also supportive of normalization, in response to the rhetoric by political and business leaders, scholars, and the mass media.[84] Newspaper surveys in June 1968 found that 42% of respondents thought that Japan should restore relations with Beijing as soon as possible, 37% supported friendly relations short of formal ties, and only 5% favored the status quo approach of trade without political relations (2% supported continuing diplomatic ties with Taiwan). From 1970 to 1972, consistently over 50-60% of the Japanese public supported normalization with the PRC immediately or as soon as possible.[85] According to the *Yomiuri Shimbun* poll in April 1968, 35% of respondents expected "more friendly" relations with China, and only 10% was satisfied with the current situation. In late 1970, Japanese legislators formed the Parliamentarians' League for the Normalization of Japanese-Chinese Relations, counting 379 of 738 total Diet members, with 95 from the LDP and the rest from a range of opposition parties.[86] Working jointly with the Japan Socialist Party, the Parliamentarians' League also sponsored a People's Congress for the Restoration of Diplomatic Ties between Japan and China.[87] With this decisive pro-China tilt, the Japanese government had little room to maneuver on China policy and the climate for diplomatic normalization was consolidated. China's stakeholder cultivation was successful in creating a coalition of diverse Japanese actors that pushed for more rapid diplomatic normalization.

Even before U.S. started to engage in ping pong diplomacy, in January 1971 Prime Minister Sato had brought up Sino-Japanese normalization as being on the political agenda in the near future. With advice

83. Soeya, *Japan's economic diplomacy with China, 1945-1978*, 119-125.

84. Ryosei Kokubun, "From the "1972 System" to "Strategic Mutual Benefits" - Japan's Foreign Policy toward China," in *Nihon no Gaiko Dai 4 Kan [Japan's diplomacy vol. 4]*, ed. Ryosei Kokubun (2013).

85. Akio Watanabe, "Japanese Public Opinion and Foreign Affairs: 1964-1973," in *The Foreign Policy of Modern Japan* (1977), 105–146.

86. Tao Peng, "China's Changing Japan Policy in the Late 1960s and Early 1970s and the Impact on Relations with the United States," *Journal of American-East Asian Relations* 15 (2008): 147–171.

87. Ogata, *Normalization with China: A Comparative Study of U.S. and Japanese Processes*.

from an academic study group to formulate China policy, the LDP secretary general (Hori Shigeru) sent a letter to Zhou Enlai offering to recognize Beijing as the sole legitimate government of China. Hori himself had also had secret talks with a key advisor to Matsumura and had met some Chinese officials at the LT Tokyo office. Zhou, however, decided to tactically reject the offer and wait for a subsequent Japanese prime minister who would be somewhat more politically beholden to Zhou because of the surge in 'global infatuation' with China.[88]

How important was stakeholder cultivation?

In highlighting the role of China's stakeholder cultivation, I do not intend to characterize it as the primary or sole factor behind Sino-Japanese diplomatic normalization. The path to normalization was a long and complicated process. Here, I discuss some additional factors at play.

First, I do not argue that China was the only or dominant player with agency in 'pushing' economic diplomacy toward Japan. In Tokyo, there was underlying interest in and desire to maintain close ties with the Mainland, and Japan was important in faciliating continued economic interactions. It was keen to reach out to China for both economic and political reasons. Under Tokyo's multi-directional post-war FP, it sought to 'shake hands with multiple countries', and stable relations with Beijing was seen as necessary [89] Many mainstream conservative politicians – of the so-called Yoshida School – would continue to hold the view (if privately) that Communist China should not be contained as a 'cold war' enemy and should be regarded as the official government of China. Tokyo's political strategy was thus to use pro-Bejing LDP members to open separate channels to the Mainland while having top political leaders take official pro-Taiwan positions to please Washington.[90] The Japanese government's policy was to keep economic and political relations separate, while allowing trade to develop.[91]

While certain Japanese actors may already have been inclined toward maintaining positive economic and political relations with China, Beijing's stakeholder cultivation further empowered their voices and

88. Johnson, "The Patterns of Japanese Relations with China, 1952-1982."
89. Interview, Matsuda Yasuhiro, professor at University of Tokyo, Tokyo, May 31, 2018.
90. Johnson, "The Patterns of Japanese Relations with China, 1952-1982."
91. Ogata, *Normalization with China: A Comparative Study of U.S. and Japanese Processes*.

enabled pro-PRC actors to consolidate their agenda, as seen by increasingly unified positions across the political spectrum. Incremental advances in private and quasi-governmental economic exchanges provided cumulative benefits and a concrete framework to promote closer Sino-Japanese ties that persisted despite domestic political vagaries in both countries. Some scholars have suggested that while business leaders had their own interests in leaning toward China, Beijing's economic and diplomatic cultivation in tandem with pro-PRC groups such as JAPIT also helped to serve China's foreign policy interests.[92]

In addition, international-level reasons were of course key in facilitating official Sino-Japanese normalization, namely the Sino-Soviet split and Kissinger's visit to China paving the way for Sino-U.S. rapprochement. Conventional literature points to Washington as a major constraint on Tokyo's ability to establish diplomatic relations with the Mainland. A shift in U.S. policy as well as the growing international support for the PRC allowed Japan to jump on the wagon. This argument would suggest that structural changes in international politics, rather than economics, were the reason for Tokyo's recognition of Beijing. For example, a few weeks after Nixon announced in July 1971 his planned visit to China, one major firm (Shin Nihon Seitetsu, a steel company)who had held out against ties with Beijing reversed its position and agreed to the four political conditions. Top *zaikai* leaders (a powerful group of business elites) made official contact with high-ranking Chinese officials, even though PM Sato was furious.[93]

At the same time, there was already plenty of momentum to normalize relations with Beijing even before U.S. rapprochement became clear, as evident in 1970 and early 1971. While certain key business leaders close to the Sato government had faced political constraints, and Nixon's announced visit to China removed those constraints, they would not have been able or interested to move as quickly toward Beijing without the preliminary groundwork of contacts, resources, and personal and political trust built up by other Japanese political and economic actors. This pro-China shift among all levels of the business community further accelerated similar trends in mainstream factions of the LDP and also affected how leaders contending to succeed Sato as prime minister moved to more clearly accepting Beijing's terms for

92. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 203.
93. Ibid., 193-195.

diplomatic normalization.[94]

As such, even with these existing Japanese inclinations and international constraints, Beijing's adoption of a stakeholder cultivation approach was immensely helpful in moving diplomatic ties forward. Engaging with a range of domestic actors in Japan laid important groundwork for accelerating the process of diplomatic normalization between the two countries. It strengthened and expanded pro-China constituencies within Japan, and contributed to positive public attitudes toward the Mainland. It also made the bilateral relationship more resilient despite political ups and downs. The Japanese government's increasing participation in civil trade meant that the strategy of 'using the people to push the government' was successful in bringing economic (and political) interactions to more official levels. Although pro-China LDP politicians, while major figures in Sino-Japanese relations, constituted a minority faction in Japanese domestic politics,[95] they were able to form lobbying coalitions with other political parties and business organizations. While international constraints and shifts served as the 'gale' to make normalization happen, China's stakeholder cultivation over the past couple of decades provided the necessary 'foundation' for normalization to occur – and at a rapid pace.[96]

An understanding of success could also vary depending on whose perspectives we are coming from. Scholars of Japan's foreign diplomatic history may view China's economic statecraft as having limited influence, but from the point of view of China's foreign policy, 'using the people to push the government' was successful in achieving certain goals.[97] In particular, stakeholder cultivation faciliated the consolidation of pro-PRC voices and interests within Japan, providing a powerful force for diplomatic normalization once the conditions were right. It is presumably true that Tokyo's official recognition of Beijing required a shift in Sino-U.S. relations, but at the same time, without stakeholder cultivation, the counterfactual would likely have been a slower, drawn-out process of normalization. It was the cultivation of ties through the business community (and favorable political elites) over the postwar decades that accel-

94. Ogata, "The Business Community and Japanese Foreign Policy: Normalization of Relations with the People's Republic of China," 203.

95. Interview, Inoue Masaya, professor at Seikei University, May 28, 2018; Interview, Sugiura Yasuyuki, National Graduate Institute for Policy Studies, Tokyo, May 30, 2018.

96. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.

97. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.

erated a change in the political environment among LDP factions and the general public, facilitating the emergence of new leaders keen to reach out to Beijing and achieve diplomatic normalization.

Japan in the contemporary era

What is the role of economic interests in Japan's foreign policy toward China in the more contemporary era? Linkages between political and economic elites appear to have reduced somewhat. Corruption scandals in the late 1980s and early 1990s sparked stricter regulations on political contributions, with businesses forbidden from making political contributions. This reduced the coziness of ties between government and business, and also served to further separate politics and economics in Japan's foreign policymaking.[98] This suggests that the line of influence from business interests to political leaders may be less direct today, which may increase the difficulty of economic statecraft particularly under conditions of greater security tensions.

Pro-China voices have also been relatively muted due to generational changes[99] and China's arguably increasing assertiveness, including its military presence and tensions over the disputed Senkaku/Diaoyu islands. Some business groups have lobbied for reducing political tensions with Beijing, although the business community remains highly pluralistic and diverse. In the aftermath of anti-Japanese protests in China in 2005, Japanese firms who continued to operate in China (although many moved to Southeast Asia) asked the Japanese government to change its policy, leading to significant changes post-2006 across the three prime ministers after then-PM Koizumi.[100] After escalating tensions in 2012 over the Senkaku/Diaoyu island disputes, the Keizai doyukai (Japan Association of Corporate Executives, 经济同友会) issued a report asking the Japanese government to reconsider its foreign policy position on the disputed islands.[101] While some Japanese businessmen voluntarily state their support for China, Chinese pressure on business actors only works for the small group that is already favorable toward Beijing.[102]

98. Kokubun, "From the "1972 System" to "Strategic Mutual Benefits" - Japan's Foreign Policy toward China."
99. Interview, Fujino Fumiaki, former managing director and chief representative of China affairs for Itochu, Tokyo, May 30, 2018.
100. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.
101. Interview, Matsuda Yasuhiro, professor at University of Tokyo, Tokyo, May 31, 2018.
102. Interview, Matsuda Yasuhiro, professor at University of Tokyo, Tokyo, May 31, 2018.

Japan's foreign policy after the 1989 Tiananmen Square incident presents another potential case study for China's economic statecraft. Despite international sanctions and against international opinion, the LDP under the Takeshita faction was quick to restart ODA to China in 1991. Japanese companies had major interests in resuming aid, as they had benefited significantly from ODA projects in China, including road and infrastructure construction. Sun Pinghua, a senior foreign affairs official who had also served as director of the China-Japan Friendship Association, frequently visited Tokyo to meet with Japanese leaders during this period.[103] Chinese officials capitalized on close ties with major Japanese firms and influential Japanese politicians to request for continued ODA from Tokyo.[104]

Conclusion

In Japan during the postwar and early Cold War era, China's adoption of a stakeholder cultivation approach that benefited a range of domestic actors (and Japan's economy more broadly) created sustainable domestic coalitions that lobbied in favor of more rapid diplomatic normalization with China. Working through established domestic political processes and institutions endowed these actors with greater legitimacy and bargaining power. While not the only factor affecting the long and complicated path toward Tokyo's recognition of Beijing, I argue that the results of stakeholder cultivation served as essential foundation on which normalization could occur. Over time, pro-China voices gained momentum and clout, buffering the bilateral relationship through political difficulties and allowing official actors to quickly jump on board the process of diplomatic recognition.

At the same time, economic statecraft may have limits. Japan's official recognition of the PRC only took place after structural changes in international-level politics. Thus, while stakeholder cultivation was necessary, it was not sufficient. As with other foreign policy tools, at times fundamental national security concerns can constrain the effectiveness of any strategy.

This case study also underscores the longer time horizon and less direct payoffs of stakeholder cultivation. This inducement strategy required a concerted and sustained effort over two decades, but was

103. Interview, Sugiura Yasuyuki, National Graduate Institute for Policy Studies, Tokyo, May 30, 2018.
104. Interview, Kawashima Shin, professor at the University of Tokyo, Tokyo, May 29, 2018.

guided by a relatively strong Chinese state, with a powerful leader (Zhou Enlai) holding the reins. Beijing's weaker political and economic position at that time perhaps gave it the patience and endurance to cultivate important relationships with Japanese elites. Yet it was also able to employ coercion when needed as the flip side of inducements – once economic benefits are received, the withdrawal of (or a threat to withdraw) continued inducements also serves as leverage for further political demands.

Chapter 9

Conclusion and Policy Implications

This book has examined how the political effectiveness of economic statecraft is determined by the interaction between the sender's inducement strategy and the level of public accountability in the target country. When inducements undermine or circumvent domestic political processes and institutions – inducements that I classify as subversive carrots – they will backfire in high accountability countries, but produce payoffs in low accountability countries. In contrast, stakeholder cultivation produces political dividends in high accountability countries but is inefficient in low accountability countries. To test these arguments, I drew on case study and survey experimental evidence, using multiple cross-case comparisons at the country level, leveraging within-country variation of inducement strategies as well as public accountability, and using within-case process tracing. In this concluding chapter, I turn to discussing the generalizability and validity of my theoretical arguments, with reference to recent global developments. In addition, I draw out the implications for the trajectory of China's economic statecraft and how policymakers should respond.

Scope Conditions

Before delving into the generalizability and broader applications of my theory, I outlined one important scope condition: the effectiveness of economic statecraft is likely to be constrained by fundamental secu-

rity concerns. Economic statecraft is not able to trump issues that threaten the existence or survival of the target state. If the sender poses a major sovereignty threat or demands a policy that undermines national survival, even if the economic inducement offered aligns with the target's accountability environment, it will remain very unlikely that target country leaders will compromise sovereignty and security.

Taiwan is one prominent example of how Beijing's economic statecraft has failed to fundamentally shift elite or public attitudes in the face of fundamental concerns. This is despite Beijing's attempts at using economic statecraft to move Taiwan toward reunification. Despite growing economic interdependence over several decades, and Beijing's open policy of *yishangweizheng, yiminbiguan* (to peddle politics through business and to influence the government through the people), for example by enticing Taiwanese businessmen to invest in the Mainland and attempting to build up domestic groups in Taiwan to support closer ties,[1] China's economic statecraft has arguably failed in the broader picture.

On one level, economic statecraft plausibly helped to deter independence efforts in Taiwan, by cultivating stakeholders that saw the benefits of peaceful relations and the costs of seeking independence. Nonetheless, given Beijing's primary goal of achieving reunification, economic statecraft has not shifted public attitudes favorably in that regard. Although some have argued that Beijing successfully targeted economic inducements to farmers situated in the voting base of the pro-independence political party (DPP) in southern Taiwan, removing bans and tariffs on selected fruit imports to weaken electoral support for the DPP,[2] others have found that there was no substantial effect.[3] Sentiment has turned against Beijing in recent years, with the current president hailing from the DPP. Because reunification represents a fundamental sovereignty threat for Taiwan, elites have limited maneuvering room and most business actors refrain from wading into the political fray, thus constraining the success of economic statecraft – or other policy tools.[4] Places such as Taiwan and Hong Kong, where PRC influence poses a fundamental

1. John Q. Tian, *Government, Business, and the Politics of Interdependence and Conflict across the Taiwan Strait* (New York, NY: Palgrave Macmillan, 2006), 3-4.

2. Norris, *Chinese Economic Statecraft: Commercial Actors, Grand Strategy, and State Control*.

3. Stan Hok-wui Wong and Nicole Wu, "Can Beijing Buy Taiwan? An empirical assessment of Beijing's agricultural trade concessions to Taiwan," *Journal of Contemporary China* 25, no. 99 (2016): 353–371.

4. Tian, *Government, Business, and the Politics of Interdependence and Conflict across the Taiwan Strait*.

threat to sovereignty and survival, are likely to see more pronounced levels of pushback against Beijing.[5]

However, for most countries, the enthusiasm for economic benefits associated with Beijing's purported largesse outweighs potential security concerns. Even for countries that have alliance relationships with the United States or have territorial disputes with China, while these factors may play a role in policy discourse, they have less explanatory power and lower salience for the public than issues of adherence to (or violation of) domestic political processes and institutions in recipient countries.

Generalizability and Validity

The arguments presented in this book have focused on the Asia-Pacific region. This is because the region is where the economic-security trade-offs exacerbated by China's economic statecraft are most acute. However, the mechanisms and patterns analyzed in this book can be translated to other countries and regions. In recent years, China's Belt and Road Initiative has garnered increasing attention, with waves of media reporting first on the challenges and backlash faced by the BRI in several countries, followed by another wave of debate on the BRI's resilience, negotiation, and adaptation. These global developments have been in line with the predictions of my argument, where dominant concerns over economic inducements center on transparency, sustainability, and comportment with procedural norms. Backlash in these countries has not been simply about anti-China sentiment or the rejection of China, but about demanding greater transparency and higher standards. This supports the mechanisms of procedural violations in economic statecraft being brought to task by public accountability institutions in recipient countries.

Similar mechanisms of public backlash against China's subversive carrots have occurred in developing democracies. In countries such as Sri Lanka and the Maldives, incumbent leaders have lost office over highly corrupt and economically unsustainable investment projects from China.[6] In Sri Lanka in 2015,

5. Nathan, "China's influence and the pushback: Tentative conclusions beyond Hong Kong and Taiwan."

6. Ellen Barry, "New President in Sri Lanka Puts China's Plans in Check," *New York Times*, January 9, 2015, https://www.nytimes.com/2015/01/10/world/asia/new-president-in-sri-lanka-puts-chinas-plans-in-check.html; Shashank Bengali, "How an island nation's new leaders are trying to unravel a web of secret deals with China," *Los Angeles Times*, November 6, 2018,

a wave of anger, including public protests against extensive corruption implicating a US$1.5 billion port and a US$1.4 billion port city, lead to the ouster of then-president Rajapaksa. Subsequently, the new government has attempted to diversify its investment partnerships by turning to Japan and India.[7]

Similarly, in the Maldives, former president Abdulla Yameen was kicked out of office in fall 2018 – he had undertaken major loans from Beijing for corrupt infrastructure projects. He had also secretly negotiated a free-trade agreement with China in late 2017, which was passed in parliament in less than an hour despite criticism from opposition legislators.[8] After coming into office, the new government withdrew from the FTA and is seeking to renegotiate with Beijing over the inflated costs of infrastructure contracts due to government kickbacks.[9] In Pakistan, local leaders and communities have been critical of the ambitious China-Pakistan Economic Corridor, which has been shrouded in mystery, lacked transparency and consultation, and brought little local benefits.[10] The new president, Imran Khan, was elected on promises to review BRI projects and demand improved terms.[11] The government has also pushed for China to shift its investments away from large-scale infrastructure and energy projects to public goods provision and manufacturing industries that bring more economic benefits to local populations. In March 2019, the Pakistani government diverted US$171.6 million from CPEC to fund other projects, while the Chinese government agreed to provide US$1 billion in grants for socioeconomic development and poverty reduction projects, such as healthcare, education, and agriculture.[12]

Political observers and analysts from major think tanks and multilateral institutions have come up with similar findings. A June 2019 World Bank report highlighted how the risks of BRI projects are ex-

https://www.latimes.com/world/asia/la-fg-maldives-china-20181106-story.html.

7. Marwaan Macan-Markar, "China runs into Belt and Road barriers in South Asia," *Nikkei Asian Review*, February 5, 2019, https://asia.nikkei.com/Spotlight/Asia-Insight/China-runs-into-Belt-and-Road-barriers-in-South-Asia.

8. "Maldives rushes through trade pact with China despite opposition," *Reuters*, December 8, 2017.

9. Simon Mundy and Kathrin Hille, "Maldives seeks to renegotiate with China over Belt and Road debt," *Financial Times*, January 31, 2019.

10. Adnan Aamir, "China's Belt and Road plans dismay Pakistan's poorest province," *Financial Times*, June 14, 2018; Michael Kovrig, "National Ambitions Meets Local Opposition Along the China-Pakistan Economic Corridor," *The Diplomat*, July 24, 2018.

11. Jamil Anderlini, Henny Sender, Farhan Bokhari, "Pakistan rethinks its role in Xi's Belt and Road plan," *Financial Times*, September 9, 2018.

12. Khaleeq Kiani, "China commits $1bn for 20 social sector projects," *Dawn*, March 8, 2019; Adnan Aamir, "Pakistan distances itself from China's Belt and Road," *Nikkei Asian Review*, March 20, 2019.

acerbated by the initiative's limited transparency and weak governance in recipient countries, calling for improvements in data reporting and transparency, open government procurement, and adherence to social and environmental standards.[13] Another report by the International Republican Institute criticized the 'opacity' and 'massive corruption' involved in BRI projects, with recipient countries with weak governance, rule of law, and transparency being particularly vulnerable, compared to the resilience of countries with stronger democratic institutions such as independent media and civil society.[14] Danny Russel, former Assistant Secretary of State for East Asian and Pacific Affairs, has written about the credibility problems resulting from the BRI and how Chinese leaders could avoid local backlash by reducing corruption, improving transparency and accountability, introducing safeguards, and engaging with local stakeholders and civil society organizations.[15]

Finally, the book's arguments are also generalizable beyond the case of China's economic statecraft, to any country seeking to use economic statecraft. The mechanisms specified in the theory elucidate the interaction between the type of inducements offered and the recipient's domestic political conditions, and are not based on China-specific factors.

For instance, the U.S. Marshall Plan stands as a prominent example of how stakeholder cultivation to bolster economies in post-war Western Europe succeeded in strengthening U.S. influence at the expense of the Soviets. In the late 19th century, the United States granted Hawaii greater access to the American market in order to prevent rival powers from gaining influence. The growing political clout of the sugar industry and its affiliates then pressured Hawaii to agree to the cessation of Pearl Harbor and eventually annexation by the United States.[16] However, foreign aid from OECD donors such as Japan to corrupt developing countries have failed to produce political influence. In Afghanistan, official U.S. aid – stakeholder cultivation — has often been siphoned off by corrupt elites, whereas bags of cash to Karzai's office

13. "Belt and Road Economics: Opportunities and Risks of Transport Corridors," *World Bank Group*, June 18, 2019, https://www.worldbank.org/en/topic/regional-integration/publication/belt-and-road-economics-opportunities-and-risks-of-transport-corridors.

14. Ed. David Shullman, "Chinese Malign Influence and the Corrosion of Democracy: An Assessment of Chinese Interference in Thirteen Key Countries," *International Republican Institute*, June 2019, https://www.iri.org/resource/new-report-exposes-chinas-malign-influence-and-corrosion-democracy-worldwide.

15. Daniel Russel, "How to Clean Up the Belt and Road," *Bloomberg*, June 11, 2019.

16. Abdelal and Kirshner, "Strategy, Economic Relations, and the Definition of National Interests."

and to Afghan warlords – subversive carrots – were somewhat more successful in gaining their support to fight against the Taliban.[17]

China's Learning Curve

Backlash against China's use of subversive carrots has produced an adverse demonstration effect. China's economic diplomacy has suffered negative reputational costs, with many countries increasingly wary of undertaking Chinese-financed investment projects.[18] But this is not to say that the United States should rest easy, or that the doors have closed on Chinese financing and investment. Many countries remain hungry for foreign investment and infrastructure development, and China is an important player in meeting this demand. My interview and survey findings in countries such as the Philippines, Malaysia, and even Australia, point to a continued ambivalence toward Beijing. China is viewed as a source of economic growth and development, but Beijing's political intentions raise concerns.

As revealed in the case studies of Malaysia and Myanmar, public backlash against the procedural violations of subversive carrots has pushed Beijing to adjust its economic statecraft strategy, paying greater attention to domestic institutions and regulations in recipient countries. Chinese firms are also attempting to improve their public image by participating in social responsibility initiatives and working with civil society actors. China has been ineffective at communication and cooperation in recipient countries,[19] but it has realized the need to pay more attention to public diplomacy and improved governance rather than bypassing regulations, as economics is inevitably wrapped up in the politics of the BRI.[20] Demands by recipient governments for greater transparency and accountability have pressured China to renegotiate terms and engage in a stakeholder cultivation strategy.

17. See e.g. Matthew Rosenberg and Azam Ahmed, "U.S. Aid to Afghans Flows On Despite Warnings of Misuse," *New York Times*, January 30, 2014; Matthew Rosenberg, "With Bags of Cash, C.I.A. Seeks Influence in Afghanistan," *New York Times*, April 28, 2013; Sean Carberry, "Secret Cash To Afghan Leader: Corruption Or Just Foreign Aid?" *NPR*, May 1, 2013.

18. Marwaan Macan-Markar, "China runs into Belt and Road barriers in South Asia," *Nikkei Asian Review*, February 5, 2019, https://asia.nikkei.com/Spotlight/Asia-Insight/China-runs-into-Belt-and-Road-barriers-in-South-Asia.

19. Interview, Pangoal Institution, Beijing, May 16, 2019.

20. Interview, National Development and Reform Commission International Cooperation Center, Beijing, May 17, 2019.

China is slowly learning from its missteps.[21] Even Chinese officials have started sounding cautionary notes over debt sustainability, particularly as economic growth slows.[22] In recent years, Beijing has sought to curb corruption and "irrational" overseas BRI investments,[23] and increased monitoring and regulatory efforts to crack down on illegal activities,[24]. In 2017, it announced plans for a new international development cooperation agency to better coordinate foreign aid in support of China's economic diplomacy and the BRI. The agency would combine the overseas aid-related responsibilities of existing ministries (such as the Ministry of Commerce, Ministry of Finance, and to a limited extent the Ministry of Foreign Affairs), and would work directly under the State Council.[25]

Beijing has gradually started to realize the importance of listening to public opinion in recipient countries and of adhering to recipients' institutional standards and processes. During the 2018 summit of the Forum on China Africa Cooperation, Xi emphasized cooperation over vital infrastructure as opposed to 'vanity projects'.[26] At the second Belt and Road Forum in April, Chinese leaders went beyond the usual bland rhetoric of "win-win," emphasizing mantras of quality infrastructure, zero corruption, high transparency, and clean governance.[27] International pressure from both developed and developing countries pushed Beijing to promote improved institutional standards and cooperation with other developed countries to build infrastructure projects.[28] China's central bank and finance ministry announced new financing criteria to attract investment partners and ensure debt sustainability.[29] In my conversations in Beijing in May 2019, a range of government officials and scholars acknowledged the problem of corrup-

21. Nadege Rolland, "Reports of Belt and Road's Death Are Greatly Exaggerated," *Foreign Affairs*, January 29, 2019, https://www.foreignaffairs.com/articles/china/2019-01-29/reports-belt-and-roads-death-are-greatly-exaggerated.

22. Keith Bradsher, "China Taps the Brakes on Its Global Push for Influence," *New York Times*, June 29, 2018.

23. "China to curb 'irrational' overseas investment by domestic firms in 'Belt and Road' projects," *Reuters*, August 18, 2017.

24. "China to set up system to monitor its firms overseas," *Reuters*, November 28, 2017.

25. "China says new agency will improve foreign aid coordination," *Reuters*, March 12, 2018.

26. "China-Africa summit: Xi denies money being spent on vanity projects," *BBC*, September 3, 2018, https://www.bbc.co.uk/news/world-africa-45394668.

27. Jane Perlez, "How an island nation's new leaders are trying to unravel a web of secret deals with China," *New York Times*, April 25, 2019, https://www.nytimes.com/2019/04/25/business/china-belt-and-road-infrastructure.html.

28. "China's Belt and Road Cracks Down on Corruption in Image Revamp," *Bloomberg*, April 22, 2019.

29. Lucy Hornby, "China pledges to address debt worries over Belt and Road," *Financial Times*, April 25, 2019, https://www.ft.com/content/f7442058-66f9-11e9-9adc-98bf1d35a056.

tion and reiterated China's openness to greater third-party cooperation.[30]

Long-Term Implications

What are some potential long-run implications of my theoretical arguments? Should Beijing tailor its inducement strategy more effectively to match the domestic political conditions in target countries, this could exacerbate global divisions in the quality of governance and accountability institutions across countries. Low accountability countries may become even more authoritarian and corrupt, with the successive corrosion of accountability institutions. On the other hand, there is a broader range of developing countries which, although they tend to be more vulnerable to subversive carrots, have had fairly resilient accountability institutions, as evidenced in multiple incidences of push-back in recent years. This process of pushback and negotiation may take time, but suggests that countries care about the quality of inducements they are receiving, and that it is more difficult for Beijing to buy political influence with its economic clout than Chinese leaders, as well as observers, may have thought..

If China were to adapt its strategy sufficiently to greater emphasis on stakeholder cultivation, its economic and political clout would likely become more significant in the future, even though Beijing would still have to overcome a substantial reputational deficit as well as reform state-business relations. Putting aside great power geopolitical concerns, this may not be a negative development in and of itself – China could help to plug a major gap in infrastructure financing and investment in many developing countries. A genuine approach of stakeholder cultivation would also suggest that Beijing is playing a more constructive role on the global stage, providing public goods and establishing longer-term relationships, rather than merely seeking to buy over elites.

The outcomes of economic statecraft could also be viewed in the broader context of China's overseas influence activities (or so-called sharp power, in the words of the National Endowment for Democracy). Beijing has made increasing efforts to influence the political and informational environment in foreign countries, such as through media ownership, funding of academic institutes and cultural institutions, as

30. Interviews, China Center for International Economic Exchanges, Pangoal Institute, National Development and Reform Commission, Beijing, May 15-17, 2019.

well as the mobilization of ethnic Chinese diaspora communities. An ability to shape the tone of public and elite discourse could ultimately affect the way that economic statecraft is perceived. Overt United Front activities are likely to be seen as foreign interference, further painting China (and any sort of economic diplomacy, even stakeholder cultivation) in a negative light. But effects may be more insidious in countries where there is a relative lack of expertise or attention on China. In such contexts, backlash or support is likely to boil down to the local socioeconomic impacts of China's economic inducements and whether or not they adhere to domestic processes and institutions.

Economic Statecraft and Grand Strategy

How does economic statecraft fit with a country's grand strategy? Scholars have examined economics as foundation for and input to grand strategies and national security policy, and economics as a structural constraint or as a result of structural constraint. In this book, I contribute to understandings of foreign economic policy as a strategic instrument in itself.

To the extent that grand strategy is the pursuit of national interest and national security goals through a combination of domestic and international policies across political, military, and economic means, it entails the use of multiple instruments of statecraft. In this book, I analyzed the outcomes of one important yet understudied instrument – positive economic inducements – when used. This analysis lays the groundwork for further evaluation of inducements in comparison with other instruments, such as economic sanctions or military force, in recognition of the higher-level, multi-variate decisionmaking processes in foreign policy. Future work examining the costs, benefits, processes, and outcomes of inducements versus sanctions, as well as economic tools versus military force, would contribute to understandings of grand strategy and statecraft in international security.

Inducements and Coercion

My theoretical framework could also shed some explanatory light on the effects of China's use of economic sanctions. While conventional arguments suggest that broad sanctions on democratic entities are more

likely to succeed, this book highlights the importance of public opinion backlash in high accountability countries. Public backlash against economic coercion, such as Beijing's attempts to pressure South Korean tourism and consumer product industries over the installation of THAAD, a U.S.-linked missile defense system, has in fact hardened public attitudes toward China, failed in pressuring Seoul to fall in line, and arguably constrained South Korean elites from backing down or looking weak. Similar mechanisms have played out in other countries, including Japan and the Philippines.

Perceptions of China's economic incentives have indeed been further colored by Xi's growing emphasis on domestic ideology and his propensity to wield economic statecraft as leverage and enticement. More prominent uses of coercion, as well as growing fears of so-called "debt trap diplomacy," have also made recipient countries increasingly wary of how economic inducements would enhance Beijing's future coercive leverage. At the same time, uncertainty over U.S. presence and leadership – and, for many countries, a lack of alternative sources for investment financing – have left countries with limited strategic room to maneuver and put a spotlight on China's initiatives.

Current trends suggest that economics is becoming a component of strategic competition among great powers, rather than a force for restraint. As China moves up the value chain and reorients its economy toward domestic consumption, its economy will become more competitive than complementary with the U.S. economy. Industrial policies such as Made in China 2025, which involves state-supported development of new high-tech industries to reduce foreign reliance, suggest that China's economy will become less economically interdependent with the United States and the global economy, and point to further clashes on the nature of international economic rules and institutions.

This has widened the divide between the United States and many other countries, even U.S. allies, on how to deal with China's economic statecraft and its overseas economic activities more broadly. At least for the China case, many recipient countries view the economic benefits as more immediate and more important than the potential notion of future coercive leverage. For recipients that have major security concerns relating to China, these future costs may be a more important part of the decisionmaking calculus. But for most recipients, not least developing countries, the tangible benefits of inducements tend to

outweigh the abstract latency of future costs. Even countries such as the Philippines, which has ongoing territorial disputes with China, are eager to strengthen economic relations with Beijing. Certainly, the scale of China's economic presence makes inducements hard to resist.

Policy Implications

What are the implications for U.S. policy and for foreign policymakers in general? First, perspective matters. Despite the extensive media coverage and political attention given to China's economic statecraft, Chinese investment and aid in regions such as Southeast Asia and Africa still lags behind several other players. Japan remains a leader in infrastructure investment. China tends to offer loans rather than grants, and its terms of repayment are often more demanding for recipient countries. Buying into a simplified narrative of China's unrivaled dominance would likely make it reality, by ceding the policy initiative to Beijing and by unnecessarily pushing recipient countries to regard China as the only option available.

Observers should avoid painting either an overly alarmist or a dismissive gloom-and-doom picture of China's overseas economic activities. The findings from this book have shown that China's expanding forays into foreign aid and overseas investment have not bought it influence. Rather, they have sparked public backlash and a broader narrative of skepticism. Beijing's use of economic inducements has been less effective in producing long-term political results than is commonly assumed.

At the same time, China is recalibrating and learning from its mistakes, meaning that it should not be underestimated. As discussed earlier, political success and failure of Chinese investments vary significantly by country. The domestic politics of recipient countries matter. Strengthening accountability institutions and promoting informational transparency of investment and aid projects—regardless of the source country—would enable bottom-up oversight in recipient countries. Focusing on project quality would improve overall outcomes for the surrounding populations, and avoid framing investment choices for recipient countries—many of whom need infrastructure and development financing—in terms of U.S.-China strategic rivalry.

The U.S. government should also work to promote the availability of alternatives for infrastructure fi-

nancing and investment projects. Without adopting zero-sum rhetoric, Washington could improve institutional resources in tandem with encouraging private commercial actors to play a bigger role, including through public-private partnerships. But the U.S. cannot go it alone. Peer competition in infrastructure financing will be difficult, given the Chinese state's ability to mobilize resources at scale.

Working with regional partners and multilateral institutions will be key

Countries such as Japan and Australia are major providers of aid and investment in their neighborhoods. These actors usually have established institutions along with extensive on-the-ground expertise and deeper knowledge of the domestic political and economic situation, as well as the operating environments in different countries. Cooperation with other major investors and donors, including Japan, South Korea, Australia, and the Asian Development Bank, will help to establish important standards and ensure multiple sources of financing.

Investor countries should also more effectively engage with and promote the use of multilateral institutions, such as the World Bank and the Asian Development Bank. My fieldwork in countries such as the Philippines shows that Chinese financing is often attractive because it moves much more quickly (although sometimes undermining local standards). Working for the reform and streamlining of multilateral lending processes could make these alternatives more appealing and effective. Having excessively rigid, top-down 'gold standards' can sometimes detract from the goals of broadening access to investment and development financing.

The bilateral or multilateral sharing of know-how would also limit Beijing's ability to circumvent accountability processes and institutional standards. Investor countries could work with developing countries and provide technical expertise, resources, and guidance to negotiate or renegotiate better deals with China. Often, developing countries may lack the relevant experience and knowledge, and this approach would be a relatively low-cost and efficient way to promote improved transparency and accountability standards while pushing Beijing to meet these standards.

Finally, Washington should consider developing new institutions to facilitate a more coherent and strategic government response to economic statecraft (by China and others). These institutions would

coordinate information-sharing and policy formulation across different national security and economic bureaucracies. For example, the institutionalized sharing of information and analyses on China's economic statecraft at the global level would overcome potential knowledge siloes among the geographic, regionally focused bureaus in the State Department and the Pentagon.

As countries craft their own policy responses toward China's economic diplomacy, they will also have to struggle with the dilemma between welcoming Chinese capital and potentially greater vulnerability to Chinese interference. Washington needs to ensure that it plays an active, constructive role to avoid alienating other countries and to ensure the United States continues to have a hand in shaping the rules of the global order.

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