



BASC NEWS

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BASC News

Protectionism in the 2008-2009 Financial Crisis

by Vinod K. Aggarwal and Simon J. Evenett

During the current sharp global economic downturn much has been made of the scale of government policy responses, whether it be monetary policy, fiscal policy, or other forms of state intervention. Indeed many argue that the reason the contemporary crisis has not descended into another Great Depression is precisely because of the scale of some government intervention. Yet governments may find themselves under pressure to act from influential sectoral groups, such as company shareholders, employers, trade unions, and the environmental lobby. Moreover, once a government demonstrates its willingness to engage in far-reaching intervention on behalf of one interest it may find itself confronted for requests from others.

Using information from the Global Trade Alert database, we examine the cross-sectoral pattern of trade-related state intervention that has been imposed since the first crisis-related G20 summit in November 2008. A second goal is to

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explore the relative importance of competing explanations for the contemporary pattern of crisis-era protectionism.

A word of caution is in order. It should be recognized that the pattern of state intervention is almost certainly not the same in every country. Still, interesting cross-country tendencies may arise. Moreover, any assessment presented here is necessarily an interim one as the global economy has not yet returned to full health and further state intervention cannot be ruled out.

Rationales advanced for crisis-era state intervention.

One rationale frequently advanced regarding intervention is to mitigate the burdens of adjustment on firms and their employees. Differences across sectors, then, in revenues - or other measures of financial performance - would, on this view, account for the observed pattern of state intervention. However, it should be acknowledged that if the goal of a government is limited solely to addressing the harm felt by employees rather than the firms that hire them then, in principle, one could use an economy-wide scheme rather than a sector-specific one. The adjustment-related explanation, therefore, may need nuance in some cases.

A second rationale advanced frequently during this systemic economic crisis is that measures should simultaneously restore aggregate demand as well as target the impediments to longer-run economic growth. A particularly popular variant of this rationale is to argue that state intervention during this crisis should accelerate "green growth" and the adjustment to a low carbon economy.

The first two rationales view the state as pursuing benign priorities of its own choosing. The associated state intervention may well be far-reaching, even unprecedented in scale and scope. Still, in both rationales governments are taken to be actors that are independently pursuing different aspects of societal good. A third perspective is that self-interested non-state actors seek to influence the design of state intervention by self-interested politicians and bureaucrats.

The third perspective would suggest that the degree of state intervention varies across sectors because not every sector's participants places the same value on the benefits that follow from state intervention, the costs to non-state actors of organizing in the political sphere are dissimilar, government decision-makers may value the support from certain non-state actors differently, and the adverse impact of any state measures on overall national economic performance may vary. A sharp global economic downturn could influence the relative importance of these four factors and, in principle, a new cross-sectoral pattern of state intervention may result.

Traditionally, in industrialized countries trade-related favoritism has been concentrated in the older manufacturing sectors (iron, steel, etc), textiles and clothing, and the agricultural sector. We now consider whether the current crisis-era protectionism departs much in its cross-sectional variation from prior experience and, therefore, whether our understanding of the underlying factors at work needs to evolve.

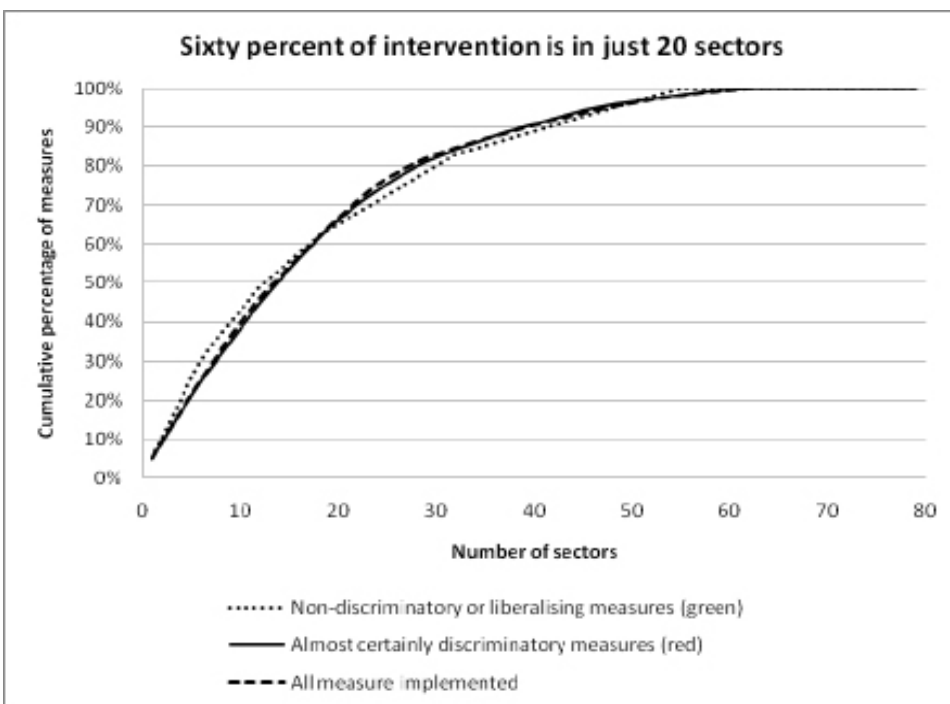


Figure 4.1. *The skewed nature of distribution across sectors.*

Evidence on the cross-sectoral variation in state intervention.

The Global Trade Alert database consists of over 425 investigations of state measures that have been announced or implemented after the first crisis-related G20 summit in November 2008. Each investigation report identifies the trading jurisdiction responsible for the announcement or implementation of the measure, a description of the measure, and an evaluation as to whether the measure introduces, eliminates increases, narrows, or otherwise changes any asymmetric treatment between domestic and foreign commercial interests. A traffic light system is used to distinguish between measures that do not change or improve the relative treatment of foreign commercial interests, that might disadvantage foreign commercial interests, and that almost certainly discriminate against foreign commercial interests.

In addition, each investigation of a state measure in Global Trade Alert identifies those economic sectors that are likely to be affected by a state measure. Details about a state initiative that are in the public domain are sought to identify the sectors affected. This assessment is conducted in a conservative manner. Indeed, if anything, there may be a tendency to under-report the number of affected sectors. The United Nations' CPC scheme for classifying economic activities for both goods and services is employed. The Global Trade Alert website's statistics page enables users to view and download the latest data on the sectoral impact of different state measures undertaken during the current crisis. As the website is updated, so are the reported statistics.

The first finding concerning the cross-sectional variation in the state intervention reported in the Global Trade Alert database is that intervention is highly skewed to a minority of economics sectors. As Figure 4.1 shows, sixty percent of the interventions affect only 20 CPC sectors. This finding holds for different measures of the degree of intervention, whether it be the total number of state measures implemented, the number of measures that almost certainly discriminate against foreign

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Director's Notes

Dear Readers,

We appreciate your interest in the Berkeley APEC Study Center and our ongoing work on political, economic and business trends in the Asia-Pacific. This issue begins with an analysis of protectionism in the current global financial crisis and an update on the recent developments of APEC. Also included are a series of spotlight articles analyzing contemporary economic and political trends in Japan, China, Indonesia, and India, as well as highlights of our latest projects.

In the first article, Simon Evenett and I analyze the governmental response to the 2008-2009 financial crisis by examining the cross-sectoral pattern of trade-related state intervention since the November 2008 G20 Summit. We find that trade protectionism is highly skewed towards a minority of economic sectors that tended to receive protection prior to the onset of the financial crisis, leading us to conclude that little has changed in the factors determining state intervention.

Ren Yi Hooi's **APEC Update** looks at the recent APEC Economic Leaders' Summit in Singapore. She emphasizes the two broad themes of the conference: sustainable growth and greater regional integration. However, she notes that the while APEC's past 20 years have been met with mixed success, the upcoming summits in the US and Japan provide APEC an invaluable opportunity to mitigate the rising tide of protectionism and perpetuate the recent momentum of global integration.

In the first of our collection of **BASC Spotlight** articles, Atsushi Yamada explores the role that FTAs play in facilitating movement of workers in the Asia-Pacific region. While he argues that recent FTAs have increasingly promoted transnational movements, such as the immigration of medical employees to Japan, such initiatives and their associated regulations remain underdeveloped. Peter Volberding analyzes the implications of China's precipitous rise in demand for petroleum on East Asian security, arguing that the global reach of Chinese oil investments has exacerbated regional competition and has the potential to upset existing political power balances. Ivy Ngo examines the growing influence of Indonesia in regional and global affairs but notes that its underdeveloped infrastructure, diverse population, and unstable political environment have hampered its development. Cindy Hwang looks at China's stimulus package, emphasizing the role that economic crises play in reforming China's economy. Michelle Chang considers India's ostensibly contradictory trade policy of protectionism and free trade, ultimately concluding that its economic policy mirrors the complexities of the Indian economy.

Finally, in our **BASC Projects** update, Kristi Govella discusses our most recent endeavors, highlighting our three-year project, "The Transatlantic Relationship in a Post-Transatlantic World", which examines the rise of Russia, India and China, its effects on the international system, and the responses of the EU and the US. We held our first conference, "Responding to a Resurgent Russia", in April and are looking forward to our upcoming conferences on India and China in 2010 and 2011 respectively. We are also busy preparing for the publication of our next book, *The Evolution of East Asian Regionalism: Ideas, Interests, and Domestic Institutions*, and we have recently created a new alumni website and BASC blog to better connect our network.

The Berkeley APEC Center would like to thank all of the generous contributors who have made its projects possible, including the Ron and Stacy Gutfleish Foundation, the Center for Global Partnership (part of the Japan Foundation), the East-West Center in Honolulu, the East Asia Foundation, the Kim Dae-jung Presidential Library Foundation, the Institute of European Studies at Berkeley, the EU Center of Excellence, and the Institute of Slavic, East European and Eurasian Studies.

Vinod K. Aggarwal, Director, BASC

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Tel: (510) 643-1071
basc@berkeley.edu
<http://basc.berkeley.edu>

802 Barrows Hall #1970
University of California
Berkeley, CA 94720-1970

BASC Staff

Vinod K. Aggarwal
Director

Kristi Govella
Project Director

Tari Ellis
Business and Politics

Michelle Chang
Research Assistant

Ren Yi Hooi
Research Assistant

Ivy Ngo
Research Assistant

Cindy Hwang
Research Assistant

Peter Volberding
Research Assistant

APEC Update | A New Growth Paradigm

by Ren Yi Hooi
BASC Research Assistant

Under the theme “Sustaining Growth, Connecting the Region,” Singapore took the reins of APEC in 2009, working to promote economic growth, cooperation and investment across the Asia-Pacific region while positioning APEC’s 21 member economies for a sustainable recovery in the post-crisis world. As the APEC Economic Leaders’ Summit concluded on November 15th, leaders resolved to embark on an innovative, people-centered “New Growth Paradigm” while maintaining support of G20 goals. In addition to working together to enhance connectivity through trade liberalization and facilitating business within the region, APEC leaders brainstormed long-term growth strategies and discussed various issues including natural disaster mitigation, anti-corruption measures, the environment, and Burma.

Continuing APEC’s strong emphasis on trade liberalization, government leaders pledged to resist all forms of protectionism and accelerate the pace of negotiations to bring a conclusion to the Doha Round, while also continuing to explore the long-term goal of a Free Trade Area of the Asia-Pacific. Leaders decided to slash the cost of doing business in the region by 25 percent by 2015 through a range of practical “behind the border” and “at the border” strategies, including a pathfinder initiative to be led by Australia, Canada, Japan, Korea, New Zealand, Singapore, and the United States and the addressing of key chokepoints in the supply chain. However, despite an earlier call by finance ministers to maintain “market-oriented exchange rates,” the issue of currency rates was omitted from their final statement in light of US-China currency tensions.

While agreeing on traditional short-term growth tactics such as the continuation of stimulus spending in response to the financial crisis, APEC leaders resolved to pursue a balanced, inclusive and sustainable growth strategy that would be supported by innovation and a knowledge-based economy. Besides implementing structural reforms to gradually unwind global imbalances and raise the potential output of member economies, they also consulted with the APEC Business Advisory Council regarding ways to broaden access to economic opportunities and increase the resilience of the most vulnerable economies against economic shocks.

These measures include: helping small and medium enterprises and female entrepreneurs gain better access to global markets and finance; facilitating worker training; investing in education; and designing appropriate social safety nets. Despite their endorsement of policies to promote sustainable growth, however, leaders disappointed environmental advocates by omitting an earlier push for a 50 percent reduction in greenhouse gas emissions from the leaders’ final declaration, preferring to leave substantive deals to the Copenhagen conference next month.

In addition, APEC made efforts to strengthen institutional capacity in the areas of anti-corruption and disaster readiness. The Anti-Corruption & Transparency Symposium in Korea renewed the decision to combat corruption and improve transparency in the region, while the APEC Emergency Management CEO’s forum in Vietnam proposed investment policies and sought to improve coordination among APEC

members in the event of emergencies and natural disasters.

Finally, the summit also acted as a medium through which leaders attempted to engage thorny issues involving “difficult” countries on its sidelines. While the statement from the inaugural US-ASEAN Summit urged Burma to ensure fair, inclusive and transparent 2010 elections, US President Barack Obama met with Russian counterpart

Dmitry Medvedev on the sidelines of APEC to discuss Iran, which has yet to agree to a Russian offer to provide nuclear material for research in exchange for the closure of a nuclear reactor.

With the closure of this year’s summit marking the 20th Anniversary of APEC, which was founded in 1989, it is interesting to reflect on APEC’s current position and achievements to date. Despite APEC’s success in promoting regional trade and bridging its member nations over the last two decades, concerns continue to be raised with respect to its effectiveness and relevance, particularly in light of the new G-20 grouping created this year. Still, with the adoption of suitable strategies, APEC may be able to work in ways that are complementary to the G-20 and maintain its key role in the region. The two upcoming summits to be held in Japan and the United States present APEC with a good chance of sustaining and enhancing its current momentum, but only time will tell how successful its “New Growth Paradigm” will be.



APEC leaders met in Singapore on November 13-15, 2009.

BASC Projects | Another Exciting Year

by Kristi Govella
BASC Project Director

It's been a busy year at the Berkeley APEC Study Center! We are constantly striving to produce insightful new research on the Asia-Pacific region, and as we approach the end of 2009, we are very excited to share the latest news about our projects with you. We would like to highlight the following projects:

We are in the midst of conducting a three-year project entitled "The Transatlantic Relationship in a Post-Transatlantic World" with the support of the EU Center of Excellence. For the first time in a century, a set of large, populous and increasingly wealthy states—Russia, India, and China—are on the cusp of achieving great-power status. These powers are entering an international system still governed by a "Western" conception of order and based on the primacy of post-World War II rules, drawn from liberal models of capitalism and democracy practiced in the U.S. and in Western Europe. In this context, the most important and most uncertain question facing the West over the next decade is this: What will be the relationship between the EU and the US vis-à-vis these rising powers? Will the transatlantic relationship hold and become stronger, faced with this new geopolitical and geo-economic challenge? Or will the US and the EU—an increasingly prominent global player—compete for economic and political advantage?

We are tackling these difficult questions through a set of three conferences

focusing on Russia, India, and China respectively. On April 2, 2009, BASC co-sponsored the first conference, "Responding to a Resurgent Russia: Russian Policy and Responses from the EU and US", with the EU Center of Excellence and the Institute of Slavic, East European, and Eurasian Studies. We brought specialists from Europe and the US to Berkeley to discuss Russian perspectives on current international politics, the position of Russia in the global economy, and policy responses of the EU and US to Russia's rise. The papers from this conference are currently being developed into an edited book, which we expect to appear in print in late 2010.

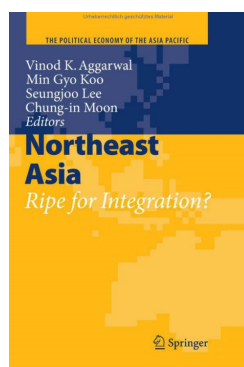
We are now making plans for the second conference, "Cooperation among Democracies? India, the U.S., and the EU", which will be held in Berkeley in April 2010. We will bring leading experts from India, Europe, and the US to discuss India's rise. This conference will be open to the public, and we invite any of you who might be in the Bay Area to attend. The final installment in our conference series, "Clash of Superpowers? Coping with China's 'Peaceful' Rise", will be held in April 2011. We will also be publishing the papers from these conferences in two separate edited volumes.

In addition, we are in the final stages of preparing our latest book for publication. *The Evolution of East Asian Regionalism: Ideas, Interests, and Domestic Institutions* is the result of two conferences held at UC Berkeley, which gathered regional and country experts to examine the interplay of domestic political

forces that lead countries such as Japan, China, Korea, Singapore, and the U.S. to pursue regional trade arrangements. This project attempts to open up the black box of each country's decision-making process by examining how contingent shocks and critical junctures have affected coalition politics among different veto holders within and outside the government. We show how subnational actors such as government agencies, business groups, labor unions, and NGOs engage in lobbying, both through their own governments and through their links to others in the region. In addition, we trace the evolution of interests and ideas over time, thus helping us to generate a better understanding of historical trends in the region based on changing preferences. This project was sponsored by a grant from the Kim Dae-jung Presidential Library and will culminate in the publication of an edited volume in late 2010.

Finally, the BASC website (<http://basc.berkeley.edu>) has recently been redesigned and now boasts a variety of new features, including an alumni website and the BASC blog. We encourage BASC alumni to update us with their latest achievements and to join our team of Research Assistants and our growing network by contributing to our new blog.

These are just a few of the many exciting things we have going on at BASC. Please check our website for the latest information about these and other projects. We thank our collaborators and sponsors for their continued support and look forward to the year to come!



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FTAs and Workers: Prospects for Freer Labor Markets in the Asia-Pacific

by Atsushi Yamada
Professor, Hitotsubashi University
Visiting Scholar, BASC

Free Trade Agreements are not only about freer trade. Today they encompass a wide range of issues such as the protection of intellectual property rights, the environment, investments, technological assistance, and more recently, the transnational movement of people (workers).

Two of the most recent FTAs signed by Japan, for example, include bilateral deals on the acceptance of some qualified workers from its neighbors in the Asia-Pacific. The Japan-Indonesia Economic Partnership Agreement, signed in 2007 and enacted in 2008, specifies that Japan will accept up to 1,000 nurses and care workers from Indonesia over two years. The first group of 208 Indonesians arrived in Japan during the summer of 2008 and, after six months of language training, started working in about 50 designated hospitals around the nation in January 2009. Similarly, in its FTA with the Philippines that came into effect in December 2008, Japan agreed to receive up to 1,000 nurses and care workers over two years. The first group of 283 arrived in May 2009.

Nations seek to promote movement of workers for the same reasons that they promote international trade in goods and services. FTAs allow nations to circumvent slow multilateral negotiations under the World Trade Organization, and to reach agreements with certain partners for mutual interests in less time-consuming ways. As part of their efforts to liberalize trade in services, WTO members have been discussing how to promote the transnational movement of persons, but the scope and duration of liberalization are quite limited, mostly consisting of intra-company transfers and temporary service providers. These

measures cannot satisfy Philippines and Indonesia, two of the world largest "exporters" of nursing personnel and eager to find their new markets. Japan, on the other hand, faces a rapidly aging society and is forced to consider supplementing its nursing staff. Broadly encompassing FTAs seem to provide the solution to the problems of these three countries.

True, the impact is still marginal. The several hundred newcomers from Indonesia and Philippines add very little to Japan's large pool of one million indigenous nurses. But this is a significant first step for larger change: Before those FTAs came into effect, Japan had less than 200 foreign-born registered medical staff.

Also, if similar FTAs expand among many nations to cover other professions and form a web of bilateral deals in the Asia-Pacific, they might help to generate freer labor markets in the region, at least in the long run. According to a recent study by Japan's Ministry of Economy, Trade and Industry (METI), more than a few existing FTAs have already incorporated provisions on the freer movement of people that go beyond those contained in the General Agreement on Trade in Services (GATS) under the WTO. These include FTAs such as: Japan-Thailand, Japan-Mexico, Australia-Thailand, Japan-Singapore, India-Singapore, Japan-Vietnam, and the ASEAN Free Trade Area (AFTA). Japanese trade officials anticipate that future FTA negotiations will entail a similar kind of provisions on workers.

But the road ahead is rocky. First, the transnational movement of workers tends to be one-way, unlike the two-way exchanges seen in trade in goods and services. The foremost concern of Japan (and perhaps many advanced economies) in FTA negotiations is promoting the export of industrial goods, not workers. Immigrants are most likely to flow

from the less-developed to the more-developed economies. If not mutual, deals will be hard, if not impossible, to negotiate. The Japanese government defined the agreements with Philippine and Indonesia as "exceptions" and is not yet ready to open Japan's labor markets.

Second, no clear international rules exist for the movement of people to be included in FTAs. With regard to trade in goods, under the WTO, each member of FTAs is required to eliminate tariffs on at least 90 per cent of its imports from the partner country within ten years. No such requirements exist regarding the movement of people. The ceiling of 1,000 was a politically set goal, a compromise made after the long, sometimes harsh, negotiations between the Japanese government and its Philippine and Indonesian counterparts.

Third, sending and hosting workers are fundamentally different from exporting and importing goods. Imported goods are to be consumed in importing countries, while immigrant workers are to be assured that their new lives in host countries will go on just as rewardingly as they expected. The lives of incoming nurses are still uncertain: even though they hold professional licenses in their home countries, Indonesian and Philippine nursing workers are defined as "candidates" in Japan and are required to take exams, all written in Japanese, within a certain period (three years for nurses and four years for care workers) if they wish to continue working as registered professionals. If they fail to pass the exam, they will be sent away.

So, are FTAs cruel to workers? Not necessarily. "I would like to work wherever I can," said one of the Indonesian nurses in a TV interview upon her arrival in Tokyo, "I'm glad [the FTA] paved the way." Now is the time to think about how to move forward and make FTAs better for workers.

China's Quest for Oil: Implications for East Asian Security

by Peter Volberding
BASC Research Assistant

Over the past three decades, China's rapid economic growth has necessitated a tantamount increase in its demand for energy supplies. Coal, China's most abundant natural resource, has historically served as the fuel of choice, and to this day, it continues to provide approximately 70 percent of China's domestic energy needs. However, the diversification of the Chinese economy away from coal-centric heavy industry and the increasing demand for personal automobiles by China's wealthier middle class has precipitated an enormous increase in the demand for petroleum. Throughout the 1970s and 1980s, China's domestic oil production was sufficient to meet the needs of its population, but in 1993, China became a net importer of crude oil. In 2004, China displaced Japan as the world's second largest importer of oil behind the US, and projections by the International Energy Agency forecast that China's import demand could outpace the U.S.'s by 2030.¹

While demand for petroleum can expand limitlessly, supply cannot. In order to secure ever scarcer petroleum supplies and maintain its robust economy, China has aggressively pursued bilateral relationships with petroleum-exporting countries around the globe as part of its "going out" strategy. China's national oil companies (NOCs), which are implicitly bankrolled by the nation's flush capital reserves, have invested billions of dollars in oil exploration, infrastructure construction, and oil extraction projects in Russia, Central Asia, Africa, and Latin America. Furthermore, as the deep and persistent recession continues to mire the industrialized world, China has taken advantage of the precipitous drop in global commodity prices to secure future oil supplies. However, in its quest for energy security, China has inevitably

challenged the historic prominence of the U.S. and Europe in the international oil market. The energy equation has become especially complex in East Asia, where regional political concerns and China's long-standing tensions with Japan have exacerbated competition and threatened regional security.

China has two broad components to its current energy strategy. First, China aims to expand and diversify its petroleum sources abroad. While concerted diplomatic efforts have been made to augment ties with the Middle East, China has emphasized Russia, Central Asia, Latin America, and Africa. Second, China seeks to protect the transport of oil. Around 75% of China's petroleum imports pass through the Strait of Malacca, reaffirming Chinese apprehension about future energy security. With these two goals in mind, China's international petroleum investments have burgeoned.

For example, in February 2009, China and Russia signed a \$25 billion oil-for-loan deal, whereby China agreed to supply two Russian oil firms with below market rate loans in exchange for 15 million tons of crude oil annually. Moreover, after fourteen years of negotiations, in April both China and Russia began construction of an oil pipeline between the Siberian city of Skovorodino and the Chinese city of Daqing, allowing the exchange to bypass volatile sea lanes. China's relationship with Kazakhstan is remarkably similar, as in April state-owned China National Petroleum Corporation (CNPC) agreed to a \$10 billion oil-for-loan deal. Three months later, both nations inaugurated the final section of China's first pipeline into oil-rich Central Asia. The creation of the Shanghai Cooperation Organization (SCO) in 2001, an intergovernmental security and economic cooperation association, has further solidified China's efforts in the region.

China's newfound interest in Latin

America has been heavily driven by the continent's plentiful natural resources as well, especially with regards to Brazil and Venezuela. In February 2009, Sinopec signed a \$10 billion infrastructure and oil exploration deal with the Brazilian state-owned petroleum company Petrobras in exchange for 200,000 barrels of oil per day. Similarly, on top of the \$12 billion allocated as a development fund, in September China agreed to provide \$16 billion in infrastructure assistance to develop Venezuela's lucrative Orinoco oil belt. In order to further cement political ties between China and Latin America, China has become an observer of the Organization of American States (OAS) and recently joined the Inter-American Development Bank (IDB) to increase investment opportunities.

In Africa, China has largely pursued a quid-pro-quo strategy of aid and infrastructure investment in exchange for oil supplies. Angola, for instance, has become China's largest oil supplier on the continent after a \$2 billion infrastructure loan package secured lucrative oil contracts, principally at the expense of Western corporations. Since then, China has successfully acquired similar contracts in Nigeria, Uganda, and Sudan, largely by sweetening the deal with large infrastructure projects like roads, bridges, stadiums, and even parliament buildings. In the past few months alone, China has bid for Nigerian oil blocks (rumored to be in excess of \$30 billion), and has expressed interest in Guinea (estimated at \$7 billion) and Ghana (approximately \$4 billion).

Despite the global reach of its investments, China's energy strategy has had an enormous impact on East Asian security concerns. First of all, China's worldwide investments directly compete with the US, oftentimes replacing American companies and institutions. By engaging with pariah states, such as Sudan and Iran, China has

¹ <http://www.iags.org/china.htm>

² <http://www.eai.nus.edu.sg/B329.pdf>

³ Thrassy Marketos, *China's Energy Geopolitics: The Shanghai Cooperation Organization and Central Asia* (Milton Park, Abingdon, Oxon: Routledge, 2009)

⁴ Michelle Chan-Fishel and Roxanne Lawson, "Quid Pro Quo? China's Investment-for-Resource Swaps in Africa," *Development* 50, no. 3 (2007): 63-68.

also undermined U.S. foreign policy objectives by providing an alternative to Western policies. However, the U.S. military presence around the Strait of Malacca, through which a majority of Chinese oil passes, and in East Asia generally, and China's lack of a blue-water navy has thus far tempered U.S. security concerns in the region. The military presence of the U.S. in East Asia has undoubtedly influenced China's decision to espouse a "peaceful rise," whereby China prefers to accept the status quo of power relations in the region rather than upset the existing political balance.

Second, Russia has increasingly come to distrust Chinese

2002 and recent joint exploration venture agreements, political skirmishes over territorial control frequently occur.

Finally, China's petroleum investments have most directly challenged Japan, which relies nearly completely on imported energy. The historic rivalry between Japan and China has driven contemporary competition for oil in East Asia, especially over pipeline construction in Russia and oil field development in Southeast Asia. However, Chinese NOCs have gained a competitive advantage with their government-backed financing, leaving Japan little option but to pursue similar tactics. For example, in order to ensure that Iran continued to export



A Chinese oil rig in the South China Sea. Photo courtesy of Siubing.

involvement in Central Asia, a region traditionally within the Russian sphere of influence. For example, the recently completed pipeline between China and Kazakhstan bypassed Russia entirely, raising Russian concerns that its regional hegemony is deteriorating. In fact, Russia only accepted the \$25 billion loan-for-oil deal with China out of economic necessity, as the sharp drop in global commodity prices drastically reduced the available capital for investment. Central Asia already faces numerous security concerns, and a battle for economic and political influence in the region by China and Russia could exacerbate tensions.

Third, China's growing interest in the Spratly Islands, located in heart of the South China Sea, has revived a long-standing territorial dispute between China, Vietnam, and the Philippines. Not only do the Spratlys contain a rich reserve of petroleum, but the islands are also strategically located along China's principal oil importation shipment route from Africa and the Middle East. Despite dispute resolution by ASEAN in

petroleum to Japan instead of China, Japan actively engaged with the pariah regime and

extended a multi-billion dollar credit line over the objections of the U.S. While armed conflict remains unlikely, persistent distrust could lead to reduced cooperation in other regional security matters.

China's meteoric economic rise has precipitated a critical need for energy supplies. In order to secure sufficient oil to sustain growth, China has relentlessly pursued investments around the globe. As a result, competition for an increasingly scarce resource has intensified regional rivalries and heightened regional insecurity. Regional organizations have responded with diplomatic initiatives to assuage differences. APEC, for example, has created an Energy Security Initiative to promote stable energy trade flows and increase regional economic integration. But as the world economy slowly improves and the demand for petroleum supplies once again increases, the stability of East Asian security will undoubtedly be tested.

⁵ Jean Garrison, *China and the Energy Equation in Asia: The Determinants of Policy Choice* (Boulder, Colo: FirstForumPress, 2009)

⁶ Jonathan A Czin, "Japanese Foreign Policy in the Middle East: Balancing Economy and Security," *Asian Security* 4, no. 2 (May 2008): 198-218

The Rise of Indonesia: A New BRIIC?

by Ivy Ngo
BASC Research Assistant

Indonesia is making waves on both economic and political fronts lately, proving itself to be one of the strongest players in ASEAN. With a population of 238 million people and a GDP that reached US\$433 billion in 2008, it is the fourth most populous nation in the world and the largest economy in Southeast Asia. Indonesia's stable situation is especially admirable given the relative newness of its democracy, which was put in place in 1998.

A number of developments have drawn positive attention to Indonesia of late. First, the Asian Development Bank recently upgraded Indonesian growth to 4.4 percent this year, with a predicted expansion to 5.4 percent in 2010, as economic recovery picks up. With a high rate of private consumption, 65 percent of GDP in 2008, Indonesia remains a promising market with potential for growth. A group of Indonesia business leaders have joined hands in the Vision Indonesia 2030 plan, hoping to raise per capita GDP to US\$18,300 by 2030 and add 300 Indonesian companies to the Fortune 500 list.

Second, Indonesia is expected to reap benefits from its relationship with US President Barack Obama. President Obama spent four years of his youth in Indonesia, and although he does not plan to visit Jakarta until next year, rumors of expanded trade and diplomatic relationships have begun to swirl.¹ In addition, Indonesia is poised for further development as a crucial leg of the 'Chindonesia' tripod: the 'growth triangle' of the Indonesia, China and India. As the world's largest palm oil exporter and second largest coal exporter, Indonesia has an important role in powering China and India. Bloomberg estimates that the three countries will provide \$10 trillion dollars of wealth for investors by 2015.

Third, there have been calls for the expansion of BRIC, the leading developing country bloc of Brazil, Russia, India and China, to include Indonesia – a new BRIIC. Advocates such as Morgan Stanley argue, convincingly, that Indonesia's significant potential and stable records of growth make it a serious contender. After all, Indonesia has higher per capita GDP than India and a higher urbanization rate (54 percent) than both China and India.

A number of important factors, however, keep Indonesia from fulfilling its potential. Indonesia's business climate is seen as unwelcoming to foreign direct investment due to protectionist measures and the overall instability of the rupiah. In addition, there are bureaucratic red tape, stringent labor laws, and blue-collar corruption. Despite the formation of the Corruption Eradication Commission (KPK), serious corruption problems remain widespread, and KPK's own officials have recently been accused of graft themselves.

Moreover, the persistent issue of weak physical infrastructure was cast in new light by the recent quake that left over 1,000 dead and the city of Padang flattened. Much of Indonesia is still traversed via dirt road over rough natural terrain and Indonesia continues to rely on a rusting system of ferries for transport between islands. Improving infrastructure, particularly transportation, will be a significant logistical challenge given the nation's 17,500 islands.

Indonesia's diversity compounds the problem of centralization post-Suharto. Separatist conflicts have largely been quelled, but national stability remains tense given the problems of religious fanaticism. Earlier in September, the leader of a fundamental Islamic militant group, Noordin Mohammed Top, was killed in Central Java. Despite Top's murder, the International Crisis Group believes that terrorism in Indonesia is not dead, and that the terrorist militants will probably regroup.

Lastly, there is the issue of human infrastructure and human capital. Indonesia's top university, the University of Indonesia, is ranked fifth in Southeast Asia and 34th in Asia but 201st in the world, according to The Times Higher Education-QS World University Ranking. Indonesia's workforce is young but needs higher standards of education if it is to be viable in the long-term.

With plenty of avenues for growth, Indonesia is currently the strongest member of ASEAN and has the potential to be a global contender. However, there are still many issues to be resolved before Indonesia can consider itself a dynamic enough economy to compete with the BRIC countries. With the re-election of President Susilo Bambang Yudhoyono earlier this year, there is hope that he can usher in the changes necessary to propel Indonesia's economic growth.

China's Stimulus Package: More Challenges Ahead

by Cindy Hwang
BASC Research Assistant

A year has passed since the dawn of the financial crisis, and China appears to be one of the few economies exhibiting confidence. The Chinese leadership has emerged from the global turmoil relatively unscathed, having successfully navigated through a number of politically sensitive anniversaries and with the promise of eight percent growth in sight. China's Keynesian

policies—a combination of stimulus, bank lending and export support—have resulted in increased government demand that has largely offset the downturn in domestic and foreign demand and helped to ensure continuing economic growth.

China's crisis management has been receiving mixed reactions from observers. Some China-watchers, initially skeptical of the effectiveness of the stimulus package, now warn of a future financial crisis fueled by investment driven asset-price inflation. Optimistic observers argue that rising asset

¹ Jason Tedjasukmana. "Indonesia Will Wait Longer for Obama" Time, October 9, 2009, <http://www.time.com/time/world/article/0,8599,1929377,00.html>

prices will help boost consumer spending. But four trillion RMB later, and despite Chinese leadership's repeated call to boost domestic consumption to shift away from export and investment driven growth, the fundamental problem of the structure of China's economic growth has remained unsolved.

The stimulus packages have stabilized China's economy from the shock of Wall Street's financial meltdown, but in order for China to generate growth internally to balance its interdependent economic relationship with the United States, considerable policy reforms are necessary. The non-state sector is the engine of economic growth in free-market economies. In China, it contributes to 60 percent of GDP, 70 percent of exports and 80 percent of employment, yet much of China's capital is allocated towards the less efficient, monopolistic state sector. Given the current discriminatory policies, more reform is needed to facilitate the entry and enhance the competitiveness of the non-state sector for the Chinese economy to shift towards consumption driven growth.

At this point, it is unrealistic to expect China's recovery

to spur global consumption. Most Chinese are still too poor to constitute a sizable market for foreign goods; the growth in China's total factor productivity has not been followed by equal growth in labor wages. And the lack of protection for intellectual property and the opaque and arbitrary bureaucracy mean that the cost of doing business in China is much higher than elsewhere in the world for indigenous entrepreneurs. Continuing economic reform therefore must be accompanied with some reform in China's governance structure.

Historically, crises like this have provided the Chinese government the opportunity and political will to push through reforms; a decade earlier, the Asian financial crisis has led to the liberalization of policies towards China's private sector. The current crisis has taught the Chinese leadership that, in order to lessen the external impact on China's economy, China must undertake decisive reforms to ensure the healthy growth of domestic consumption. Thus, despite continuing uncertainties, we have reasons to remain optimistic.

India: Fragility and Strength as Seen through its Trade Policies

by Michelle Chang
BASC Research Assistant

At the recent G-20 meeting in Pittsburgh, one of India's top priorities was to warn against protectionism and non-tariff barriers by developed countries. This should not be surprising. Between August 2008 and August 2009, Indian exports had dropped 20 percent due to sinking demand from major markets like the US and the EU, and export-dependent countries like India and China will suffer even more if developed countries take protectionist measures to revive their own domestic economies. Recently, India has tried to counter these measures by pursuing various free trade initiatives. In August, the country signed an FTA on goods with ASEAN countries, and it has already moved on to pursue an FTA with ASEAN on services as well. India is eager to gain access to South Asian markets like those of Malaysia and Singapore in which a sizeable English-speaking population offers many opportunities for Indian professionals.

On the other hand, however, India is still seen by many as a notorious protectionist. Indeed, India's tariffs are on the higher end among countries, it frequently uses anti-dumping measures, and it is still one of the very few countries that ban foreign investment in retail. Most notably, in January this year India imposed a temporary ban on imports of Chinese toys, making India's warnings against protectionism at the January G-20 meeting seem rather hypocritical.

How, then, in light of India's often contradictory trade policies, should we comprehend India's current stance on trade? This question is increasingly important as the world emerges from the worst financial crisis since the Great Depression.

One may begin by observing that the Indian economy has remained relatively steady through the global financial crisis, although it has suffered from falling exports and withdrawal of

much foreign investment. That the two developing economies of India and China have passed through the crisis relatively intact has led to the general consensus that they will gain much importance and recognition in the aftermath of the crisis. But it is precisely India's relative economic isolation and its protectionist measures that have shielded it from much of the damage of the crisis.

At the same time, the new initiatives taken by India in trade and other important issues can be seen as signs of the growing strength of its economy. Besides actively initiating free trade deals with countries like Thailand, India has also changed its tone on climate issues. Once reluctant to comply with the global fight against climate change, India has recently proposed to set limits on its own carbon emissions. India is taking these initiatives beyond mere economic issues because its growing economic strength allows it to compromise certain short-run economic benefits and look farther into the future. It is also because India recognizes that becoming a major power means looking beyond the scope of the economy and to take initiatives in other areas of global concern.

Therefore, be it protectionist measures or free trade initiatives, India's often contradictory trade policies can be interpreted as indicators of its economic strength. On the one hand, the protectionism India fears from developed countries and the protectionism it uses to envelope its own economy demonstrate the vulnerability of a developing economy. On the other hand, India is opening up to free trade and taking initiatives in climate change as a result of its growing prowess. When seen in this light, India's contradictory trade policies do not seem so contradictory after all. They are manifestations of both the fragility and the vigor of a growing economy that is conflicted by nature—an economy that is struggling to maintain balance but has the will and potential to take on the world.

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commercial interests, or the number of non-discriminatory or liberalizing sectors.

Global Trade Alert also contains records of state measures that have been announced but not yet implemented. Here this is potentially important because, although the measures implemented from November 2008 to September 2009 may have been skewed towards a minority of sectors, this may not be the case for the measures pending implementation. In Figure 4.2 for each CPC sector, the number of pending measures is plotted against those already implemented. The two series are positively correlated (in fact, the correlation coefficient is 0.4), suggesting that those sectors that have been subject to plenty of state intervention in the recent past will continue to do so in the near term. The skewed nature of intervention, then, appears for the moment to be an important feature of crisis-era state intervention.

It is also possible to identify which sectors have been affected by the state measures under-taken during the crisis. Table 4.2 presents information on those sectors where 10 or more state measures have almost certainly discriminated against foreign commercial interests. Other than the financial services sector, where bailouts and other forms of financial assistance have been offered extensively, most sectors where discriminatory measures have been undertaken are not typically associated with “growth poles” or “green growth.”

In fact, many of the sectors where contemporary discrimination against foreign commercial interests is rife are sectors that tended to receive higher levels of trade protection before the onset of the global economic crisis. Three agricultural sectors, basic metals, textile and apparel and basic chemicals are all in the list of the top 10 sectors where discrimination against foreign commercial interests has occurred the most. In terms of state intervention in general (not just measures that discriminate against foreign commercial interests), six similar sectors, basic metals, textile and apparel and basic chemicals are all in the list of the top 10 sectors where discrimination against foreign commercial interests has occurred the most. In terms of state intervention in general (not just measures that discriminate against foreign commercial interests), six similar sectors are in the corresponding top 10 sector. In the light of these findings it is tempting to discount claims that the pattern of state intervention during the crisis is particularly different from before.

Keeping in mind the caveats detailed in the introduction, the findings here suggest that perhaps little has changed in the factors determining the cross-sectoral variation in state intervention. That so many relatively highly protected sectors before the crisis have been affected by state measures taken during the crisis points to defensive considerations playing

an important role in influencing policymaking, an observation not inconsistent with the first and third rationales discussed in Section 2.

At least in terms of the number of state measures implemented, the results presented here call into question the importance that

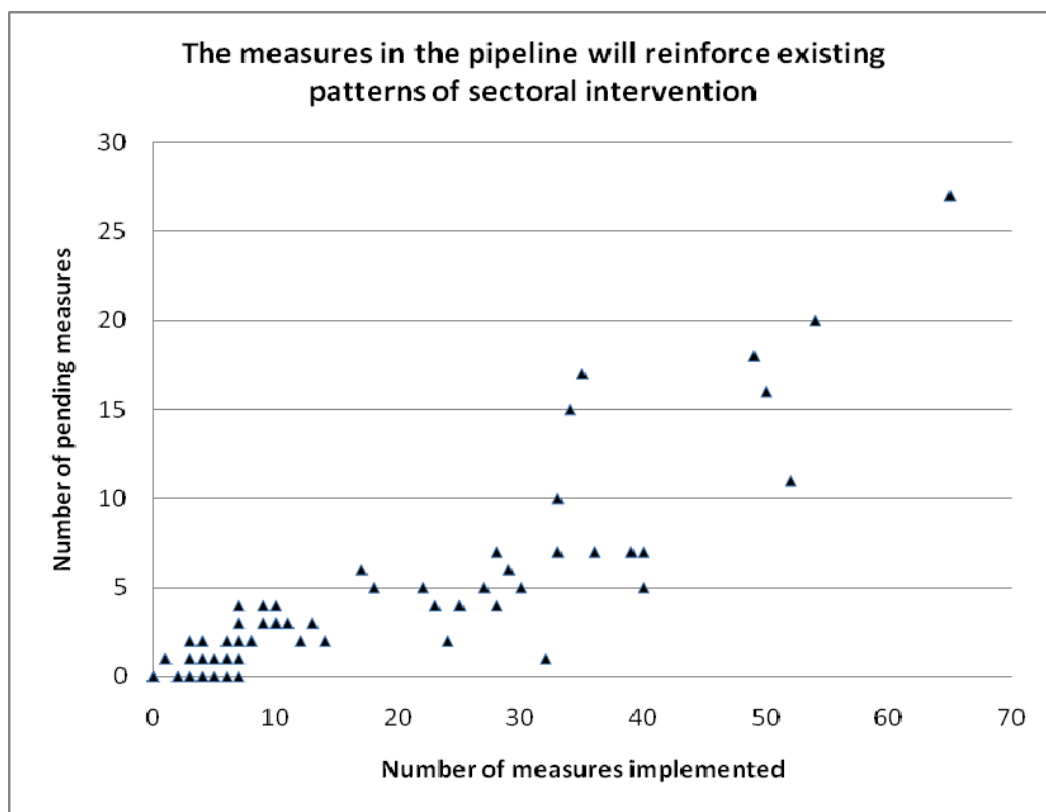


Figure 4.2. No change is expected in the likely distribution of state intervention.

has been publicly attached to promoting economic growth and promoting certain environmentally-friendly outcomes. This is not to say that the latter goals are unimportant or without value, nor does it imply that no measures have pursued these objectives. Rather, the prominence given to rhetoric concerning promoting long-term growth, innovation, and green growth poles may not be reflected in terms of the distribution of projects being undertaken on the ground.

Abridged from “Have Long-Established Patterns of Protectionism Changed During this Crisis: A Sectoral Perspective”, in Simon J. Evenett, ed., *Broken Promises: a G20 Summit Report by Global Trade Alert* (London: CEPR, 2009).

Vinod K. Aggarwal is Professor of Political Science at the University of California, Berkeley, and Director of the Berkeley Asia Pacific Economic Cooperation Study Center (BASC).

Simon J. Evenett is Professor of International Trade and Economic Development, University of St. Gallen, Co-Director of the International Trade and Regional Economics Programme, CEPR, and Coordinator of Global Trade Alert.

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Table 4.1. Table of sectors affected by 10 or more almost certainly discriminatory state measures (coded Red in the GTA database).

Affected Sector: CPC code (sector description)	Total no. of measures in GTA database	(Green) Measures	(Amber) Measures	(Red) Measures	Implemented measures	Pending measures	Number of jurisdictions implementing measures affecting specified sector and classified as red
81 (Financial intermediation services and auxiliary services)	32	1	2	29	31	1	13
21 (Meat, fish, fruit, vegetables, oils and fats)	40	2	13	25	35	5	16
44 (Special purpose machinery)	52	7	20	25	41	11	16
01 (Products of agriculture, horticulture and market gardening)	40	4	14	22	33	7	17
23 (Grain mill products, starches; other food products)	39	3	14	22	32	7	40
41 (Basic metals)	65	7	36	22	38	27	38
27 (Textile articles other than apparel)	36	4	13	19	29	7	13
34 (Basic chemicals)	54	7	28	19	34	20	12
42 (Fabricated metal products, except machinery/equipment)	49	4	26	19	31	18	13
49 (Transport equipment)	50	7	24	19	34	16	13
38 (Furniture; other transportable goods n.e.c.)	30	2	10	18	25	5	13
47 (Radio, television and communication equipment)	29	2	9	18	23	6	10
22 (Dairy products)	27	1	9	17	22	5	40
28 (Knitted or crocheted fabrics; wearing apparel)	28	3	8	17	24	4	12
43 (General purpose machinery)	33	4	12	17	26	7	11
02 (Live animals and animal products)	25	2	7	16	21	4	41
29 (Leather and leather products; footwear)	24	3	6	15	22	2	11
36 (Rubber and plastics products)	28	3	10	15	21	7	13
46 (Electrical machinery and apparatus)	23	2	7	14	19	4	10
26 (Yarn and thread; woven and tufted textile fabrics)	33	6	15	12	23	10	9
37 (Glass; glass products; other non-metallic products n.e.c.)	34	4	18	12	19	15	11
39 (Wastes or scraps)	25	5	8	12	21	4	11
31 (Products of wood, cork, straw and plaiting materials)	18	1	7	10	13	5	8
35 (Other chemical products; man-made fibres)	35	7	18	10	18	17	9
Total for sectors mentioned above	849	91	334	424	635	214	
Total for all sectors	1136	135	428	573	849	287	

Source: *Global Trade Alert* database, www.globaltradealert.org, data extracted 15 September 2009.