East Asia and the EU: The Unavoidable Partnership
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Message from the Executive Director

Asia-Europe Institute, University of Malaya (AEI-UM) is the realization of Malaysia’s commitment to the Inaugural Asia-Europe Meeting (ASEM) Summit held in Bangkok in March 1996. The Asia-Europe Centre (AEC) was consequently established at the University of Malaya on 1 December 1997. The commitment of AEC is to promote and enhance linkages in higher education between Asia and Europe. In January 2000, AEC transformed into what is now known as the Asia-Europe Institute (AEI). The current aim of AEI is to enhance the cooperation between Asia and Europe in the field of higher education. In this view, I am delighted to introduce you to the inaugural edition of *AEI Insights: The International Journal of Asia-Europe Relations*. Hence, *AEI Insights* has been established as an annual, peer reviewed journal in order to contribute further to the achievement of the abovementioned objectives. It is our sincere intent at AEI that this publication will facilitate the promotion of findings resulting from collaborative research within academia as well as government and private sector institutions.

The collaboration of knowledge regarding Asia-Europe relations and the discourses connected to this issue shall be extended through this publication. This journal occupies an important area in this dialogue and opens up new opportunities to members of this conversational community to expand understanding through research. The establishment of this academic resource also serves as a foundational source of shared concepts, complementary plans for research, as well as support for the social sciences and humanities to catalogue the progress of the relationship between Asia and Europe.

This inaugural edition of *AEI Insights* features a selection of eight scholars that contribute timeless and critical points to the issue of international relations. A contemporary global positioning is introduced through the view of antiquity with Dr Pekka Korhonen providing historical cartographic accounts of conceptual, political, and geographical foundations of where the ideas of Asia, Africa, and Europe originated to help with a greater understanding of the direction ASEM may take. Dr Mi Park illuminates the growing assertiveness of China with regard to bilateral trade relations with the European Union and what future geo-political implications this may have for the world economy. Professor Dr Ansgar Belke and Associate Professor Dr Ulrich Volz share a view of the European Central Bank and its approach to maintaining the Euro’s position against other international currencies. Dr Carina Ren and Matias Thuen Jørgensen show the expansive trend of Chinese tourism and the response from a Scandinavian perspective. Professor Dr Fumitaka Furuoka addresses the continuing development of China’s currency entering into a role of significant influence within new patterns of East Asian regionalism. Dr Ramon Pacheco Pardo concludes this selection by providing a view of the direction that relations and regional dialogues between East Asia and the European Union may be taking currently.

These selections provide voices from current conversations within relationally regional spectrums, but more importantly impart themes consistent with the scholarly motivations of AEI. As AEI continues to provide a venue for intellectual discourse on globalization, regionalization, and inter-regional relations between Asia and Europe, this inaugural issue enables the expansion of that venue for widening this area of discourse. So too is the Socio-Cultural Pillar of the ASEM Process given further promotion by inviting more scholars to create new dialogues on the relations between Asia and Europe. As such, *AEI Insights* will continue to promote and advance findings.
resulting from collaborative and inter-disciplinary research to help future academics and leaders in this region not only face the rapid changes of this world, but shape and guide these changes.

It is through this publication that thanks are given to the authors that have contributed to the inaugural edition of *AEI Insights: The International Journal of Asia-Europe Relations* and I look forward to future submissions to the journal.

Associate Professor Dr Md Nasrudin Md Akhir  
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Abstract
The bilateral relationship between East Asia and the EU is yet to develop to the same extent that US relations with each of them has. In an international system characterised by the prevalence of transnational threats to international security and the increase in number and growth in number of international institutions, East Asia–EU bilateral relations are becoming an unavoidable partnership. Indeed, relations between East Asia and the EU are becoming increasingly institutionalised as a result of shared interests, sufficient resources and expertise, the development of regional governance in each of them, and interactions at the global level. The case studies of the counter-proliferation of weapons of mass destruction and financial governance regimes show the extent to which these four elements are drawing East Asia and the EU closer to each other. Nonetheless, these two case studies concurrently exemplify the shortcomings of a relationship yet to fulfil its potential. Developing a new, well-functioning region-to-region dialogue only including East Asia and the EU would serve to create a framework for the unavoidable partnership to strengthen.

Keywords
East Asia; EU; partnership; counter-proliferation; finance

Introduction
The relationship between East Asia and the EU is often characterised as the weakest link in the East Asia–US–EU strategic triangle. Certainly, links between both of them cannot compete in terms of depth or breadth with their respective bilateral relationships with the US. Yet, as the economic and politico-diplomatic importance of the East Asia–US–EU triangle intensifies, relations between them are becoming increasingly relevant to global dynamics. It seems that East Asia and the EU are moving towards an unavoidable partnership.

Two central characteristics of the current international system underpin the inevitability of cooperation between East Asia and the EU. To begin with, most current threats to international stability are transnational in nature. The incidence of inter-state war has declined dramatically since the end of the Cold War (Tertrais, 2012). For the most part, tensions between states do not lead to confrontations beyond diplomatic spats and—sometimes—short-lived economic retaliation. Meanwhile, issues such as the proliferation of weapons of mass destruction (WMD), financial
crises, climate change, human trafficking or piracy affect a large number of countries. Globalization has weakened borders to the extent that no country is exempt from these inter-state issues.

In addition, the current international system is characterized by a surge in the number of international organisations and—more importantly—their growing relevance to the coordination of global governance. International organisations (IOs) proliferated following the end of World War II (Raustiala, 2012). Nonetheless, Cold War enmity between the Soviet Union and the US severely constrained the work of these IOs for decades. This situation changed following the disintegration of the Soviet Union. Since the early 1990s, many IOs have become more effective discussion forums and decision-making bodies with real power. Certainly, this power still rests upon sovereign states agreeing to implement the decisions taken by IOs. Yet, there is evidence that states are likely to follow through on the commitments made within these organisations (Hurd, 1999). At the very least, IOs serve to bring together officials and experts from different countries. This enhances knowledge-sharing and the diffusion of acceptable behavioural norms.

As a result of the trans-national nature of threats to international security and the proliferation and growing effectiveness of IOs, interactions among East Asian and European policy-makers, officials and civil society representatives have been growing. This has been helped by the launch of the Asia–Europe Meeting (ASEM) and related initiatives from the mid-1990s onwards. It can be argued that links between countries and societies in East Asia and Europe have never been stronger. This underpins the relationship between two regions which together account for over half of the world’s GDP.

In this article, I analyse the extent to which a strong Euro–East Asian relationship has become unavoidable. In order to make this argument, I first provide a historical overview of relations between East Asia and the EU up to the present time. I then present two case studies to highlight the extent to which both actors have areas of common concern—one security issue followed by one economic issue. These are counter-proliferation of WMD and financial governance. In the concluding section I will explore the potential for bilateral cooperation as well as the implications for global governance of a strengthened partnership between East Asia and the EU.

**East Asia–EU relations: Historical overview**

When writing about East Asia, it is first necessary to define the meaning of this term. For the purpose of this article, East Asia is defined as ASEAN+3—that is, ASEAN, China, Japan and South Korea. These countries are forging a regional economic community—especially in the area of financial governance, one of the case studies used in this article. In addition, the thirteen countries have recently started to cooperate in the area of security through the ASEAN Defence Ministers’ Meeting-Plus (ADMM-Plus). Launched in 2010, ADMM-Plus only includes ASEAN+3 countries as its East Asian representatives. Thus, it can be argued that ASEAN+3 is starting to foster a security community.

The history of East Asia’s relations with the EU can be split into four distinct periods. The first period would encompass from the creation of the EEC in 1957 until 1975. During this period, the EU had a set of bilateral relations with like-minded countries in East Asia. Like-minded countries included those with a market economy and aligned with the US, regardless of whether they had democratic or authoritarian political systems. Thus, the EU formalised diplomatic relations with Japan in 1959, with South Korea in 1963, and with US allies in Southeast Asia throughout the
1950s and 1960s. Relations with countries from the communist bloc were limited to formal contacts within international institutions.

EU–East Asia relations during this period were therefore driven by ideological affinity and, to an extent, economic interest, with EU member states providing economic aid to US allies in East Asia and developing commercial relations with Japan as it became wealthier (Frattolillo, 2013). Washington’s set of security alliances in both regions also guided relations between East Asia and the EU. Nevertheless, security dynamics were different between an East Asia characterised by tri-polarity and an EU at the centre of American-Soviet bipolarity. Bilateralism based on ideology and economics, therefore, were the drivers of East Asian–EU relations until 1975.

The second period in East Asia–EU relations would run from the establishment of diplomatic relations between China and the EU in 1975 to the launch of the Asia–Europe Meeting (ASEM) in 1996. This period was marked by the normalisation of diplomatic relations between the EU and countries in the region and a strengthening of economic links (Frattolillo, 2013). Brussels started to open up to communist countries as Cold War rivalries subdued and intra-Southeast Asian relations improved—most notably with the expansion of ASEAN throughout the 1990s to eventually include all of its current members. Meanwhile, trade and investment flows expanded as more East Asian countries moved beyond low income status and formerly communist countries started market reforms.

Concurrently, interregionalism emerged as a defining characteristic of relations between East Asia and the EU. In 1977, ASEAN and the EU established a dialogue, reinforced in 1980 with the signing of a Cooperation Agreement (ASEAN Secretariat, 2014). The culmination of this interregionalism process would be the launch of ASEM in 1996. At the time, ASEM was seen as the forum that would bring closer East Asia–EU relations (Camroux & Lechervy, 1996). Bilateral relations were not abandoned, however. Japan and the EU established a bilateral head of government summit in 1991, with China and the EU launching a political dialogue in 1994. Diplomatic normalization and economic interests therefore drove relations between Brussels and East Asian countries throughout this period. Washington’s set of security alliances in the region became less relevant to EU policy. As the European Commission’s *Towards A New Asia Strategy* argued, the economic development of the region called for European business to invest and the EU to provide aid (European Commission, 1994). Thus, incipient interregionalism and bilateralism built upon improving political links and economics guided East Asia–EU relations throughout this period.

A third, shorter period in East Asia–EU relations began in 1996, finishing in 2007 with the advent of the Global Financial Crisis (GFC). This period was marked by the strengthening of Sino–European relations, a boom in economic links, and a move away from interregionalism. In 2003, China and the EU signed Brussels’ first-ever, formal strategic partnership (Scott, 2007). As such, it realigned East Asia–EU relations, since the latter prioritised one specific relationship over the rest. A multitude of bilateral sectorial dialogues would give shape to this partnership. With regards to East Asia as a whole, bilateral economic relations became stronger year-on-year. Trade and investment flows in both directions grew, and EU aid to less developed East Asian countries remained significant. The strengthening of bilateral links was to an extent the result

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1 See European External Action Service (2014a).
2 See ibid.
of the failure of the ASEAN–EU Cooperation Agreement and ASEM to drive East Asia–EU relations. Most notably, discussion on an ASEAN–EU free trade agreement (FTA) faltered due to Brussels’ refusal to include Myanmar (Weatherbee, 2009). As for ASEM, the addition of new countries from outside East Asia and disinterest both in the EU and East Asia seem to have made this forum decreasingly relevant.

Economic interests and a move towards bilateralism therefore were the main forces behind East Asia–EU relations during this third period. The influence of the US on this relationship waned, and hard security matters had minimum influence on it—if any. The European Commission’s *Europe and Asia: A Strategic Framework for Enhanced Partnerships*, published in 2001, informed these developments on the EU’s side (European Commission, 2001). The difficulties for interregionalism to produce practical results reinforced these dynamics.

The fourth and current period in East Asia–EU relations began with the GFC and its aftermath. This is a period defined by the strengthening of bilateral political and economic relations and the beginning of meaningful cooperation in global governance regimes. With regards to bilateral relations, progress since 2007 has been very quick. Most notably, South Korea–EU relations produced head of government annual summits from 2009 and a Strategic Partnership, an FTA, and a Framework Agreement in 2010. Meanwhile, China and the EU established high level strategic and economic and trade dialogues in 2007. As for Japan–EU relations, they moved forward more slowly, but in 2013 negotiations for a Strategic Partnership and an FTA were launched. Finally, six ASEAN countries—Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam—are either negotiating or having exploratory contacts with the EU to sign bilateral FTAs, and several ASEAN members are discussing Partnership & Cooperation agreements—which Indonesia already signed in 2009.

With regards to global governance regimes, East Asian countries have become more prominent in them, thus boosting the possibility of cooperation. This is particularly the case for China, Indonesia, Japan and South Korea, the region’s four members in the G20. Singapore has also become a more relevant actor in economic and financial regimes (Davies & Green, 2008). With the rise of multi-layered governance—in which global, regional and bilateral layers affect each other—and the strengthening of regionalism in East Asia and the EU, the two of them are poised to interact more often with each other in global governance regimes. Bilateral relations between Brussels and particular East Asian countries would support these regimes. This is already happening in areas including climate change, aviation or the two case studies in this article—counter-proliferation of WMD and finance.

**East Asia and the EU in the counter-proliferation of WMD regime**

Proliferation of WMD is a top concern for most states around the world. The European Security Strategy (ESS) issued in 2003 highlighted proliferation as “potentially the greatest threat” to the security of the EU (European Council, 2003). Brussels sees multilateral cooperation in international institutions as one of the means to address this threat (European Council, 2003). Similarly, the Chairman’s Statement published following the first-ever ADMM-Plus summit in 2010 identified

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3 See European External Action Service (2014e).
4 See European External Action Service (2014c).
6 See European External Action Service (2014b).
proliferation a one of several security threats “beyond the scope of any country to handle alone” (ASEAN Secretariat, 2010). Thus, both East Asia and the EU see proliferation of WMD as an important security issue requiring multilateral cooperation to address.

**Counter-proliferation of WMD regime: main institutions**

Arguably, the counter-proliferation of WMD regime is one of the most successful security regimes ever created, especially in the area of nuclear weapons. The cornerstone in this area is the Treaty on the Non-Proliferation of Nuclear Weapons (NPT). Opened for signature in 1968, it entered into force in 1970 and was extended permanently in 1995 (United Nations Office for Disarmament Affairs [UNODA], 2014a). Its three pillars include non-proliferation, disarmament, and peaceful use of nuclear energy. The treaty has almost-universal membership and from 1975 onwards NPT Review Conferences have been held every five years (UNODA, 2014a) This has allowed the regime to adapt to the evolving threat of proliferation and thus remain relevant. Since the NPT entered into force, “only” three countries have become nuclear powers—India, North Korea and Pakistan. Along with newly independent South Sudan, these are the only countries that are not parties to the treaty. For the most part, proliferation of nuclear weapons has been very limited (Cirincione, Wolfsthal, & Rajkumar, 2005), which points out the success of the NPT.

Another anchor of the counter-proliferation regime is the International Atomic Energy Agency (IAEA). Established in 1957, the IAEA is entrusted with assisting in the peaceful use of nuclear energy, developing high standards for nuclear safety, and verifying the peaceful use of nuclear materials and facilities (International Atomic Energy Agency [IAEA], 2014). Similarly to the NPT, this IO has almost universal membership. Besides some small countries, island states and South Sudan, the only notable exception is North Korea—it withdrew from the organisation in 1994.

Other WMD covered by counter-proliferation treaties are biological and chemical weapons. Both have almost-universal membership—26 countries are not part of the Biological Weapons Convention (BWC), including Myanmar, and only six are not members of the Chemical Weapons Convention (CWC), including, Myanmar again and North Korea. Both conventions aim at prohibiting the development, production, and stockpiling of the respective types of weapons that they cover, with the CWC also prohibiting their use. The BWC and CWC seek the destruction of the weapons that they refer to as well. Proliferation of biological and chemical weapons has been limited throughout the existence of these two treaties (Cirincione, Wolfsthal, & Rajkumar, 2005), indicating their success.

Notwithstanding the accomplishments of the nuclear, biological and chemical weapons treaties and related institutions, the George W. Bush administration launched the Proliferation Security Initiative (PSI) in 2003. Established as a result of the perceived inefficiencies of existing counter-proliferation mechanisms, the PSI introduced interdiction of WMD as one of the principles of the counter-proliferation regime (The White House, 2003). With slightly over 70 participants, membership is far from universal. Nonetheless, all EU member states and nine East Asian countries are part of the initiative (U.S. Department of State [USDOS], 2014b). Despite the secrecy of its operations, it seems that the PSI has reduced proliferation activities (Valencia, 2005).

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2. Ibid.
East Asia in the counter-proliferation regime

A conflict involving the use of WMD in East Asia is extremely unlikely. Nonetheless, East Asian countries are concerned about the possibility of proliferation of WMD from and inside the region. These concerns focus around two countries. The main worry is North Korea, a well-known proliferator and the only country ever to have withdrawn from the NPT (Winters, 2005). Indeed, the PSI was to a large extent established to stop Pyongyang’s proliferation activities (Bolton, 2007). Even though it is very unlikely that North Korea will use WMD itself, its proliferation of nuclear technology materials and know-how are considered a serious threat by most if not all East Asian countries.

A second—if smaller—concern is Myanmar. Uniquely for the region, this country is not a party to the BWC or the CWC, as already stated. Arguably more worryingly for other East Asian countries, Myanmar received WMD-related technology from North Korea as recently as 2010 (Rublee, 2014). Even though the country’s government has launched an economic and political opening up process, there is no indication that it has given up its WMD programme. Located between China, India and other Southeast Asian countries, Myanmar has long been strategically important. This exacerbates the concerns that other East Asian countries have regarding its WMD-related activities.

In order to deal with these proliferation concerns, East Asian countries have for the most part relied on intra-regional IOs. In the case of the North Korean issue, the four-party talks of 1997–99 and the six-party talks launched in 2003 and discontinued in 2009 have been the main counter-proliferation initiatives (Pacheco Pardo, 2014). The talks are necessary insofar, as above-mentioned, Pyongyang is not part of the NPT or the IAEA. The six-party talks—the most recent consistent initiative to deal with North Korea’s nuclear programme—focused on denuclearisation in exchange for a number of inducements, including economic and energy support as well as normalisation of diplomatic relations with the US and Japan (Pacheco Pardo, 2014). Thus, East Asian countries have been willing to accommodate North Korean demands to address proliferation of WMD even if Pyongyang is in non-compliance with the international nuclear non-proliferation regime.

In the case of Myanmar, ASEAN’s principle of non-interference in domestic affairs limits the range of possibilities for East Asian countries to deal with its proliferation-related activities (Roberts, 2010). Therefore, there have been no North Korea-style talks to address this issue, nor has it been dealt with through the ADMM-Plus. Nevertheless, concurrently to its opening up process, Naypyidaw has publicly stated that military links with Pyongyang have ceased (Selth, 2011). However, the broader issue of its WMD-related activities remains unaddressed at the regional level.

Meanwhile, there are similarities but also an important difference among East Asian countries in the way that they approach counter-proliferation. East Asia is a keen supporter of multilateral institutions in the areas of nuclear, biological and chemical weapons non-proliferation. Thus, East Asian countries contribute to meetings and initiatives related to the NPT, BWC and CWC. Some of them, such as Japan and South Korea, seem to be more active. But all of them are relatively involved, depending on their resources.

The main divide separating East Asia into two groups pertains to the PSI. Brunei, Cambodia, Japan, Malaysia, the Philippines, Singapore, South Korea, Thailand and Vietnam are all part of the

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9 Ibid.
10 Ibid.
initiative (USDOS, 2014b), while China, Indonesia, Lao and Myanmar are not. Therefore, there are nine countries in the region that have decided to be involved in the interdiction of WMD. Japan, Singapore and South Korea have been especially active in the PSI, hosting military exercises and meetings (USDOS, 2014a). Since the PSI technically breaches the principle of non-intervention in domestic affairs, participation in the PSI clearly shows which countries are more concerned with countering proliferation of WMD.

The EU in the counter-proliferation regime

Proliferation of WMD is a top concern for the EU, as highlighted in the ESS. Differently from the case of East Asia, this worry does not relate to countries within the region. In the case of the EU, it is in relation to the Middle East and terrorist networks. In the case of the Middle East, there is real fear among EU countries about the possibility of countries in its neighbourhood acquiring nuclear weapons (European Council, 2003). This would increase instability in an already unstable region. The main concern is Iran. Hence, France, Germany, the UK (or the EU-3 as they are known) and the EU itself have held talks with Tehran regarding its nuclear programme since 2003 (Pacheco Pardo, 2011). Iran’s nuclear programme, however, is not the only country of concern. Egypt, Syria and Libya—during Muammar Gaddafi’s regime—are known to have received WMD from North Korea (Rublee, 2014).

A second important fear for the EU in the area of WMD proliferation relates to the threat that terrorist groups might acquire them (European Council, 2003). A clear example is Hezbollah’s links to the North Korean regime and the possibility that it might have acquired weapons from Pyongyang (Pollack, 2011). Terrorism remains a threat throughout many parts of the EU (Europol, 2013). Even though WMD are yet to be used by terrorist groups targeting Western objectives, the fear that they might acquire them persists.

At the EU level, several official documents underpin Brussels’ counter-proliferation policy. The most relevant are ‘Basic principles for an EU strategy against proliferation of weapons of mass destruction’, ‘Mainstreaming non-proliferation policies in the EU’s wider relations with third world countries’, both issued in 2003, and ‘Council common position on the universalisation and reinforcement of multilateral agreements in the field of non-proliferation of weapons of mass destruction’, published in 2005 (Pacheco Pardo, 2011). At the EU level, these and related documents lay out a policy based on information sharing and capacity-building. Equally relevant, the EU presents a common position in international institutions. A clear example was the common position that the EU drew for the 2010 NPT Review Conference (Pacheco Pardo, 2011). Furthermore, Brussels has a number of bilateral programmes and dialogues with selected partners to increase safety standards or even decommission WMD-related materials (Pacheco Pardo, 2011).

At the global level, the EU has been one of the most active actors in this area. Brussels is very actively involved in IAEA and other IOs, making proposals and working on strengthening implementation mechanisms (Kienzle & Vestergaard, 2013). Member states are also very active in the UN, most notably in the drafting of sanctions on countries which are proliferation concerns—especially Iran and North Korea. France and the UK are very involved in this area as a result of their permanent membership of the UN Security Council (Kienzle & Vestergaard, 2013).

Meanwhile, the EU and all its member states are part of the PSI, as already noted. EU countries have been amongst the most actively involved in PSI initiatives. France, Germany, Italy, Spain
and the UK have been especially supportive of the initiative, for example (Durkalec, 2012). Furthermore, Poland has been very dynamic in the coordination of PSI meetings and infrastructure (Durkalec, 2012). Also, EU member states account for 10 of the 21 members of the PSI coordination body—the Operational Experts Group (Pacheco Pardo, 2011). In summary, the PSI would not exist without EU ideological and material support.

4. East Asia and the EU in the financial governance regime

From the onset of the re-emergence of financial openness in the 1970s, financial crises resumed (Reinhart & Rogoff, 2009). Crises became very common throughout the 1980s and 1990s, when entire regions—including East Asia—and different countries everywhere around the world suffered them (Reinhart & Rogoff, 2009). Finally, the recent GFC and Eurozone Sovereign Debt Crisis (ESDC) have shown that financial crises can hit several regions at the same time and affect highly developed countries. Having suffered one of the biggest crises prior to the GFC, East Asia is well aware of the risks inherent to financial openness. Indeed, the 1997 crisis was the main catalyst for ASEAN+3 cooperation (Emmers & Ravenhill, 2011). In the case of the EU, the ESDC has led to the creation of its first-ever regional financial safety net in the form of the European Stability Mechanism (ESM) (Fabbrini, 2013). Financial governance to prevent and manage crises is therefore a central concern to both East Asia and the EU.

Financial governance regime: main institutions

Financial governance is an area in which reaction to crises has shaped the institutional framework. Following the GFC, the G20 has become the main IO to guide financial governance (Cooper, 2010). However, G20 meetings are not convened as often as it would be required for such a complex issue. As a result, most of the practical work in the area of financial governance is carried out by a set of expert-led institutions. The Financial Stability Board (FSB) —launched in 1999 but given new impetus in 2009 as a result of the GFC—is directly linked to the G20 as its main agenda-setting and coordination body (Financial Stability Board [FSB], 2014c). Central bankers, ministers of finance and regulators make up the FSB.

Banking, securities and insurance are the main areas covered by financial governance. Of these three, banking is the area with a better-developed framework. Created in 1930, the Bank for International Settlements has become the host of different banking regulation IOs and initiatives (Toniolo, 2005). The most relevant of these IOs is the Basel Committee for Banking Supervision (BCBS). Created in 1975, the BCBS is the main rule-making, information sharing and monitoring institution in the area of finance (Tarullo, 2008). Crisis prevention and management, liquidity provision, and financial market strengthening are its main goals.

The most important instrument to achieve these goals is the Basel III Accord. Entering into force in 2013, this accord replaced the Basel II Accord of 2004, which in turn replaced the Basel I Accord of 1988. The fact that a third accord was signed reflects the inadequacy of the previous two. The Basel III Accord establishes minimum capital requirements for international banks, a supervisory review process, and market discipline (Bank for International Settlements, 2014). Importantly, the 2013 accord covers banks from many countries that were not covered by the previous two—including several countries in East Asia.
In the areas of securities and insurance, the International Organisation of Securities Commission (IOSCO) and the International Association of Insurance Supervisors (IAIS) were created in 1975 and 1994, respectively. Neither of them were as active as the BCBS prior to the GFC. However, this crisis has empowered them (FSB, 2014b). Their main goals are information sharing and international standards promotion.

Finally, another IO involved in financial governance is the International Monetary Fund (IMF). Its main function is liquidity provision to countries suffering from a liquidity crisis. Nevertheless, the stringent conditionality attached to its loans has made the IMF very unpopular, to the extent that during the 2000s it ran the risk of becoming almost obsolete (Buira, 2005). It was revived during the GFC and, especially, the ESDC. However, its role became secondary to that of other actors who asked the IMF to contribute to rescue packages rather than to lead them. The creation of other liquidity provision mechanisms such as the New Development Bank launched by the BRICS in 2014 or regional initiatives—of which more below—have diminished the role of the IMF.

East Asia in the financial governance regime

The 1997 financial crisis that struck East Asia affected all countries in the region—most notably Indonesia, Malaysia, South Korea and Thailand. The causes and behaviour of the IMF during the crisis were the main drivers of subsequent approaches to financial governance by countries in the region. With regards to the causes explaining the crisis, the two main immediate ones were a sudden withdrawal of foreign capital and the collapse in the value of local currencies (Wade, 1998). The withdrawal of foreign capital could not be addressed through the use of central bank reserves, which helps to explain their huge increase since then (Aizenman & Lee, 2008). As for the collapse in the value of local currencies, it led to the inability by many private companies to repay dollar-denominated debt instruments. (Wade, 1998) The launch of Asian Bond Markets Initiative (ABMI)—a regional initiative—was the direct effect to this problem.

Without recourse to other sources of capital, Indonesia, South Korea and Thailand resorted to IMF bailout packages. These packages, however, came with stringent conditions attached. For many, these conditions exacerbated the effects of the crisis (Haggard, 2000). As the IMF later admitted, the conditions should have focused “on the problems at hand” rather than trying to deal with other issues (International Monetary Fund [IMF], 2013). Avoiding reliance on the IMF has been an important driver of East Asia’s financial regionalism since the 1997 crisis.

Regional financial governance is well developed in East Asia. Liquidity provision, directly related to the just-discussed role of the IMF in aggravating the 1997 crisis, is one of the areas in which regional governance is well established. Launched in 2003, the Chiang Mai Initiative was multilateralised in 2010. The Chiang Mai Initiative Multilateralisation (CMIM) pools together the financial resources of ASEAN+3 countries. All of them can borrow from the CMIM if suffering from liquidity problems (Kim & Yang, 2014). Even though only 40% of the borrowed capital is de-linked from the IMF, this IO would have limited power to impose its conditions when providing capital to an East Asian country (Kim & Yang, 2014). Furthermore, the ASEAN+3 Macroeconomic Research Office (AMRO), created in 2011, has a monitoring function designed to prevent liquidity crises (Kim & Yang, 2014). AMRO should eventually become an IO independent from ASEAN+3 countries.
Meanwhile, East Asia has also launched the ABMI and the Credit Guarantee and Investment Facility (CGIF), in 2003 and 2010 respectively, to boost the supply of local currency denominated bonds (Kim & Yang, 2014). Thanks to ABMI and CGIF guarantees, East Asian countries and companies are able to borrow in their local currency. This way, fluctuations in the value of the local currency against the dollar has a more limited effect on the ability of countries and companies to repay their debts.

At the global level, the most important contribution by East Asia has been to the G20/FSB and the BCBS. China, Indonesia, Japan and South Korea are permanent members of the G20, with ASEAN being regularly invited to meetings (Cooper, 2010). The four countries plus Singapore—and Hong Kong—are members of the FSB (FSB, 2014a). Thus, there are up to five East Asian countries plus ASEAN and Hong Kong regularly involved in shaping the framework underpinning global financial governance.

In the case of the BCBS, China, Indonesia, Japan, Singapore and South Korea—plus Hong Kong—are all members. However, China and South Korea (Bank for International Settlements [BIS], 2009b) only became members in March 2009, followed by Indonesia, Singapore and Hong Kong in June of that same year (BIS, 2009a). As a result, East Asia—with the exception of Japan—was not involved in crafting the Basel I and II accords. Differently, East Asian countries contributed to the crafting of the Basel III Accord. In any case, East Asia has only recently been part of the process whereby financial governance rules are set.

The EU in the financial governance regime

The GFC and subsequent ESDC were a shock to the EU. Before them, there was a widely-held belief that financial crises had been eradicated from developed countries, since none had suffered a major crisis for almost twenty years (Reinhart & Rogoff, 2009). Given that the major effects of these two crises were felt by several countries in the recently created Eurozone suffering from capital flight—most notably Greece, Ireland, Portugal and Spain—the main response from the EU focused on avoiding both contagion and another crisis. Therefore, liquidity provision to countries suffering from capital shortfalls was the main preoccupation for the EU.

At the regional level, the European Financial Stability Facility and the European Financial Stability Mechanism were agreed upon in 2010. They provided capital to Eurozone countries suffering from liquidity problems (Fabbrini, 2013). In 2012, the ESM was launched as a permanent IO to provide such liquidity in the future and this way ensure rapid resolution of crises while also avoiding their spread to other countries (Fabbrini, 2013).

There are discussions in Brussels regarding creation of a banking union in the Eurozone which would also be open to other EU member states. The union would include a Single Supervisory Mechanism, launched in November 2014, and a future Single Resolution Mechanism (European Commission, 2014). If successfully and fully implemented, a banking union would enhance financial governance in the EU—or at least in the Eurozone—by regionalising management of the banking sector, thus increasing transparency.

At the global level, France, Germany, Italy and the UK—plus the EU itself—are part of the G20 (Cooper, 2010). The four countries plus the Netherlands and Spain are also part of the FSB (FSB,
Similarly to their East Asian counterparts, membership of these institutions makes these six countries and the EU central to the establishment of guiding principles for financial governance. The role of the EU is arguably more important in the BCBS. Belgium, France, Germany, Italy, Luxembourg, the Netherlands, Spain, Sweden and the UK are all part of the committee (BIS, 2009a). Together with the US, EU member states were the main drivers behind global financial governance since the creation of this institution. Most notably, the Basel I Accord was essentially created by the G10—which included Belgium, France, Germany, Italy, the Netherlands, Sweden and the UK (Posner, 2009). This accord lay out the basis of the capital adequacy requirements principle that still governs global financial governance in the area of banking. Equally relevant, the Basel II Accord was basically the result of negotiations between the US and the EU (Posner, 2009). Supervisory review process and market discipline were added to the principles underpinning the regulation of the banking sector in this accord. Thus, even though other countries contributed to the Basel III Accord during the negotiation phase, the principles were already laid out in previous accords.

Potential cooperation between East Asia and the EU

East Asia and the EU share their concerns in different areas. Counter-proliferation of WMD and financial governance—the former a security issue, the latter an economic matter—are two examples of these. They prove that there are similarities and some differences in the ways in which East Asia and the EU feel vulnerable to them, as well as in terms of their approach to dealing with transnational threats. They also show that there are some differences within East Asia. Nonetheless, similarities seem to outnumber differences (see table 1). This suggests that there is great potential for East Asia and the EU to cooperate in the resolution of these and other trans-national threats.

Table 1. East Asia and the EU in the counter-proliferation of WMD and financial governance regimes

<table>
<thead>
<tr>
<th>Regime</th>
<th>East Asia</th>
<th>EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>Counter-proliferation of WMD</td>
<td>Threats: - Intra-regional states: North Korea &amp; Myanmar</td>
<td>Threats: - Neighbourhood: Middle East</td>
</tr>
<tr>
<td></td>
<td>Responses: - Regional institutions: Six-Party Talks (not universal) &amp; ADMM-Plus</td>
<td>- EU-wide policies</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Participation in global institutions: NPT/IAEA, BWC, CWC &amp; PSI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Divisions regarding participation in all global institutions: universal in NPT/IAEA but not universal in BWC, CWC &amp; PSI</td>
</tr>
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<td></td>
<td>- IMF intervention?</td>
<td>- Crisis contagion</td>
</tr>
<tr>
<td></td>
<td>Responses: - Regional institutions: liquidity provision &amp; local currency denominated bond market development</td>
<td>- Regional institutions: liquidity provision &amp; Eurozone banking union</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Participation in global institutions (not universal)</td>
</tr>
</tbody>
</table>
Considering the similarities between East Asia and the EU in terms of their approaches to security and economic governance, it is possible to infer different opportunities for region-to-region cooperation. These include capacity-building, monitoring, and regime development at the global level. East Asia and the EU have the necessary human and economic resources to make these happen. The institutional framework, however, is still in the process of developing.

With regards to capacity-building, the 1990s model was based on East Asian “learning” from the EU (Jetschke & Murray, 2012). This model is now obsolete, if it ever existed. Not only are the integration processes in East Asia and the EU different, but this model implied that East Asia had to follow on a blueprint set up by Brussels. However, capacity building based on mutual learning and best-practice sharing is a distinct and workable possibility which should be considered.

Taking the case of counter-proliferation of WMD, China, Japan and South Korea have participated in the Six-Party Talks, and China, the EU-3 and the EU itself are taking part in discussions about Iran’s nuclear programme. The possibilities for East Asia and the EU to share their experiences and link the two issues—as the US has tentatively suggested—are clear. Since both East Asia and the EU agree on the broad goal of eventually reversing the nuclear programmes of North Korea and Iran, sharing their experiences would be a win-win situation.

Moving beyond specific issues, East Asia and the EU can engage in capacity building by examining their distinct experiences at the regional level. ADDM-Plus and EU-wide cooperation are different approaches to counter-proliferation which nonetheless can serve for East Asia and the EU to learn from each other. Brussels can share its knowledge on trust-building and the necessary bargaining process involved in joint policy-making. For their part, East Asian countries can share their experience in trying to accommodate the presence of outside powers—including the US and Russia—that might be able to contribute to intraregional discussions.

In fact, financial governance is an area in which East Asia’s and the EU’s regional IOs have already started mutual capacity-building. The directors of AMRO and the ESM are in regular contact, and their officials interact in global institutions. Even though cooperation between both may seem logical, it is not always the case that regional institutions support each other.

Monitoring is a second possibility for East Asia and the EU to cooperate. More specifically, the sharing of information collected through monitoring activities. Indeed, the sharing of some information already takes place within global institutions and at the EU-East Asia country bilateral level. Nevertheless, the sharing of information collected through monitoring could be institutionalised. Most notably, proliferation of WMD from North Korea to the Middle East is perceived as a threat both in East Asia and the EU. However, there is no region-to-region framework for information to be regularly exchanged.

The case of financial data monitoring also shows the unfulfilled potential for cooperation. Given the interconnectedness of financial systems across regions and the fact that there is an overlap between the end of the business day in East Asia and its beginning in the EU, information sharing through the G20/FSB and the BIS/BCBS should be supplemented by a region-to-region mechanism. Since, for example, regular contacts between AMRO and the ESM already exist, it would be possible to institutionalise them and create a more permanent institution.

Author’s interview with AMRO official, Singapore, 26 September 2013.
Arguably, governance regime development at the global level is the area in which cooperation between East Asia and the EU would be easiest to implement. To begin with, both of them are already members of global governance institutions—or at least some countries in each of them are in the case of financial governance. Furthermore, several East Asian and EU countries have an active role in multilateral institutions. Therefore, they could build on existing cooperation to help to further develop global governance regimes.

This further development could be based upon two pillars. To begin with, a working region-to-region dialogue in which to come up with new proposals. For example, since both East Asia and the EU are or have been involved in dealing with countries of proliferation concern and have suffered from financial crises, their similar experiences would be useful to discuss negotiation and prevention mechanisms, respectively, at the global level. A second pillar would be taking a leading role in the creation of well-functioning monitoring mechanisms at the global level. The IAEA and the BCBS already have monitoring responsibilities in the areas of nuclear proliferation and finance, respectively. However, as the cases of North Korea, Iran or financial crises show, these have not worked properly.

Ultimately, cooperation between East Asia and the EU in the areas of capacity-building, monitoring, and regime development at the global level need an institutional framework to work properly. ASEM has proved unable to play such a role. The presence of too many members and disinterest on the part of East Asia and the EU explains this inability. Bilateral dialogues between the EU and specific East Asian countries, meanwhile, are very valuable and should not be discontinued. Nonetheless, they create a fragmented framework without an overarching structure.

Development of an East Asia–EU dialogue would solve the limitations currently imposed by the inadequate ASEM and bilateral frameworks. ASEAN+3 is evermore institutionalised; since the Lisbon Treaty entered into force in December 2009, the EU is moving towards a truly common foreign and security policy in many areas. Therefore, it is not an overstretch to think that East Asia and the EU could have a region-to-region dialogue on which to base EU–East Asia country bilateral relations.

Meeting on a regular basis, the region-to-region dialogue could serve as the structure for multiple sectorial, lower-level dialogues to take place. This is the framework on which the EU–China and EU–South Korea relationships are based. A region-to-region dialogue would be a cost-effective means for East Asia and the EU to discuss issues on which broad agreements exist. Issues requiring deeper discussions could still be dealt with at the bilateral level.

The unavoidable partnership

Transnational threats and the growing number and importance of IOs underpin the increasing importance of global governance regimes. These regimes include multiple layers. As the cases of counter-proliferation of WMD and financial governance show, East Asia and the EU are two regions in which the regional layer is well-developed. They are also two regions actively involved in the global layer.

The above explains why East Asia and the EU would need to establish well-functioning region-to-region cooperation. Creating an institutionalised region-to-region dialogue would be an important

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step in this direction. Such a dialogue would provide the structure for East Asia and the EU to engage in capacity-building, monitoring, and regime development at the global level. A region-to-region dialogue would still allow for bilateral dialogues to exist.

It seems clear that the relationship between East Asia and the EU can be characterised as an unavoidable partnership. Shared threats and interests, sufficient expertise and resources, and regular interactions already underscore existing and possible cooperation between both. Transforming this cooperation into a partnership seems a logical next step.

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Getting “China Ready”. Challenging static and practice based configurations of the Chinese tourist

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Abstract

Lately, the Scandinavian tourism sector has identified the Chinese market as attractive, but difficultly accessible. As a consequence, initiatives have been undertaken in order to make Scandinavia ‘China ready’. In this article, we use an extensive literature review, an example of such an initiative and a range of interviews with practitioners engaged in Chinese-directed tourism in Denmark to demonstrate how the Chinese tourist is configured by different stakeholders in tourism. We discuss how culture is usually deployed in making sense of tourists and show how mostly quantitative methods are used, often in combination with cultural notions of difference, to represent the tourist Other, in this case the Chinese tourist. We show how two opposing configurations of the Chinese tourists emerges. Where one is static and based on cultural difference, the other takes a practice-based perspective, seeing the Chinese tourist as ‘just another customer’. The article points to a third affinity based approach, which enables us to see beyond perceived differences and to focus on meeting grounds where local qualities and characteristics are developed to suit a Chinese market. This abstains from reducing people into stale and stereotypical representations and takes an important step towards getting truly ‘China ready’.

Keywords

China; tourism; culture; configuration; affinity

We in the West have an odd way of looking eastward. It is odd because it is at the very latest a late-19th century way of seeing. The Asia in our minds resembles a disassembled machine. It is long on data (the lowest form of knowledge) and short, very short, on understanding (the highest form of knowledge).

(P. Smith, 2010)
Introduction

Chinese outbound tourism is currently experiencing tremendous growth, globally as well as in Europe. As a consequence of this growth, the Scandinavian tourism sector has identified the Chinese market as an attractive, but also difficultly accessible future market. In public discourse and the media, where the Chinese tourism market has received sizeable attention, this difficulty for Scandinavia to ‘connect with’ the Chinese market is most often explained as rooted in language barriers and cultural differences. As a consequence of these felt barriers in catering to the Chinese market, a number of initiatives has been undertaken in order to make Scandinavia ‘China ready’. In this article, we use an extensive literature review, an example of such an initiative and a range of interviews with tourism stakeholders engaged in Chinese-directed tourism in Denmark to demonstrate how the Chinese tourist is configured by different stakeholders in tourism. To do so, we start out with discussing how culture is usually deployed in representing tourists and destinations. We also show how mostly quantitative methods are used, often in combination with cultural notions of difference, to represent the tourist Other, in this case the Chinese tourist. After introducing our own methodology and data collection process, we turn to the analytical part in which we draw on collected data from what we identify as three prominent stakeholder groups involved in developing tourism for Chinese tourists: tourism researchers, public destination management organizations (DMOs), and tourism practitioners.

In our first analysis, we introduce and discuss the current literature on Chinese outbound tourism, which show how primarily quantitative data impacts our abilities to see beyond the confines of numbers and difference. Through the literature review, we also display how a heavy focus is put on ‘China’ (and all that is Chinese and different) rather than on ‘getting ready’. This approach is subsequently pursued into a tourism development program entitled Chinavia used to exemplify how initiatives led by Scandinavian DMOs often rest on a specific set of assumptions about Chinese tourists. In the case of Chinavia, we see how Chinese directed tourism has been primarily concerned with, 1) gathering data about Chinese tourists and 2) has focused extensively on the Chinese tourist as different. As seen in the above quote, this approach to the “Eastern Other” offers some quite restricted possibilities of engaging with or understanding, in this case, the Chinese tourist, since, as we argue, initial data is often collected on the basis of assumptions and hypotheses, which may in turn be based on prejudice and/or the objects of research that seem most obvious, which in many cases are the cultural differences.

As opposed to these two examples of how China readiness is addressed in Scandinavia by conceptualising the Chinese tourist as radically different and generating data through not very context sensitive representations, we offer a third example, namely that of the practitioner. Drawing on interviews with practitioners, we show how these do not conceptualise or engage with the Chinese tourist as Chinese, but rather as customers. Cultural differences seem to play a less important role and catering directly to them is considered as a way to accommodate, rather than necessities based on actual needs. Also, many practitioners seem to be more concerned with the way of travel (group versus independent travelers), than with the nationality of the traveler. Drawing on these two ways of engaging with the Chinese tourists—one as radically different and one as practice-based, we show that the challenge to attract Chinese tourists is perceived quite differently in tourism research, by DMOs and with practitioners. We argue that static representations of otherness and a ‘culturally bare’ practice-oriented approach could be replaced with a stronger empirical and analytical focus on affinities rather than strangeness in the work of developing destinations to become ‘China ready’.
Configuring the Chinese tourist

How does one come to perceive and engage with those who we see as being different from us? In the context of tourism, this question is relevant not only in regard to the encounters which take place between hosts and guests (Smith, 1989), but also in relation to how tourism as a business and product is developed and marketed. What we have chosen to call the configuration of the Other following the work of Said, 1979 is intrinsically linked to how we seek to attract them to a specific city, region or country by developing and marketing them as attractive destinations. On a smaller scale, it is also connected to the wish of the tourism company to strike an attractive balance between strangeness and familiarity in order to best reach customers, which are per definition from ‘out of town’. In the present case, the Other encompasses ‘the Chinese tourist’, which we will further describe is under substantial interest and scrutiny in tourism management and research. We argue that the configuration of the Chinese tourist herein generally takes place through two interrelated approaches, one of culture and one of research. In the following, this double-sided configuration is elaborated upon as are our theoretical considerations as to how and why such approaches must be if not avoided, then at least supported by other types of configurations.

Configuring the Chinese tourist through culture

Until very recently, management-oriented tourism research as well as tourism management have been dominated by a predominantly static conceptualization of culture. A dominant understanding of culture easily found in tourism research, management and marketing is that of culture as difference. This is not so strange, as one could say that a very essential part of travelling is the search for strangeness, exotic experiences, otherness or even encountering “the Other”(Cohen, 1972). This understanding of other cultures as implicitly different is well founded in anthropological tradition, where anthropologists would venture to distant and exotic places. An important task was to map out the entire world in different cultures. With an overall objective of distinguishing “us” from “them”, an essentialist agenda of difference is reproduced in tourism. Its view of culture is supported and reproduced by countless tourism brochures, travel books, and other materials promoting tourist destinations. In this process, differences in culture are not only conceptualised as disparate in time as well as in space, but also as static and incommensurable.

As a challenge to seeing the tourist other as strictly different from ‘us’, we introduce a competing notion of culture in this article, that of culture as practice. This concept does not aim at negating or dismissing the idea of culture as difference, as it is as first noted inherent to tourism. It does however work against a static understanding of how cultural differences may be grasped and managed in real tourism situations, in this case in seeking to configure the Chinese tourist. As shown through the different examples presented in greater depth below, the implicit understanding of culture as difference recurs in both research and tourism development, where culture is reduced to a number of collective and mutually exclusive entities and addressed as an identifiable and manageable entity of static and incommensurable Otherness.

In this article, we suggest taking a more dynamic approach to culture, seeing the tourism encounter not as potentially problematic encounters—or even clashes (Smith, 1989) - between homogenous and incommensurable cultures but rather as dynamic platforms in which differences are not played out, but rather created, contested, evened out and bridged in relational practices. Through such an approach, we wish to encourage the investigation and reflection of how culture works in the tourism encounter, what constructs and changes it and how it is negotiated and put to use to face
challenges in tourism. We do so, as we believe that an understanding of cultural practices and complexities are important and necessary skills in managing tourism but also, in a broader sense, in improving cultural relations and communication between Asia and Europe.

Configuring the Chinese tourist through research

Following the idea of the incoming tourist as Other or culturally different, marketers and managers have often resorted to quantitative data collection and to segmentation in order to cluster and manage its potential customers. As we shall later see, this has been no exception in the case of Chinese incoming tourists. Such an exercise consists in dividing and labelling tourists according to pre-existing categories, typically revolved around age, gender, nationality, income, schooling, motivation etc. Only slowly has management oriented tourism research begun to resort to other research tools than those strictly quantitative but as shown in more detail in the literature review below, much of the (little) qualitative research existing in the field has been analysed, somewhat instrumentally, through methods that involves, segmenting, clustering or in other ways that aims to make qualitative data measurable.

Drawing on insight from the work of Law (1994, 2004) and Mol (1999, 2002) and the larger body of work of Actor-Network Theory (Latour, 2005; Law & Hassard, 1999), we argue in this paper how methods deployed to research and investigate tourist demographics and motivations are not ‘innocent’, but are active partakers in constructing tourists and tourism realities (Ren, 2011) in certain ways rather than others. As we argue in this article, the ways in which we develop our categories and carry out segmentation based on tourist representations are often based on a priori notions about what to research and the categories by which to do so. However, as Law warns us, we must not see representations, i.e. the direct description, as ever becoming one-to-one with the things they seek or claim to represent (Law, 2004). Although claiming status as “institutions of authority” (Law, 2004, p. 89) and as literal depictions of reality, representations are never direct, but always mediated.

The process of representing through segmentation, for instance, is seen as an outcome of a specific way of creating and distributing knowledge about Chinese tourists. In segment-based representation for instance, they become graspable through a reduction in which they ‘are’ their age, gender, educational background or nationality. Following Woolgar (1990), we see the mediated outcomes of researching, categorising and subsequently representing and engaging with the Chinese tourist as an act of configuration, which “occurs in a context where knowledge and expertise about users [or in this case, the Chinese tourist, eds.] is socially distributed.” (p. 59). In that sense, methods and the configurations which they produce are highly performative as they shape reality and our understanding of it. In the case of researching the Chinese tourist, the configuration of the Chinese tourists takes place through a process of validation in which (mostly) quantifiable tools are deployed as mediators.

Configuring the Chinese tourist: a relational approach

Differentiating, categorising and segmenting Chinese tourists are useful and efficient ways to make sense out of a more complex and heterogeneous reality. However, as we have sought to show, they also impact the ways in which we make sense of and get involved with reality and in this present case, how the tourist Other is perceived and engaged with. In this article, we seek to pursue and illustrate these ideas further by means of three examples, in which the Chinese tourist
is represented and hence, made present as a specific ontological figure (what Mol (2002) terms as enacted into being). These examples are that of tourism research, that of a tourism development scheme and that of tourism practitioners working with Chinese tourists. Through a close and critical qualitative investigation of these examples, we show how the Chinese tourist is configured as homogenous and radically different.

As opposed to a ‘segmentation-oriented’ approach, we then seek to discuss how other methodologies and views upon culture as something other than mere differences may shed light on the complexity and multiple features of ‘the Chinese tourist’. This challenges ‘the Chinese tourist’ as a taken for granted, a priori category and showing it rather as emerging and ever-changing through relational processes which connect different entities and activities of tourists, researchers and practitioners (Ren, Pritchard, & Morgan, 2010). Hereby, we hope to show how characteristics or actions connected to the Chinese tourist are not innate or fixed, but are rather relationally constructed. As such, they emerge as the effects, rather than the pre-given basis, of social relations.

As we will illustrate and discuss further on, qualitative enquiries into how differences are produced and which differences come to matter in the practical field of working with and handling Chinese tourists may in fact be used to strengthen our interrogations into and our analytical understanding of how the other is constructed. As we show, it may also lead us from merely collecting data through the use of taken for granted categories and segmentation models to more dynamic, practice-sensitive methods of enquiry which do not only focus on extrapolating difference between Western tourism stakeholders and their Chinese market. Hence, by not taking culturally engrained differences or motivations as an ‘obvious’ starting point, theory and practice can be combined in productive ways, as we will later show.

Methodology

In this article, we make use of a qualitative approach in order to describe and discuss how the Chinese is configured by researchers, DMOs and practitioners. The research configurations are identified and discussed based on a review of existing literature on Chinese tourism to Europe. In order to show how Scandinavian DMOs conceptualise the Chinese tourist, we draw on material and own participation in Chinavia, a collaborative project on tourism research and development, while the views of practitioners are drawn from qualitative interviews. We will give a more in-depth account for the latter two in the following.

The case of Chinavia

"A must-win battle for Scandinavia”. This quote about Chinese tourism was used as an introduction to the project of Chinavia along with others such as: “... [the] outbound travel market is growing exponentially while Europe’s economy and consumption are stagnating.” “middle class is on the rise”; “the travel industry’s number one growth segment.”; “rapid development and huge potential”; “European cities across the continent have seen an average of two digit annual growth rates”; “middle class is already larger than the entire US population”; “expected to overtake the US as the world’s largest economy”; “average of 25 million first-time (...) travellers per year – or 70.000 every day.”. Chinavia was developed as a Scandinavian cooperation project and managed by the DMO of Wonderful Copenhagen in cooperation with three Scandinavian project partners, Göteborg & co, Stockholm Visitors Board and Helsinki Tourism & Congress Bureau. According
to the project holders, the project was initiated as an answer to the huge potential witnessed by the above quotes:

“... the project was initiated in acknowledgement of the rapid growth in Chinese bed nights and huge potential of the travel industry’s number one growth segment, yet also as a consequence of the relatively small share of Chinese bed nights in Scandinavian cities as compared to other European city destinations.” (Chinavia website, n.d.).

Beginning in 2012, the project was managed according to a three-track project design involving a research track, a strategy track and a funding track. The purpose of the first track was to gain more knowledge about the Chinese tourists, and culminated with the delivery of a Research Package, including a total of five reports that sought to contribute to a more comprehensive understanding of the Chinese outbound travel market. This package was meant to probe a larger, strategic roll-out and to lay the groundwork for the Chinavia II project, which is currently running, with the aim of developing China-ready Scandinavian destinations. The primary data from the project used in this article are four of the five reports delivered as the result of the research track (more information on these reports will be provided in the analysis).

The idea for this article came as a consequence of the authors’ participation in a conference and workshop as part of the Chinavia II project. The way that the Chinese tourist was presented and configured at these events, combined with existing knowledge of literature on Chinese outbound tourism and previous work with Danish nation branding endeavours in China (Ren & Gyimóthy, 2013; Ren & Ooi, 2013), spawned a number of questions regarding the Chinese tourist as Other. These concerned how and in what ways our cultural perceptions of Chinese tourists and our representation of them through certain research methods contribute to configure the Chinese as something particular. Also, our questions revolved around how such ‘research driven’ configurations were related to those of practitioners. Because of this specific context, our own role as presenters and participants in the conference and workshop and thus in the Chinavia project also form a source of data, that must be taken into account when reading the article.

**Qualitative interviews with practitioners**

For the study, 10 explorative, qualitative, semi-structured interviews with representatives of tourism practitioners in Denmark were conducted. The companies included three, four and five star hotels in Copenhagen, as 83% of the Chinese bed nights in Denmark are in Copenhagen (Wonderful Copenhagen 2011) and since Chinese tourists generally prefer to stay in three to five star hotels (Xie & Miao, 2009, p. 239; Becken, 2003, p. 2). They also included attractions in Copenhagen and Odense since these are the main destinations for attractions for Chinese tourists, who often take one day trips to Odense (Visit Denmark interview; Scandinavian Tourist Board 2012). Also, one flight carrier was included because of their main role in making Denmark an accessible destination for Chinese tourists as well as an incoming bureau who takes in Chinese groups, because of their potential insight into the Chinese market. The interviews were between half an hour and one hour long and primarily conducted face to face in the offices of each organisation, in order to create the most comfortable situation for the interviewee. The interviews were recorded and the recordings underwent a process of simultaneous translation and transcription, with elements of meaning being condensed, as passages that were found to be irrelevant were left out.
The interviews were conducted prior to the initiation of the Chinavia project, which means that the practitioners’ configurations of the Chinese tourist were unaffected by perspectives they may since have achieved from the project. This distinction between what we might term as ‘theory’ and ‘practice’ becomes clear in the following analysis, in which we see research and DMO projects as rooted in ‘culture and difference’ and the work of practitioners in ‘business as usual’.

Research configurations of the Chinese tourist

Put bluntly, existing literature on Chinese outbound tourism can be summarized as studies that segment Chinese tourists based on demographic characteristics (Paños 2009 in Andreu, Claver, & Quer, 2013a; Andreu et al., 2013a; Andreu, Claver, & Quer, 2013b; Becken, 2003; Corigliano, 2011; Guo, Seongseop Kim, & Timothy, 2007; Kim, Guo, & Agrusa, 2005; Latham, 2011; e.g. M. Li & Cai, 2009; Ryan & Mo, 2002); focus on travel motivations and group package tourists (Andreu et al., 2013a, 2013b; Becken, 2003; Cai, Lehto, & O’leary, 2001; Chow & Murphy, 2008; Corigliano, 2011; Guo et al., 2007; Kim et al., 2005; Latham, 2011; M. Li & Cai, 2009; X. R. Li, Lai, Harrill, Kline, & Wang, 2011; Mok & Defranco, 2000; Pan & Laws, 2003; Ryan & Mo, 2002; Sparks & Pan, 2009; Wang, 2008; Yu & Weiler, 2001; Yun & Joppe, 2011; Zhao, 2006); and use either retrospective quantitative data or qualitative data, which, through different means, aim to place the tourists into segments or clusters, or in other ways try to simplify the qualitative perspectives into measurable data. An example of the latter (X. R. Li et al., 2011), who in their study of 11 focus groups, ask the interviewees about specific criteria for choosing certain things, instead of asking them openly about their expectations, which is what they really wanted information on, arguing that “service expectation might be too abstract for participants to talk about” (X. R. Li et al., 2011, p. 744). One could argue, however, that it seems more likely that the answers would be too abstract to fit into the clustering approach chosen for the study, than for the participants to talk about.

Segmentation based on demographic characteristics rarely acts as the main focus of the publication, but is instead often used to establish the group that the study is focusing on—in this case the Chinese tourist. However these characteristics turn out to be extremely broad—25–40 years old, urban, middleclass, well educated, and rarely contribute much to an actual understanding of the Chinese tourist. On the contrary, one could argue, it often illustrates the absurdity in treating Chinese tourists as one group with certain characteristics. With their focus on travel motivations, researchers often aim to gain a deeper understanding of the Chinese tourist, beyond the broad generalizations of the demographic characteristics. However, there is still a tendency to only investigate group package tourists or to treat the Chinese tourists as one homogenous group, despite the fact that close to half of the Chinese tourists who travel to destinations outside Hong Kong, Macau and Taiwan, do it as independent travellers.

There can be many reasons for this choice of focus. Practical explanations could be that (1) it is easier to collect data on group package tourists because they are more easily assessable through tour operators etc. (2) treating the Chinese tourists as one group makes it possible to collect data on the motivations of tourists who have not yet left home, making it more assessable for researchers based in Asia. Yet, the fact that these approaches are as dominating as they are is problematic. Existing research has shown that Chinese tourists are in fact not homogenous and that there are vast differences in travel motivations depending on whether you are for example a group package tourist or an independent traveller (Prayag, Disegna, Cohen, & Yan, 2013). Finally, the fact that Chinese tourists are not a homogeneous group makes the lack of in-depth qualitative studies even.
more evident, since such in-depth perspectives can often help provide the understanding needed to make sense of the existing data.

Returning to the quote that opened this article, what our review of research on Chinese outbound tourism illustrates is that the research so far has provided a lot of data on Chinese tourists, but in terms of understanding, the research still seems to be in its infancy. Based on existing research we have a lot of retrospective knowledge about the general motivations and demographics of the Chinese tourist if we accept that such a character exists. But, in terms of more detailed knowledge, for example relating to the Chinese tourists coming to specific destinations in Europe or on independent tourists specifically, we know very little. More important yet, what we do know is based on raw data rather than understanding, something which is problematic when dealing with a market under rapid expansion, development and change, where static retrospective data can quickly become irrelevant.

As we shall see in the following, the deployed research methods and the more tacit assumptions on the feasibility and usefulness in categorising tourists according to nationality or other vastly reductionist criteria also impact how tourism is developed as it can be traced into concrete projects and initiatives launched to get a bite of the attractive Chinese market. In the following example, we will use the Scandinavian and EU-funded research and development project Chinavia to illustrate how leading Scandinavian DMOs were influenced in their work by the research methods described in the above as well as the notion of culture as difference retrieved in public and media discourse.

**Replicating research configurations in tourism development. The case of Chinavia**

The primary data to be analysed in the following will be the reports published to conclude the Chinavia project. However, we also identify the origin and undertaking of the Chinavia project itself as a significant aspect in understanding and pointing out how the participating DMOs configure the Chinese tourist. As mentioned earlier on, a primary factor for launching the Chinavia project is a huge perceived growth and potential of the Chinese market. Such a potential would explain increased awareness of a certain market, as well as increased marketing or other activities toward that market. What it does not explain, however, is the focus on the Chinese as one, as a stable and delimited category.

As an explanation for the Chinavia project, its websites states that: “The purpose of Chinavia is to get more knowledge on the Chinese market. Who are the Chinese, what are their demands and where should Scandinavia put its effort in order to get a larger share of the Chinese market” (“Chinavia website,” n.d.). This explanatory project text, the project reports that we address in more detail in the following but also the discourse surrounding the project expressed a need for better understanding the Chinese. The need seems to come from a tacit or sometimes explicit notion that the Chinese are not like us, that they are radically different. It is assumed that they are different because they are not Western, different because they come from another culture, different because they are Chinese.

Aside from the origin of the Chinavia project, this notion is also explicit in the repeated and pronounced attention within the daily press and among some tourism actors to what could be considered minor differences or issues when dealing with Chinese tourists, such as their demand for hotel amenities, a water cooker in the hotel room or Chinese breakfast in the hotel buffet. The
emphasis on such minor differences became clear to the authors of this article in our participation in a conference and workshop as part of the Chinavia project. Here, participants often returned to cultural differences, culminating with a local actor asking a Chinese student present at the conference to stand up and tell what a Chinese person would feel about certain things, assuming that this one person could speak on the behalf of all Chinese tourists. While this focus on difference is not clearly present in the reports that we will analyse in the following, we see it as a very important context to take into account when analysing the DMOs configurations of Chinese tourists, as it seems as if cultural difference to the DMOs form an important, yet often tacit departure point for configuring the Chinese tourist.

The Chinavia reports

The main contribution of the first part of the Chinavia project was five reports meant to reach “... a deeper insight into the Chinese travel market, the preferences of the modern Chinese travellers and the performance of our destinations in serving them.” (Chinavia, Report 1, 2013, p. 3). These reports consist of a review of existing knowledge and research on Chinese outbound tourism; a best practice survey of marketing activities of European cities towards the Chinese market; a Chinese visitor survey, profiling the Chinese tourist in Scandinavia and identifying main travel motivations and experiences of the Chinese tourists; a statistical benchmark analysis of Chinese market growth potential to the European and specifically Scandinavian tourism industry; and finally, an investigation of the Scandinavian online presence in China. These five reports account for the results of the first part of the Chinavia project. The knowledge they contain is used as the basis for the second part of the Chinavia project, which includes product development, but they are also presented to tourism practitioners and made public to other people with interest in the growing incoming Chinese tourism market. The report on the mapping of the Chinese internet landscape is focused on the Scandinavian presence in Chinese media rather than on the Chinese tourist, and is therefore not included in the following. The other four reports will form the basis for the following analysis.

The review of existing knowledge and research on Chinese outbound tourism (Chinavia, Report 1, 2013) presents a condensed version of the rather broad results found in literature on Chinese outbound tourism: Chinese tourism is growing, there is great potential and they are primarily group tourists; in terms of European tourism, there is a visa challenge as well as challenges related to language and service, or lack thereof; Chinese tourists are shoppers and mobile netizens, with all that this entails. Such a review is a very natural way to initiate an investigation into an unknown topic. The side effect of this practice, however, might be that methods, results, perspectives or constructions existing in the literature are transferred or emulated by, in this case, the DMO. This would not be much of an issue if the existing knowledge was a reflective representation of different ways of investigating and configuring the Chinese tourist. However, as we have argued, since quantitative methods prevail in representing the Chinese tourists in the literature, this results in homogeneous perspectives, which are subsequently replicated or recreated by the DMOs.

Two of the reports focus on European destinations. The European market study (Chinavia, Report 5, 2013) is a statistical benchmark analysis showing the Chinese market growth potential to the European and specifically Scandinavian tourism industry. The report does not contribute much to the understanding of Chinese tourists, but seems more like an argument for destinations and practitioners to focus on the Chinese market. The best practice survey of marketing activities of European cities towards the Chinese market (Chinavia, Report 4, 2013) is based on a quantitative
questionnaire responded by 13 DMOs from European cities. The success of a city in this survey is based on its marketing activities aimed at the Chinese market and the time of commencing these activities. A successful city being one that has as many marketing activities towards the Chinese market as possible and that has preferably had these activities running for as long as possible. The quality of the activity or the basis that this activity was founded on is not considered.

In terms of reaching “... a deeper insight into the Chinese travel market, the preferences of the modern Chinese travelers...” (Chinavia, Report 1, 2013, p. 3) this leaves us with the final report, which is a survey of 678 Chinese tourists in three different Scandinavian cities. Although the methodology section of the report regards the data collection method as interviews, the data collections show that it is rather a quantitative survey, “The survey was conducted on the basis of printed questionnaires, which the respondents in most cases were able to fill out themselves once given a brief instruction.” “The questionnaire consisted of 26 questions, 3 of which were completely open-ended.” (Chinavia, Report 2, 2013, p. 19).

Taking the methods chosen for the study into account, the broad demographic characteristics found in existing research are unsurprisingly replicated as the answer to the question of who the Chinese tourists visiting Scandinavia is. A distinction is made between the independent tourist and the group tourist. It is reported that the older Chinese travellers tend to travel in groups and that independent travellers generally have higher incomes and are more educated than group travellers. In addition, three characteristics of independent tourists vs. group tourists in terms of activities at the destination are also mentioned “… the activities listed also induce the observation of a more thematic distribution between activities typically related to the traditional Chinese tour group traveller and the predicted trends of a more exploratory and independent Chinese traveller.” (Chinavia, Report 2, 2013, p. 53). These differences being that independent travellers are more inclined to go beyond the known and challenge their palate and that independent travellers shop for local products. However, the distinction between independent and group tourists is largely ignored in significant parts of the survey where the Chinese tourist is, again, considered a homogeneous group. Thus, results similar to those found in the existing literature are also replicated in the second and third part of the report: The main bulk of Chinese tourists are group tourists, are 1st timers to Scandinavia, are often touring several countries, are big shoppers, have short stays of 0-2 nights and go for major tourist attractions. This is followed by similar broad data that accounts for the planning behaviour of the homogeneous Chinese tourist.

In the analysis of motivations and expectations it becomes clear that the difference between group tourists and independent tourists is perceived as something important, but that the methods used for the survey provides data that connect motivations and experiences of the travellers to them being either group travellers or independent travellers. Previously in the report it was mentioned that a relatively large portion of tourists going to Copenhagen (82%) travel as group tourists compared to Helsinki (50%) and Stockholm (39%)(Chinavia, Report 2, 2013, p. 6). To compensate for the lack of clear data on the motivations and experiences of the group tourists vs. those of independents, Copenhagen is chosen to represent the group tourists in the on-going analysis, when compared to the other two cities “Keeping in mind, however, the considerably larger share of tour groupers among Copenhagen respondents, it is interesting to compare the scatter plot of Copenhagen to that of the other two cities.” (Chinavia, Report 2, 2013, p. 78). This practice indicates that the DMOs conducting the research has realized that Chinese tourists at least has to be divided into group travellers and independent travellers in order to provide results that fairly depict the Chinese traveller. However, since this realization has evidently emerged
in the analysis process, the methods deployed to investigate the Chinese tourists does not allow results that address Chinese tourists as two separate groups, which in this case necessitates the questionable practice of letting Copenhagen represent group package tourists. This practice illustrates how the methods chosen to study the Chinese tourists have developed out of the way of reaching nuanced results.

The final part of the report accounts for the answers to the three open-ended questions, which is the only qualitative aspects in the Chinavia I project. The respondents are asked to write down their motivation for travelling to Scandinavia, as well as their best and worst experience in Scandinavia. This analysis provides insights from the respondents, which go beyond generic characteristics. Interesting examples of motivations include: Experiencing local customs, traditions, culture, people. Another interesting result of this part of the analysis is a comparison of the ideal Scandinavian experience and the actual Scandinavian experience. It is reported that the ideal experiences include an experience of Scandinavian cities as green, clean and relaxed, an opportunity to escape a busy everyday life and indulge in the serenity and tranquillity of Scandinavia to ease the mind and lastly an educational journey to broaden the mind by exploring local history, tradition and society. Meanwhile, the actual experience is explained as inconvenient due lack of Chinese information and service, not as clean and green as expected and providing an inadequate service level (Chinavia, Report 2, 2013, p. 85).

Even though these qualitative perspectives are underrepresented compared to the quantitative perspectives in the reports and relatively shallow compared to other qualitative studies, they add an important nuanced perspective on the motivations of the Chinese travellers. This addition of a few qualitative perspectives to the motivations of the Chinese tourists illustrate how such ways of representing and understanding the tourist adds to and alters the idea of the Chinese tourist in general. Such insight might change or nuance the way in which the Chinese tourist is configured by the DMO who argue that they try to get in-depth knowledge of them. What we see in the qualitative approaches is that affinities and differences in perception are pointed out in a way that might not be generalizable, but instead is very concrete and usable. This further illustrates the importance of supplementing generalizable quantitative data with in-depth qualitative perspectives. We will discuss this relation as well as a more affinity based approach further in our final discussion.

The Chinese challenge: a practitioner perspective

As previously mentioned, the interviews with practitioners who have engaged with Chinese tourists took place in 2012 before the launch of the Chinavia project. Hence, we may presume that the views brought forward by the interviewed practitioners are not affected by the project, but rather stem from a practical engagement with Chinese tourists. By looking at how the practitioners understand the Chinese tourists, we are able to provide another view of how the Chinese tourist can be represented, configured and engaged with, which diverts from that offered by research and DMOs. As we will now see, the practise based approach takes its departure not in nationality or cultural difference, but instead in ‘business as usual’, focussing on accommodating ever changing customer needs. While this configuration challenges the researcher/DMO configuration, the ‘business as usual’ approach also creates limitations in engaging with the Chinese tourist, which we will deal with in the final section of the paper.

Unlike researchers and the DMOs, nationality and cultural difference are rarely the points of departure in dealing with different types of tourists for practitioners, as becomes clear in the
interviews. This was witnessed by how quickly conversations with the practitioners most often turned from being about Chinese tourists to aspects such as group tourists more generally or travel career. When asked, practitioners describe the Chinese not as part of a specific segment based on their nationality or culture, but rather as part of the group tourism segment or the segment of tourists who are early in their travel career. The following statements from three different hotel representatives illustrate this. According to the first representative “There are also a lot of Japanese in the summer, but we don’t distinguish between whether it is a group from Asia or from the Middle East. That is the same for us.”. The second representative provides an example of the ‘travel carrier’ perspective: “... in the beginning it’s mainly about getting out and getting notches in the belt: “How many countries have I seen? I need to see the most popular places that I have heard about – Paris, Rome and so on.”. As noted by the last representative this perception impacts the way the Chinese are met in the hotel: “We treat all our tourists similarly, we don’t do specific things because we have a Japanese group, a Chinese group or a Russian group.”.

Challenges related to cultural differences, such as the language barrier and the need for Chinese food at the destination, which are often pointed out as a crucial aspect of the tourism encounter in the literature (Becken, 2003; Kau & Lim, 2005; X. R. Li et al., 2011; Ryan & Mo, 2002; Wang, 2008), are acknowledged by the practitioners. Yet, contrary to the literature these are not seen as major challenges. Rather, they are seen as things which can easily be accommodated: “... we can make Chinese breakfast if they want it and have it in the buffet (...) but they [The tour operators] have not asked for that, they [The Chinese tourists] would like to try Nordic food when they are here...”as one hotel representative puts it. An airline carrier backs up this understanding in the following quote “... it is not all Chinese people who like meatballs and mashed potatoes, they like to have their noodles. But these are small things and not big challenges.”. Lastly, a hotel representative tones down the language barrier: “Obviously there is the language challenge, but they typically have a guide, who speaks English, so that is not a problem.”

While the starting point for Chinavia and much academic literature was to pinpoint the differences of the Chinese Other, these examples illustrate that most practitioners do not perceive cultural difference as a barrier. Some even contest it as a matter of fact. Some perceive the Chinese tourist as “easy to satisfy” while others point to how in time, the Chinese tourists will become like other travelers and how this will diminish or erase eventual differences or difficulties. As noted by an attraction representative:

"... I think that, at some point, the Chinese will also figure out how to go to Europe by themselves – that they don’t want be a part of a travel group. They will also, like we have done in Denmark, find out how to travel on their own and then they will be like every other tourist group.”

This displays a radically different way of configuring the Chinese tourist, in which nationality and culture are subsumed or even replaced by an identity as consumer or guest. Implicitly (although probably inadvertently) Chinese culture and cultural identity are addressed not as stable entities as in the case of literature and DMOs, but rather as being in constant flux. This corresponds with the idea, as noted by Ren & Ooi (2013):

“... identities are never unified and are increasingly fragmented and fractured; they are never singular but variously constructed across different intersecting and antagonistic discourses, practices and positions. [...] They are constantly in the process of change and transformation. Identities are about questions of using the resources of history, language and culture in the
Throughout the interviews, we are given examples of how the practitioners in their practise relate to just that; the process of becoming. Although some of the representatives mention different cultural issues when dealing with Chinese tourists, these issues are only perceived in a few cases as unique to Chinese tourists, as exemplified here: “In the hotel business we are used to flight crews where there are a lot of cultural issues and hierarchies and so on. (...) the hotel industry should be ready for everyone.” Many of the representatives also argue that the cultural issues related to Chinese tourists in particular are very limited. As noted by an Airline Carrier representative, “They know that they are travelling under certain conditions, that they are no longer in China and it is not everyone who speaks Chinese and that it is not a good idea to spit on the marble floor in the National Museum, they know this.”

This practise based configuration of the Chinese tourist as a costumer goes to show how literature and development projects might be overstating the importance of certain attributes, in this case cultural difference and nationality, simply because they are the point of departure for a research project in which differences are the most striking—and most easily researched—characteristics. However, at the same time, the practitioners also illustrate why nuanced research into these spheres is necessary, since their ‘business as usual’ approach is to a large extent lacking the understanding necessary to engage with new markets and customer groups in a culturally sensitive way.

An example of this is found in a conversation with a hotel representative, lamenting how Chinese tourists never complain during their stay: “If they complain, then they wait until after their stay and then it is too late, which is a shame because we would like to help them, but that is their mentality”. Another hotelier backs up this concern: “… one of the negative things – we never get any complaints or hear anything from them. But I don’t believe that not at least one person has gotten a room that he or she does not like or something like that.” This problem of ‘no complaints’ could be grounded in the need to save face (Mok & Defranco, 2000), but by seeing past culture, the managerial possibilities to deal with it are restricted. In their attempt to treat all tourists similarly they may miss important signals or ways to accommodate needs and behaviour which may be culturally related. In their wait for the Chinese tourist to become ‘just like any other traveller’ they may miss out on opportunities for growth. More importantly, ignoring differences that may actually be present is just as big of an issue as overstating them. In the last section, we will discuss the opposing configurations of the Chinese tourist, which we have introduced so far, and discuss how to strike a balance between them.

**Concluding remarks**

As shown, the different stakeholders in developing and managing Chinese tourism in Scandinavia work according to two very different configurations of the Chinese tourist. As we have shown, both configurations allow them to engage with this new and important tourist in different ways, which have positive as well as negative impacts.

In the research configuration, which has also been taken in by DMOs, the Chinese tourist is represented as a nationally and culturally rooted category, using research methods that bring forth and reproduce differences rather than exploring and challenging them. While this allows researchers and developers to discern a new homogenous tourist figure, it also neglects how Chinese tourists...
are far from homogenous and far from stable. Tourists are not their culture or nationality and do not (only) act ‘according’ to it. Reversely, in the practice oriented configuration, the point of departure is not differences, but rather to service and provide for a customer. While this approach creates a more dynamic configuration, it also reduces the tourist to just another customer, hereby omitting or neglecting important cultural aspects.

So the question remains how to strike a balance between seeing the Chinese tourist as radically different and as ‘just another customer’? How may we make other analytical cuts into—or around, difference? How do we develop categories which are manageable yet dynamic enough to reflect change and heterogeneity? In this last section, we would like to suggest an affinity approach which makes use of other cultural categories, which are rooted in in-depth empirical work and do not already assume categories such as ‘Chinese’ or ‘just another customer’. While allowing us to categorise—and hence to manage—this substantial tourism market, such affinity based categories abstain from (re)producing stereotypical representations.

In an interview, a practitioner described how the famous writer H.C. Andersen is attracting Chinese tourists to Denmark, rather than the destination itself: “H. C. Andersen is more famous than Denmark. If you ask a Chinese person where Denmark is, they have no idea, but if you ask them whether they know H.C. Andersen they will say” yes!” and start telling one of the stories.”. Other interviewees point to a unique culture and more intangible things which interest and attract a Chinese public to Denmark. As proposed by the airline carrier representative examples of this are: “cleanliness, fresh air and logistics”. Also heritage, authenticity and welfare are affinities, where Scandinavian society and a Chinese market could find communalities from where to meet and exchange. By working to collect empirical examples of such affinities and analytically addressing how to categorise and later to operationalise them, we are able to see beyond perceived differences and instead focus on meeting grounds where local qualities and characteristics are developed to suit a Chinese market. For future research, we therefore encourage a stronger focus on what people say, do or aspire to in their travelling and how affinities that comply to this can be developed at the destinations, rather than what they ‘are’. This abstains from reducing people into stale and stereotypical representations and takes an important step towards getting truly ‘China ready’.

References


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On ASEM and the Cartography of Asia, Africa and Europe

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Abstract

The ASEM has been growing steadily in size and scope since its inception in 1996, and will probably continue to do so in the future. This article tries to map both the history of the concepts for depicting the classical continents and their very flexible boundaries, as well as a possible future course for ASEM from a cartographic point of view, especially in regard to the importance of and interest in Africa that most current ASEM members are showing. This is also considered as one of the future recommendable directions of the expansion of ASEM.

Key words
Asia; Africa; Europe; ASEM; cartography

Introduction

I will attempt to combine in this article three completely disparate elements: commenting on the contemporary Asia Europe Meeting (ASEM), on ancient cartography of the old continents, and on the developmental needs of Africa. The result may be confusing, but yet, perhaps, conceptually interesting. This is the way a conceptual historian thinks.

During its brief history ASEM has rapidly evolved from a mid-size international organization in 1996 to a fairly large organization in 2014. In the inaugural meeting in 1996 there were 25 state members, clearly limited to member states of the European Union and the ASEAN+3 formation. The categories of Asia and Europe were clear and undisputable, and it seemed that the two economically and politically strong two extremes of the Eurasian landmass were monopolizing the usages of Asia and Europe (Korhonen, 2007).
ASEM in 2014, after several rounds of enlargement during the Summits in 2004, 2008, 2010 and 2012 is a fairly large organization with 51 members, 49 of which are states: the 10 ASEAN countries, China, Japan, South Korea, Mongolia, Bangladesh, India, Pakistan, the 27 EU member states, Norway, Switzerland, Australia, New Zealand and Russia. The ASEAN Secretariat and the European Commission are also counted separately as members. In Milan in 16–17 October Croatia is supposed to join, becoming the 52nd member, while Turkey and Kazakhstan are on the waiting list. Many more states, which in terms of formal modern geography would be situated in either Asia or Europe, are still missing from the organization, and as the acceptance rate of new applicants has been rather high in the past, we can reasonably expect that the organization will go on expanding also in the future. Central Asian, Western Asian, Eastern European and some Southeastern European states are still largely empty spaces on an ASEM map.
At the same time the binary categories of Asia and Europe have become slightly blurred, because geographically peripheral and boundary states have been added. During the 8th ASEM Summit held in 2010 in Brussels Australia, New Zealand and Russia were accepted as members. They were problematic cases in terms of definitional categories, as in Asia there has been a long debate whether Australia and New Zealand could be defined as Asian states, dating to Australian Foreign Minister Gareth Evans’ redescription of the “East Asian Hemisphere” in the 1990’s (Evans, 1995). In the case of Russia the categorical problem was that it is situated both in Europe and Asia, so that it was unclear whether it joins as a “European” or as an “Asian” state, while the EU at that time still reserved the category of Europe only for EU member states. These definitional hurdles were overcome by adding a new category, namely the “Third group” (Gulyaeva, 2012), called also the “Pacific group” (Yeo, 2013). During the 9th ASEM Summit in 2012 in Vientiane, Norway and Switzerland were added, thus again diluting the narrow definition of “Europe” to mean only the EU within the ASEM categories.

There exists a perennial discussion on the importance of ASEM, which has accompanied it since its inception (Bobrow, 1999). As Yeo Lay Hwee recently commented, although the large membership accounts for 60% of the world’s population, 50% of global GDP, and 60% of world trade, it remains relatively unknown among the citizens (Yeo, 2013). The media does not cover the meetings very seriously, comments in media usually are that ASEM cannot achieve very much, and there is also a feeling that national leaders are loosing interest in the organization, one reason being the low level of visibility of the summit meetings, and another the fact that contemporary governance of the world and its regions demands lots of participation in meetings. ASEM has to compete with other organizations and forums for attention during a period, when “principled multilateralism” is giving way to “diminished multilateralism” and “forum shopping”, as Jürgen Rüland argues (2012). International organizations have turned into fora of intensifying power struggles between states aspiring for regional or global leadership roles, and between established and rising powers, or status quo and imperialist powers, as Hans Morgenthau formulated it already in 1935. Forum shopping implies that existing international organizations are shunned, and instead new ones are created, and bilateral forms of interaction are favored against multilateral ones. Of forum shopping Nicolas Sarkozy’s L’Union pour la Méditerranée of 2008 is one example (Balfour et al., 2008); the BRICS after 2006 are another (Keukeleire et al., 2011), and the new Development Bank launched by the BRICS in July 2014 (Xie, 2014; Robles, 2014) are cases in point. Instead of ASEM, the EU and ASEAN can engage in direct dialogue with each other; the EU has direct strategic partnerships with major states like China, India and Japan; all East Asian states as well as the EU are engaging in a multitude of bilateral free trade agreement negotiations, a number of which have also been concluded during the past years.

There are of course also attempts to invigorate the ASEM summits, to maintain their momentum and increase their importance among institutions of global governance. These include attempts to make the meetings less bureaucratic, producing fewer and shorter papers requiring less haggling, and to arrange a “retreat” session for national leaders, where they can discuss relatively freely among themselves (Islam, 2014). The open conflict in Ukraine with EU sanctions against Russia is also a clear problem for ASEM now that Russia is a member, but apparently Italy as the chair attempts to keep the ASEM structure intact, specifically trying to ensure that also President Vladimir Putin will attend the conference (Interfax, 2014).

However, perhaps the main importance of ASEM does not lie in the summits. Unlike many other large interregional institutions, ASEM has systematically tried to construct a deep structure for
the interaction, including various ministerial meetings, business leader meetings, and meetings of civil society organization representatives. The Asia Europe Foundation (ASEF), Asia Europe Journal (AEJ), and Asia Europe Institute (AEI) are all important fora for the exchange of culture, understanding, ideas, and scholarship, all with a vision over immediate political concerns and day-to-day politicking. ASEM’s long-term importance may rather lie in its broad level of institutionalization, rather than with the summits.

Even the brief history of ASEM shows that temporal political constellations and decisions influence geographic categories, rather than vice versa. On a longer historical perspective we can say that the formation of geographic regions, especially their boundaries and peripheral areas, or what belongs to which category and what somewhere else, is historically a haphazard process, depending primarily not on geographic characteristics, but rather more on political and economic, but sometimes also on cultural, climatological, religious, and perhaps even artistic circumstances—in the sense that cartographers are individuals, who also have an aesthetic sense. We could take a look at the origin of the concepts of Asia, Africa and Europe to open more the possibilities of understanding the potentialities in the interpretations of these concepts. They could mean much more that they happen to nowadays, and old meanings can acquire new importance as a basis for political arguments in such expansion prone organizations as ASEM. Irrespective of the future importance of the summits, the larger organization itself could remain important for managing the vast trading regime, which maintains the momentum for adding new members during the following decades. The emergence of Africa as an important trading region should be of interest also for ASEM in the future.

The Origin of Continental Names

Unlike often thought, originally Asia, Africa and Europe were not European concepts, but rather Eastern Mediterranean geographic names, which at the time of the birth of continental thinking was a distinct cultural region of its own. Only quite recently, during the nineteenth century, have they become commonplaces in the entire world. They are best analyzed as synecdoches, which represent larger narratives, while as names they also become established by being used within narratives. The basic plot of old Greek narratives follows the geopolitical structure of civilization developed by Mircea Eliade in his *Cosmos and History*, first published in 1959. The centre of the world is depicted as a culturally based cosmos, where normal and normative human beings dwell, and around it are situated zones of increasingly miraculous beings. In the ancient Mediterranean world there was variation whether the centre was based in Egypt, which was considered as the origin of civilization, or in a contemporary political centre, such as Athens, or later Rome. This issue was never settled in ancient literature.

One of the origins of the names Asia and Europe has been traced back to the language of the Akkadian empire around 2500 BC, where āsīu referred to the rising sun, and erēbu to the setting sun (Klein, 1966). Akkad was a Semitic language belonging to nomads living in Arabia and the Zagros Mountains. They invaded and conquered the collection of Sumerian city states in the lower reaches of the Euphrates and Tigris, and the empire of King Sargon (2334–2279 BC) which extended west to the Mediterranean. We do not know where Sargon’s capital Agade was situated, but it probably was somewhere in the Sumerian heartland, where most of the population and wealth were concentrated. If you looked from there to the east in the morning, you might have seen the sun rise behind the Zagros Mountains, while it set in the west in the lands, where Jews
and Phoenicians later built their kingdoms. Etymological research cannot by its nature establish undisputable truths, the āsū-erēbu pair is only a logical guess. Even less is known how the words were incorporated into Mesopotamian geographic theories as names for continents, but during the following two millennia they spread widely through the region. The Lydians, Medians, and Persians used these names and eventually also Ionian Greeks learned them. We do not know when this cosmological construction of the world took place, but even in Greek the concepts are so old that two millennia after Sargon they were woven into Greek myths of the origin of the world. The study of continental metaphors normally starts with Greek literature. The Greeks did not know where the idea of dividing the world into continents came from, but Strabo suspected that the origin lay in the fact that general names were needed for Greek lands facing each other over the Aegean Sea. A number of Greek villages, towns and city-states existed in both the eastern and western coasts of the Aegean, and Europe and Asia served as useful regional names (Strabo 1968I.4.7.). Inhabitants around the Aegean would thus have applied the originally Semitic words Asia and Europe to their own living environment. The division was thus an intra-Greek affair, because it was used in separating Greeks living in Hellas from Greeks living in Anatolia. It is in this sense that Herodotus presented the Persian argument that European Greeks invaded Asia when they attacked Troy (Herodotus 1990 I, 4).

It seems, nevertheless, that the names were eventually adopted as parts of the general Greek cosmology and the area of the continents was extended over the whole known world, with a third continent, called Libya at that time, added to the list quite early. The earliest surviving literature already told about places as distant as southern Egypt. Even though the concepts were not as important as they are nowadays, they formed an interesting intellectual puzzle, and among historians there was an ongoing debate about the boundary separating Asia from Europe, and Asia from Africa. The Aegean was a clear area of continental division, but there was no general agreement where the boundary might lie farther to the north. The Mediterranean neatly separated Libya/Africa from Europe, but the demarcation in the southeast was debatable. The debate was never solved during the millennia of classical Greek civilization, which later enabled various innovative redescriptions by Roman and Christian authors. Of course, the boundary issue is unsettled even nowadays (Lewis & Wigen, 1997).

**Classical Conceptions of Asia, Africa and Europe**

The Homeric and Hesiodic legends, dating from about 700 BC, were authoritative cosmological sources for later Greek thinkers. Strabo considered Homer to have been the founder of the science of geography, because he explained the general shape of the world, and established its basic divisions (Strabo 1968I, 2-11). Because of the importance of Egypt, the Nile was considered to be the greatest and most venerable of all rivers. Ethiopians were thought to be living on the southern side of Egypt, occupying the whole southern part from the sunrise to the sunset, and because their living places were separated by the Nile, they were thus considered to be living in two places (Homer 1995I, 22-24). Strabo interpreted this to mean that Homer considered the Nile to be the first continental divide, although he did not yet name the continents. At the opposite side of the world dwelled Nomads in the north. These two peoples inhabited the climatological extremities, while ordinary people lived in the middle, along the coasts of Tethys, with which we can understand not only the Mediterranean, but all expanses of salty water sailed by the Greeks from Gibraltar to the Black Sea. The basic geographic division of the world in Homeric literature was thus made along the climatological south-north dimension.
In a fragment of Aesculus a definition of the boundary between Europe and Asia was given as the mighty river Phasis (Aeschylus, 1992, Fragment 106). There are many small rivers flowing from the Caucasus Mountains to the Black Sea, and it would be impossible to say which one of these actually was meant. The Phasis was above all a mythical river, the end of the sailing of the Argonauts, and a mighty stream at the end of Tethys was necessary for the Greek cosmography. If there was to be a geographic division of the world, it necessarily had to relate somehow to the two existing magical bodies of water, Tethys and the Nile, i.e. the division had to run as a logical continuation of either of these waterways. Tethys ran from west to east, and the Nile from south to north. The Aeschulian solution was to concentrate on the west-east direction, and elevate Phasis to a rank similar to the Nile, as a wide stream dividing two continents from each other. This is the oldest mentioned boundary between Asia and Europe. A little later Hecateus seems to have separated the western peninsula of Asia into a special continent called Libya; the boundary naturally lying along the Nile (Strabo 1968I, 11-12). Thus we have arrived at the classical division of the old world into three continents.

For Herodotus, Libya was a blessed place, because its eastern end was in Egypt, the seat of ancient civilization and abundant harvests. Nowhere in the world were there as many marvellous things and so many works of unspeakable greatness as in Egypt. Ethiopia to the west of Egypt was not a bad place either. There was plenty of gold in Ethiopia, as well as elephants, woodland trees and ebony. The people were the tallest, fairest and longest-lived of all men (Herodotus 1990 III, 113). Nevertheless, nothing could surpass the greatness of Egypt itself. For instance, the greatest king of all history had been Sesostris, king of Egypt, whose empire had reached from Ethiopia in the west to Arabia in the east, and to Europe in the north (Herodotus 1990 II, 102-110).

Asia seemed to be a place similar to Libya, but perhaps smaller. Asia was so small that it was basically covered at any time by a single empire, like those of the Median, Scythian and Persian empires, which all were said to have encompassed all Asia (Herodotus 1990 I, 104-6, 130). Likewise, Alexander the Great was also said to have ruled all Asia. Asia was inhabited from the eastern banks of the Nile all the way to India, but after India there existed only uninhabited deserts, and Herodotus did not have any information about them, or what lay beyond them. Anyway, he did not think that Asia would extend far to the east (Herodotus 1990 IV, 37-41). Thus, nearly all of the Asia of Herodotus was composed of a few civilized kingdoms. It was the wealthiest of all the continents, and besides the eastern deserts, with nothing residual imposed on its area.
Europe was the greatest anomaly, because it seemed to be indefinitely vaster than the other two continents. It spanned the length of them both, and no one knew where it ended, either in the west, north, or east (Herodotus 1990 IV, 45). Europe thus contained all residual land that could not be meaningfully placed into the other two continents, which is a clear indication that although Europe was geographically meaningful, culturally it was a rather unnecessary category. It was the most unknown of continents, and practically all of it represented peripheral chaos in the Eliadean sense, except the areas settled by the Greeks themselves. Most of Europe was populated by Scythians. The general term Scythian was not an ethnic denomination, but rather described a way of life, that of nomadic people moving around after pasture with their herds of horses, cows and sheep over the grasslands and forests of Europe, living in wagons and light dwellings, seldom building towns, except on the coast, where they could get additional income from robbery and trade. Thus within the Greek cosmology Europe was an unbounded vast region inhabited by wild barbarian tribes, cannibals and mythical beings. Excepting Greece, Europe was essentially a place without history. Asian history, instead, was political. It was a grand narrative of succeeding political organizations, with Lydians, Medians and Persians fighting alternately for grand empires. With Alexander’s conquests, Greek awareness of the east expanded, and especially India, which Alexander was not able to conquer, became during the following centuries a land of mythical proportions. Travellers, ambassadors and merchants visited India and told various tales of it. Strabo already reported from his own trip up the Nile in 25–24 BC that annually about 120 ships sailed from the Arabian Gulf to India, many of them financed by Alexandrian merchants (Strabo 1968II, 5, 12).

Map 4 The world according to Strabo

Strabo (64/63 BC–c. AD 24) divided the world differently from the earlier classics. He decided to present Europe as a small continent. That meant adopting a new river as the boundary between Asia and Europe. The mythical proportions of the Phasis had dwindled during the centuries of
travel, while the Tanais (Don) truly was a big river, so that it was more suitable as a continental boundary. Strabo was a Roman citizen, and although Rome was an intercontinental empire, the origin and capital of Rome was clearly in Europe, so it was not politically feasible to present Europe simply as vast unknown barbarity. Strabo argued that the valleys in Europe produced peaceful people interested in good administration, while mountains provided for fierce warriors. Europe thus had an ample supply of both elements, a warring spirit for military expansion and an ordering spirit for the administration of the lands conquered. Strabo’s examples were the Greek, Macedonian, and Roman empires (Strabo 1968II, 4, 5-7).

Strabo was able to use good geographic information in writing his geography, and thus he was of the opinion that the Red Sea would have been the most logical boundary between Libya and Asia (Strabo 1968I.2.28), but in the end he decided to agree with the ancient definition and to keep the Nile as the eastern boundary of Libya. Everything to the east of Europe and Libya was Asia, so that Asia became the biggest of all continents, occupying half of the known world (Strabo 1968II.5.26). Notwithstanding, Asia remained the most exalted continent even in his account. For instance, he reported the barbarous customs of Scythians in his narratives of Europe, even though a large portion of the Scythian lands had now been allocated to Asia. Strabo also placed in Asia the only place on earth that exceeded Rome in blessedness, and that place was India. Strabo called it the greatest of all nations and happier than any other (Strabo 1968II.5.32). The western boundary of Asia could not be defined clearly except by naming the rivers; the origins of the Nile and the Tanais were unknown, and both rivers could simply be extended all the way to the surrounding world ocean. It can thus be argued that on the whole the geometry of continental thinking had not changed much, only the Euro-Asian boundary had been shifted to run from the south to north.

The Greek debate on the continental boundary did not end with Strabo. Procopius of Cesarea, a Greek historian, who lived in Eastern Rome in the sixth century AD, summarized both arguments in his History of the Wars, pointing out that some authors demanded that the boundary had to be understood as a continuation of Nile, while others maintained that the Euro-Asian boundary had to be understood as a continuation of the Mediterranean in the eastwards direction (Procopius 1993VIII, vi, 1-12). He offered no conceptual solution to the thousand year long debate, because both arguments had been presented so many times by different authors. Empirical exploration seemed to offer the only solution, the practical discovery of the real waterway that actually separated the continents. Nevertheless, the kind of definitive solution to determine the boundary of Asia and Europe by way of exploration was never actually attempted. The problem was not considered very important.

Roman thinking was definitively less global than Greek thinking, usually being confined to the Roman Empire and adjacent regions, not trying to encompass the whole world. Most Roman authors treated Asia only as a Roman province at the western end of Anatolia. The main continental change they made was the renaming of the southern continent as Africa, according to a Roman province there. They transmitted the Greek ideas to later periods, though, by preserving Greek geographic literature as translations into Latin, an example being Pomponius Mela’s De Chorographia. Similarly, Medieval Europeans were not interested in continental geography. They were peripheral people, staying for the most on their own habitat, and their main cosmological concepts were religious, not geographic. Of course the production of mappaemundi started during the late Middle Ages in connection with the Crusades, but their simple schematic nature clearly displays the lack of definite geographic knowledge of the world.
Portuguese cartography during the explorations

It is only during the period of explorations from the fifteenth century onwards that the continental divisions of the world again became intellectually important. This is especially true for Portuguese explorers, who sailed along the African and American coasts, in the Indian Ocean, in Southeast Asian waters, and in the Western Pacific. Duarte Pacheco Pereira’s (14??-1533) *Esmeraldo de Situ Orbis* is important in this sense. He was one of the most important Portuguese seafarers, making exploratory journeys in Brazil, the African coasts and India. As Joaquim Barradas de Carvalho shows, Pacheco Pereira’s treatise finely amalgamates classical learning from Homer onwards, Christian cosmology, and contemporary Portuguese empirical observations of four different continents (Barradas de Carvalho, 1968).

![Map 5: The world of Pacheco Pereira, early 16th Century](image)

Pacheco Pereira used the three classical names, *Europa, Asya and Africa*, separated from each other by the usual Mediterranean, Don and Nile, as said in classical books. He did not actually, however, think of them as continents, as on the basis of Biblical evidence he thought that most of the earth had to be dry, sea being only a large salty lake bounded on all sides by land. Most of it was thus far unknown. The Brazilian coast that he had visited was part of this outer land crescent. Martin Waldseemüller published in 1507 his map *Universalis Cosmographia*, where he gave for the fourth continent the name *America* in honour of the Italian explorer Amerigo Vespucci, who financed at least part of the drawing of the map. This is the time when Duarte Pacheco Pereira was writing his manuscript, but apparently he was not aware of Waldseemüller’s map.
Africa and the Nile were of most interest to Pacheco Pereira, because he knew that region best, while Europe was of no apparent interest to him, except that he already oriented his cartographic thinking towards the north, and thus Europe becomes the uppermost continent in visualizations of his thinking. He thought that theoretically he had understood where the origin of the Nile was. As Ptolemy had suggested, and as had been accepted in much medieval literature, the origin of the Nile was supposed to be in the Montes Lunae (Mountains of the Moon), a long way south from Egypt, so that the flooding pattern of the Nile in summer when there was little or no rain in Egypt could be explained. Because the Nile was the boundary between Asia and Africa, the Montes Lunae theoretically had to lie at the southern end of the land; otherwise the river could not have served as a proper boundary. Thus Pacheco Pereira logically thought that they had to be the rocky mountains seen while sailing past the Cape of Good Hope. From there the waters then flowed along two main courses, one of them entering the sea in the west as the Senegal and Niger rivers, the other course flowing to the Mediterranean as the Nile (Pacheco Pereira 1937, 16-7, 78, 80, 154-5). This conceptualization meant that as soon as the Portuguese sailed around the Cape of Good Hope, they entered Asia.

However, as Homer had already told 2,200 years before Duarte Pacheco, all land south of Egypt was also called Ethiopia. Duarte Pacheco also recognized two Ethiopias, or sometimes three. The Lower Ethiopia extended on the southern side of the Senegal River all the way to the Indian Ocean. The other Ethiopia was called Upper Ethiopia, and it began at the Indus east of the great kingdom of Persia, and then extended eastwards, without a specific eastern boundary (Pacheco Pereira 1937, 78-9). It is thus impossible to find any special conceptual difference between Asia and Ethiopia, except that perhaps Ethiopia was a larger concept. Or perhaps we should say that Ethiopia unified Asia and Africa into one region, covering most of them both, at least as seen from the perspective of southern seas.

Duarte Pacheco was not the only Portuguese explorer who used the concepts in this way. Fernão Mendes Pinto’s (1509-1583) Peregrinação (Pilgrimage) is the most famous Portuguese travelogue, translated into various European languages. It was an autobiography, dealing with the travels of Pinto himself as an adventurer and occasional pirate for over 21 years in eastern waters, written during the 1570s, and published posthumously in 1614. It is a colourful book, describing the adventures of the protagonist during alternating fortunes and misfortunes in various eastern kingdoms. Because it is written in the form of a memoir, it is impossible to ascertain the truthfulness of the narratives, and it has the fame of a book full of lies, similar to de Mandeville’s Travels. Nevertheless, perhaps the book resembles even more John Bunyan’s The Pilgrims Progress, written in 1678. Both books are deeply religious works describing unwavering Christian faith through a string of changing fortunes in strange lands. The name Peregrinação also refers to this aspect. Notwithstanding, it is an interesting book, and its advantage is that it was written by a truly non-scholarly person, presenting language that probably was used among common Portuguese adventurers at the time. In his first chapter Pinto explains that he had travelled all over within the boundaries of Asia, listing its places as ‘Índia, Etiópia, Arábia Feliz, China, Tartária, Macaçar, Samatra e outras muitas províncias’ (Pinto, 2001, 23). Thus, again we see Ethiopia and Asia occupying at least partly the same space; they belong together.

Pinto never specifies his geographic regions, so that we are not able to say anything specific about their locations or boundaries; we can only notice the association. However, what we can say is that for the first 2,300 years of the continental conceptualizations of the three old continents,
the boundary between Asia and Africa laid on the Nile, rather than on the Red Sea, and as a large regional concept, Ethiopia blurred the boundary between these two. Similarly, we can also observe that the boundary between Asia and Europe has been equally contentious. Of course lots of defining and boundary making has taken place during the past 500 years—but a mere half of a millennium is actually a rather short time.

ASEM and Africa

When one reads publications by international developmental organizations for Africa, there are strong signs of positive economic performance in the continent, although mostly the argument about true development at the citizen level is still about future possibilities. Anyway, numerically good economic growth has taken place there for the past twenty years, picking up during the past ten years, and in 2013 Africa was the second most rapidly growing macro region in the world, at 4.7 percent, overtaken only by Southeast Asia and the Pacific, which grew by 7.2 percent. Both figures were well above the world average, which was only 2.4 percent (World Bank, 2014). In statistical macro figures, Africa is thus doing well nowadays. Most of this growth is lead by investment, which is pouring in not only from the traditional donors Europe and the USA, but also from China, Japan, Korea, India, Russia, Brazil, and elsewhere (UNECA, 2013), most of these countries being ASEM members. Investment goes mostly on the extraction of basic commodities, especially oil and minerals, and on building infrastructure, but food production is also one target. Fairly robust growth takes place also in the service sector, where tourism industries are expanding, and investment in transport, telecommunications, and banking is growing. Much of the incoming capital flows go to countries with rich natural resources, such as Angola, Mozambique, Sierra Leone and the Democratic Republic of Congo, but also to countries with poorer resource endowments, such as Ethiopia and Tanzania (World Bank, 2014).

Problems connected with this growth are that it has not been markedly facilitating African industrial development, nor has it yet been very effective in linking Africa into international chains of production, except at the stage of exporting natural resources. Global value chains, based on offshoring, outsourcing, and in general on the role of intermediate goods in modern production networks, are concentrated on East Asia, Europe, and North America, and Africa is mostly outside of them. Its share is small, and increasing only on a minuscule pace, from 1.4 percent to 2.2 percent between 1995-2011 (AfDB et al 2014, 13). Besides the natural commodities, the potential African advantage is its growing young work force, which is mostly stagnant or shrinking in other parts of the world, such as in China, whose population growth is coming to an end, while wages go on rising rapidly (Yi et al 2013). This leads to the famous thesis by Vandana Chandra, Justin Yifu Lin, and Yan Wang, according to which several millions of light manufacturing jobs could find their destination in Africa in the near future. According to their figures, China alone employs 85 million workers in its manufacturing sector. A fair share of them will lose their price competitiveness fairly soon. If we add Brazil, India and Indonesia, we get some 40 million workers more in global manufacturing, and these jobs are later during the coming decades expected to locate somewhere else. Of course all manufacturing jobs would not be relocated, but if China relocated to Africa only 10% of its jobs requiring only unskilled low wage workforce, or 8.5 million jobs, this could double the amount of African labour force in manufacturing (Chandra et al., 2013, 77). As light manufacturing has historically been afforded a crucial role in jumpstarting latecomer countries towards the process of industrial development (Korhonen, 1998, 48-66), this opens a rather hopeful horizon for Africa’s future.
However, as the African Development Bank warns, this kind of horizon is not a destiny. It is only a possibility, which may not be realizable. Technological developments, such as robotics and 3D printing, can erode the cost effectiveness of unskilled cheap labour, and keep or redirect simple manufacturing processes to traditionally industrialized countries (AfDB et al., 2014, 14). Yet, neither are these pessimistic possibilities a destiny. With education, state-led industrial policies, creation of reliable administrative and physical infrastructure, including a sufficient electricity supply, and infusion of capital and know-how, speeding up Africa’s industrialization and linking it deeper into the multilayered world economy is completely possible (UNECA et al., 2014). In the long run we probably could be rather optimistic about African development, but we cannot really yet know during which of the future decades we will actually see tangible results of all this.

There is nowadays also a lot of conferencing taking place in and around Africa. Japan started it early in 1993 with the Tokyo International Conference on African Development (TICAD) series, with follow-ups in 1998, 2003, 2008 in Tokyo, and in 2013 in Yokohama. These were large-scale meetings since the beginning, and developed eventually into systematic summit meetings. Connected with TICAD, Japan initiated with Indonesia also the Asia-Africa Forum (AAF), with meetings in 1994 in Bandung, in 1997 in Bangkok, and in 2000 in Kuala Lumpur. The EU and China followed in 2000. The European Union has had summit meetings (EU-Africa Summits) with African heads of states in 2000 in Cairo, in 2007 in Lisbon, in 2010 in Tripoli, and in 2014 in Brussels. China similarly established the Forum on China–Africa Cooperation (FOCAC) in 2000 in Beijing, follow-ups taking place in 2003 in Addis Ababa, in 2006 in Beijing, in 2009 in Sharm El-Sheikh, and in 2012 in Beijing. China started also in 2003 a specific ministerial level Fórum para a Cooperação Económica e Comercial entre a China e os Países de Língua Portuguesa (Forum Macau) with Portuguese speaking countries, four of which are in Africa: Angola, Cape Verde, Guinea Bissau, and Mozambique (Tavares Martins, 2014). Follow-ups have taken place in 2006, 2010 and 2014. India followed in 2008 in the form of the India–Africa Forum Summit in New Delhi, followed by another summit in 2011 in Addis Ababa. The United States has been rather late in focusing on Africa; the inaugural United States–Africa Leaders Summit took place in Washington D.C. in August 2014 (Usman, 2014). Lots of other international conferencing is also taking place regarding Africa and its individual states. Many of these meetings have nowadays a structure resembling that of ASEM, with at least business forums and sometimes also civil society forums connected with them.

There has not been this much international interest in Africa since the days of the European Scramble for Africa in the 1880s. Because most states interested in cooperation with Africa are simultaneously ASEM members, and ASEM seems to be growing larger in practically every meeting, ASEM could in the future take also Africa on its agenda. Because Africa is the focus of so much interest now, and because its needs for infrastructural investment are immense, beginning with the Grand Inga Dam on the Congo river (Taliotis et al., 2014), a concerted international effort, with lots of publicity, would better ensure that also social and environmental aspects are taken care of in this kind of mega project. EU’s policies towards Africa have in the past suffered from the fact that they have been used also as a venue for European self-aggrandizement in the form of projecting its norms on weaker actors in a paternalistic manner (Scheipers et al., 2008). On the other hand, the EU does not behave in this way towards strong actors, such as China, except on a minimal verbal level (Keukeleire et al., 2011). As Mikael Mattlin puts it, these kinds of policies towards big powers are “dead on arrival” (Mattlin, 2012). This may be diminishing, as the prime minister of a major European state has already started preaching against liberalism (McNamara, 2014). Anyway, a concerted effort within the ASEM framework towards Africa probably would balance and harmonize European and Asian approaches, while simultaneously providing economic
and technological basis for effective developmental drives towards Africa. As we saw in our review of the development of the concept of Asia, there is historically no definite boundary between the two regions; the same terms, Asia and Ethiopia, sometimes covering large areas of both since the time of Homer. As ASEM seems to be bound on becoming bigger and bigger, making it truly big might be the best strategy for ensuring its continuing relevance in today’s world governance.


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The Strong Euro: Challenges for the European Central Bank and Implications for the Global Economy

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Abstract

The exchange rate can have important effects on inflation, export performance and growth. Against the backdrop of a strong euro and calls for the European Central Bank (ECB) to lower the common currency’s external value, this article discusses the challenges for the ECB and the Eurozone stemming from a strong euro and weights the arguments for and against currency intervention by the ECB to weaken the euro. We argue that a devaluation strategy is no panacea to the Eurozone’s problems. Macroeconomic imbalances within the Eurozone need to be resolved primarily by structural adjustments. However, a modest euro devaluation and higher inflation in the core countries will facilitate adjustments in the periphery countries. Given that a resolution of the European debt problems and a sustained recovery of the Eurozone is also in the interest of the rest of the world, a modest euro devaluation should not trigger a competitive devaluation spiral.

Keywords

Euro Exchange rate; European Central Bank; Monetary Policy; Foreign Exchange Intervention, Currency Wars.

Note: Paper prepared for the inaugural issue of AEI Insights. Parts of the paper draw liberally from a briefing paper written by the first author for the European Parliament’s Committee on Economic and Monetary Affairs in June 2014 (Belke, 2014).
Introduction

The euro-dollar exchange rate has seen large fluctuations over the past decades (Figure 1). After its creation on 1 January 1999, the euro (EUR) depreciated against the US dollar (USD) from its initial value of 1.9 USD/EUR to 0.83 USD/EUR in October 2001. It then rose to an all-time high of 1.6 USD/EUR in April 2008. Between July and October 2008, with the outbreak of the Global Financial Crisis, the euro dropped by 22%. By October 2009, it had risen again to 1.5 USD/EUR due to its ‘safe haven’ status. With the outbreak of the European debt crisis and speculation on a break-up of the euro area, the euro slumped again below 1.2 USD/EUR by June 2010. After regaining its losses and rising to 1.49 USD/EUR in May 2011, the euro short selling started again so that the euro fell to 1.21 USD/EUR in July 2012. It was only after European Central Bank (ECB) President Mario Draghi uttered the now famous words “[w]ithin our mandate, the ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough” (Draghi, 2012) on 26 July 2012 that the euro regained trust and started rising again. By end-2013, the euro had reached a level of almost 1.4 USD/EUR again. The euro has not only appreciated against the dollar, but also in trade-weighted terms (Figures 2 and 3).

Figure 1: USD/EUR, January 1999-August 2014

Source: Compiled by authors with data from the ECB.
Figure 2: BIS nominal effective exchange rates (monthly averages; 2010=100), January 1999-June 2014

Source: Compiled by authors with data from the BIS effective exchange rate indices (updated 15 July 2014), www.bis.org/statistics/eer/

Figure 3: BIS real effective exchange rates (monthly averages; 2010=100), January 1999–June 2014

Source: Compiled by authors with data from the BIS effective exchange rate indices (updated 15 July 2014), www.bis.org/statistics/eer/
While Draghi’s verbal intervention has been very successful in restoring trust in the euro’s survival and thereby ended speculation against the euro, the renewed strength of the euro has complicated the resolution of Europe’s sovereign debt and growth problems. It is hence no coincidence that the ECB has received numerous calls for intervening in the foreign exchange markets and drive down the euro’s external value. Draghi, like his predecessors, has repeatedly emphasised that the ECB takes into account the level of the euro’s exchange rate only to the extent that it affects the ECB achieving its inflation target of below but close to 2%. During a press conference in Brussels on 8 May 2014 Draghi (2014b) stated:

“...over the last few days we received plenty of advice from political figures, from institutions and, almost every day now, on interest rates, on exchange rates but also, on the other side of the scale, on the excess liquidity. So we are certainly thankful for this advice and certainly respect the views of all these people. But we are, by the Treaty, we are independent. So people should be aware that if this might be seen as a threat to our independence, it could cause long-term damage to our credibility.”

Nonetheless, Draghi and other members of the ECB’s Executive Board have conceded that “[t]here is no doubt that the appreciation of the euro since the summer of 2012 has contributed to the current low level of inflation” (Cœuré, 2014) and that “the strengthening of the exchange rate in the context of low inflation is cause for serious concern in the view of the Governing Council” (Draghi, 2014b). ECB Governing Council member Josef Bonnici warned that “[i]f the exchange rate keeps behaving as it is, if it gets stronger, then it becomes an issue that one has to take into account” (Buell & Lawton, 2014).

When the ECB adopted forward guidance in July 2013,1 the expectation was that this would put downward pressure on the euro exchange rate. As Draghi (2014a) points out “the ECB’s forward guidance ... creates a de facto loosening of policy stance, and real interest rates are set to fall over the projection horizon. At the same time, the real interest rate spread between the euro area and the rest of the world will probably fall, thus putting downward pressure on the exchange rate, everything else being equal.” Against the expectations, the euro, however, continued to strengthen. This is in part due to capital inflows to the euro area reflecting improved fundamentals of the euro area including a growing current account surplus and more benign investor sentiments.

To the extent that “[t]he strengthening of the effective euro exchange over the past one and a half years has certainly had a significant impact on our low rate of inflation, and, given current levels of inflation”, Draghi (2014a) has pointed out that the exchange rate is “becoming increasingly relevant in [the ECB’s] assessment of price stability.” The exchange rate can also have important effects on export performance and thereby growth. Against this background, this article discusses the challenges for the ECB and the Eurozone stemming from a strong euro and weights the arguments for and against currency intervention by the ECB to weaken the euro and possible implications of such a policy for other economies. The next section discusses the challenges arising from a strong euro for the euro area and the ECB’s monetary policy. Section 3 discusses the potential pitfalls of exchange rate intervention. Section 4 concludes.

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1 At its July 2013 meeting the ECB Governing Council stated: "Looking ahead, our monetary policy stance will remain accommodative for as long as necessary. The Governing Council expects the key ECB interest rates to remain at present or lower levels for an extended period of time. This expectation is based on the overall subdued outlook for inflation extending into the medium term, given the broad-based weakness in the real economy and subdued monetary dynamics. In the period ahead, we will monitor all incoming information on economic and monetary developments and assess any impact on the outlook for price stability." (Draghi, 2013)
Challenges arising from a strong euro

There are three channels through which a too-strong euro can harm the Eurozone’s economy. Firstly, an appreciation of the currency lowers the price of imports and puts downward pressure on the inflation rate, which is already too low in the Eurozone. Second, a too-strong exchange rate can hurt exports from the Eurozone and dampen much-needed growth, especially in the Eurozone’s periphery countries which are still struggling to regain competitiveness. Thirdly, through the inflation and growth effects, too strong a euro can hamper the reduction of debt across the Eurozone.

Effects on inflation and challenges for the ECB’s monetary policy

As pointed out by Belke (2014, p.7), “[t]he challenges posed by the strength of the euro for ECB’s monetary policy are to be assessed in a macroeconomic context characterised by overall low inflation levels—stemming from necessary competitive price adjustments in the euro-area periphery as well as a from widespread deleveraging processes still on-going—and improved growth projections in the euro-area.”

Since February 2013, Eurozone inflation has been constantly below 2% and moving ever closer to zero (Figure 4). Inflation rates for food and non-alcoholic beverages have already entered negative territory. Three factors are of particular importance. First, a general fall in global commodity and oil prices has driven down inflation across all advanced economies. According to Draghi (2014d), “it was mostly the declines in the price of oil and food and perhaps some other commodities [since late 2011] that have accounted for something like 75%–80% of the difference between inflation then and inflation now [June 2014].”

Figure 4: Harmonised Index of Consumer Prices (HICP) for the euro area (changing composition)—Overall HICP index and HICP for food and non-alcoholic beverages (annual rate of change)

Source: Compiled by authors with data from the ECB/Eurostat.
The two other factors are specific to the Eurozone (Draghi, 2014c). One is the necessary downward adjustment of prices and wages in the Eurozone’s crisis economies which drags down aggregate inflation.3 As Draghi (2014c) puts it:

“Several euro area countries are currently undergoing internal devaluation to regain price competitiveness, both internationally and within the currency union. The crucial adjustments vis-à-vis other euro area countries have to take place irrespective of changes in the external value of the euro. This process began hesitantly in the early years of the crisis, largely due to nominal rigidities in wages and prices. The result was that adjustment took place more through quantities – i.e. unemployment – than through prices. Stressed countries thus experienced a protracted period of declining disposable incomes and long-drawn-out price adjustment. In this context, several have seen domestic core inflation – that is, excluding the energy and food price effects ... – fall well below the euro area average. For example, the recent overall fall in services price inflation for the euro area is almost entirely accounted for by price declines in these components in stressed countries. Nevertheless, in the last few years relative price adjustment has accelerated in stressed countries. While this may also have initially weighed on disposable incomes, by creating a closer alignment between relative wage and productivity developments, it should increasingly support future incomes through the competitiveness channel. Export growth has been impressive in several stressed countries. And indeed, nominal income growth in stressed countries turned positive in the fourth quarter of 2013.”

The third factor, which is a “common factor” for all Eurozone countries, is the appreciation of the euro exchange rate since July 2012. While internationally traded commodity prices haven’t moved much in dollar terms over this period, the euro’s appreciation has driven down import prices which has fed into falling inflation. Draghi (2014c) emphasises the importance of the exchange rate effect for a relatively open economy like the Eurozone, especially in conjunction with falling global food and energy prices:

“The bulk of the imported downside pressures on euro area consumer prices are explained by the strengthening of the effective euro exchange rate, in particular vis-à-vis the dollar. In the past year or so, oil prices in US dollars have fluctuated – by historical standards – over a relatively narrow range. And they have exhibited no clear downward or upward trend. This creates a balance of forces that might affect future inflation. On the one hand, lower commodity prices driven by euro appreciation help compensate for the generally weak developments in disposable income in the euro area. Indeed, real disposable income declined at a slower pace throughout 2013, and turned slightly positive in the fourth quarter, increasing by 0.6% year-on-year. To the extent that this supports domestic demand in the euro area it will also create upward pressure on inflation. On the other hand, exchange rate appreciation affects external demand and reduces the competitiveness gains of price and cost adjustment in some euro area countries. This has a countervailing effect on real disposable incomes, while also making disinflation more broad-based. Indeed, if we look at prices of non-energy industrial goods, which are mainly tradable, we see a downward trend across all euro area countries.”

Given the ECB’s worries about deflationary effects of a rising euro, and hence the undershooting of the ECB’s inflation target of below but close to two percent, it is not surprising that the ECB has apparently intensified verbal interventions aiming at lowering the external value of the euro since spring 2014. In May 2014, Draghi (2014b) voiced that “the strengthening of the exchange rate in the context of low inflation is cause for serious concern in the view of the Governing Council”. At the August 2014 meeting of the Governing Council, Draghi (2014f) gave the clearest hint to

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3 For a discussion of macroeconomic imbalances as a major cause of the euro crisis see Volz (2013).
date that he would like to see a euro devaluation when saying that “the fundamentals for a weaker exchange rate are today much better than they were two or three months ago.”

**Effects on growth**

While reiterating that “[t]he exchange rate is not a policy target for the ECB”, Draghi (2014e) admitted his concerns in a hearing at the European Parliament in Strasbourg in July 2014 that “[i]n the present context, an appreciated exchange rate is a risk to the sustainability of the [Eurozone’s] recovery”. While the effects of exchange rate appreciation on growth are not straightforward and depend on the structural characteristics of an economy and export and import price elasticities in particular, the general understanding is that exchange rate appreciation will hamper exports and drag down growth. While Imbs and Méjea (2010) find low export elasticities for rich open economies, Bénassy-Quéré et al. (2014, p.7) estimate that for France, the Eurozone’s second largest economy, “a 10% depreciation in the euro in relation to a partner country outside the eurozone increases the value of the average exporter’s sales to this country by around 5-6%”, with most of this effect realised in the same year as the depreciation. Moreover, they estimate that a “10% appreciation in the euro has a symmetrical impact, with the value of exports reduced by an average of 5-6% for an exporting company” (ibid.). The aggregate effect of a 10% euro depreciation may be even larger with 7-8% because new firms may start to export. Overall, Bénassy-Quéré et al. (2014, p.7) estimate that “a 10% depreciation in the euro would result in a 0.6% increase in the French GDP after one year and a 1% increase after two years.” Belke (2014, p.14), in contrast, is more sceptical and points out that “the relation between the long-run interest rate, the exchange rate and in turn, growth, is rather loose”.

**Effects on debt**

By contributing to low inflation (or even deflation) and lower growth rates in the Eurozone, a strong exchange rate can make the reduction of public and private debt overhang more painful and lengthy. Given that most debt is fixed in nominal terms, their real value gets eroded by higher inflation. To overcome the debt overhang and invigorate growth in both the US and Europe, Chinn and Frieden (2011, p.6) advocate to “use a tried-and-true tool to manage crippling systemic debt: inflation.” The argument for reflating the economy to fight a debt overhang was originally put forward by Bernanke (2003) in a speech in Tokyo in 2003:

> “I think the [Bank of Japan] should consider a policy of reflation before re-stabilizing at a low inflation rate primarily because of the economic benefits of such a policy. One benefit of reflation would be to ease some of the intense pressure on debtors and on the financial system more generally. Since the early 1990s, borrowers in Japan have repeatedly found themselves squeezed by disinflation or deflation, which has required them to pay their debts in yen of greater value than they had expected. Borrower distress has affected the functioning of the whole economy, for example by weakening the banking system and depressing investment spending. Of course, declining asset values and the structural problems of Japanese firms have contributed greatly to debtors’ problems as well, but reflation would, nevertheless, provide some relief. A period of reflation would also likely provide a boost to profits and help to break the deflationary psychology among the public, which would be positive factors for asset prices as well. Reflation—that is, a period of inflation above the long-run preferred rate in order to restore the earlier price level—proved highly beneficial following the deflations of the 1930s in both Japan and the United States.”

3 Obviously, inflation will not help in reducing debt when debt is inflation-linked and maturities are short-term.
In a similar vein, Chinn and Frieden (2011, p.6) argue that “as prices rise and wages follow, debtors (house-holds, businesses and governments) find it easier to service their debts and can more readily resume regular economic behavior.” Chinn and Frieden (2011, p.7) acknowledge that inflation would hurt creditors, but they maintain that, “as politically daunting as that might be, some redistribution from creditors to debtors would almost certainly be part of any durable settlement of the Eurozone debt crisis anyway, as it has been in the case of the Greek sovereign debt restructuring.” Likewise, Rogoff (2011) argues that “[i]f direct approaches to debt reduction are ruled out by political obstacles, there is still the option of trying to achieve some modest deleveraging through moderate inflation of, say, 4 to 6 per cent for several years. Any inflation above 2 per cent may seem anathema to those who still remember the anti-inflation wars of the 1970s and 1980s, but a once-in-75-year crisis calls for outside-the-box measures.”

Importantly, Chinn and Frieden (2011, p.11), argue that a slightly higher inflation rate in the Eurozone’s core countries would facilitate adjustment in the periphery:

“Consider the adjustment of labor markets to chronic unemployment. It is widely agreed that in order to create jobs, Spain and other relatively unproductive economies on the southern periphery of the Euro-zone need to reduce real wages. But it is very difficult to impose nominal wage cuts, especially in countries with strong organized labor. By contrast, a bit of inflation could erode real wages, without the perception that labor is being singled out to bear the adjustment burden. We’re not claiming that inflation is a painless way to speed deleveraging. We are claiming, though, that it is less painful than the realistic alternatives. At this juncture, the highest priority for monetary policy in the United States (and, for that matter, in Europe) ought to be getting the economy out of the long, deep recession that has cost trillions of dollars in lost output and disrupted tens of millions of lives. Unusual times call for unusual measures.”

But there are, of course, also critics who maintain that “[t]he idea that inflation can be raised by a controlled amount for a fixed period then easily brought back down again is naive” (Redwood and Bootle as quoted by Buttonwood, 2011).

Problems with exchange rate intervention

Having discussed potential negative side effects of a strong euro exchange rate that may justify further verbal intervention or even intervention in the foreign exchange markets, we now turn to potential drawbacks of such action.

What is the equilibrium level for the exchange rate?

Our starting point is the fundamental insight that the variable driving expenditure switching is not the nominal but the real exchange rate and that there is scarce evidence that central banks are able to affect the real exchange rate durably (Belke, 2014). As pointed out by Belke (2014, p.8-9), the statement “the euro is too strong” necessitates an exact well-founded benchmark, an estimate of the equilibrium exchange rate which corresponds with the ECB’s HICP inflation target. But one can hardly think of a more controversial issue in international macroeconomics than identifying equilibrium exchange rates (Krugman et al., 2012, p.350ff.).

Which factors are driving the euro appreciation? Some analysts try to determine the drivers of the euro’s appreciation by referring to the ECB balance sheets which have been shrinking vis-à-vis the Federal Reserve’s (Fed) and the Bank of England’s (BoE) balance sheet during the previous
year. The significant current account surplus of the euro area as a whole, capital inflows into the euro area’s South, at times falling yields for dollar bonds and shrinking amounts of dollar traded euro-area monetary financial institutions may also have had an impact (Belke, 2014).

Currently, the euro appears too strong for some of the Southern euro-area countries and too weak for a set of Northern euro-area countries, among them Germany. If this can be corroborated, a further fall of the external value of the euro would create windfall gains for countries which are already now faring better in macroeconomic terms (Belke, 2014).

In this context, it is important to assess the extent to which the euro is too strong for a specific euro area member country. For this purpose, for instance Redeker (based on a simple unit labour cost calculus, see Eckert and Zschaepitz, 2014)estimates the USD/EUR exchange rate pain thresholds and ranks the euro area member countries accordingly. The USD/EUR threshold is estimated to be 1.54 for Germany, 1.29 for Spain, 1.28 for Finland, 1.23 for France, 1.19 for Italy, and a very low 1.04 for Greece. The point estimate for Germany turns out to be rather close to the pain threshold of USD/EUR 1.55 which has been calculated by Belke et al. (2013). Accordingly, these studies come up with the conclusion that there is no unique USD/EUR exchange rate to target which is able to “revive the euro-area economy, avoid deflation and preserve the ECB price stability target” (Belke, 2014).

Moreover, the economic literature has often detected destabilising effects from intervention. As highlighted by Belke et al. (2004): “Experience shows that intervention increases the probability of stability only when the rate is clearly misaligned. An additional, and perhaps more striking argument against intervention, is that the factors driving the direction and intensity of exchange rate moves—that is, for instance, expected growth and capital returns—are beyond the reach of monetary policy: apart from the price level it is hard to see how monetary policy can have a systematic impact on the variables which are usually held responsible for exchange rate levels”. Additionally, the standard economic relation among the exchange rate and its fundamental drivers itself conveys the impression to be highly distorted by unconventional monetary policies undertaken by the world’s leading central banks. Hence, it is not at all surprising that the interest rate parity hypothesis does not have much explanatory value for the relatively high external value of the euro in the current macroeconomic scenario of low growth (Belke, 2014).

Finally, reiterated interventions are required to influence the exchange rate durably. However, direct foreign exchange interventions are politically costly. There is thus an incentive for central banks not to intervene in the foreign exchange market. However, the capital markets seem to have understood that the ECB’s unconventional monetary policies are targeted towards the exchange rate (Belke & Gros, 2014). In line with many others, Jolly et al. (2014) observe that “the biggest problem the E.C.B. really faces is the strength of the euro. The Federal Reserve, the Bank of England and the Bank of Japan (BOJ) all set out deliberately to weaken their national currencies … and now the European Central Bank is catching up”.

ECB President Draghi has stressed on several occasions that the external value of the euro can definitely not be considered to represent an ECB policy target. When asked to comment whether the ECB “Governing Council has some kind of a trigger point where the euro exchange rate is too strong, prompting the bank to act in the future” he clearly responded “No, we don’t have a trigger. We just see that this is having the effect of basically depressing further the inflation rate. […] And it’s actually the exchange rate that keeps the inflation rate low and depressed” (Draghi, 2014a).
Devaluations vs. structural adjustments

It can be doubted that employing direct or indirect exchange rate policies to tackle bad growth performance in parts of the Eurozone will provide remedy. High (youth) unemployment and low GDP growth in some euro area member countries are structural phenomena. Besides significant fine-tuning problems, a plethora of studies has demonstrated that a too strong focus has been put on public budget and debt consolidation as compared to increasing international competitiveness of crisis countries (Belke, 2014, p.9-10; Gros et al., 2014). The biggest benefits of a weaker euro would relate to enhancing the euro area’s problem countries’ international competitiveness. If these benefits are later neutralised by higher wage growth, weakening the euro today does not appear to be a solution. If a spiral of devaluations and wage increases sets in, the ensuing unanticipated variability of uncertainty about the (equilibrium) euro exchange rate will have negative economic consequences. This type of macroeconomic environment often coincides with periods of excessive speculation which have the potential to harm the economy because the speculation waves hamper a sound calculation by the export oriented firms” (Belke et al., 2004).

Taking this as a starting point, exchange rate policies backed by discretionary unconventional monetary policies could potentially trigger cumulative destabilising real effects and modify the dynamics of the economy permanently. It has to be added that most of the familiar standard asset price models for sovereign bonds or stocks cannot be used anymore since they do not properly incorporate the dynamic consequences of discretionary central bank interventions. Hence, it seems obvious that the recent appreciation of the euro was significantly driven by speculation about future ECB policy itself. Investors may be willing to test the bottom line of the ECB’s pain threshold for the USD/EUR exchange rate: is it located at 1.30, 1.40 or 1.50 (Belke, 2014; Belke et al., 2004). Overall the best way to calm down currency markets and stop the euro’s upward trend may be for the ECB to refrain from directly or indirectly targeting the exchange rate through its current and future unconventional monetary policy measures (Belke, 2014).

Belke (2014, p.10) maintains that a credible ignorance of the exchange rate level will put both entrepreneurs and politicians under pressure to undertake the necessary structural adjustments instead of hoping for central bank intervention. Moreover, he argues that”[e]specially in the case of negative supply shocks, one should refrain from accommodating devaluations which at best alleviate the short term symptoms of low growth in Europe. Proactive devaluations significantly lower the incentives to break open encrusted structures on labour and product markets and, thus, prospects for growth and employment” (Belke, 2014, p.10).

In the past it has nevertheless often been argued that low international competitiveness due to labour and product market sclerosis connected with low productivity can be counteracted much easier and quicker if the necessary macroeconomic adjustment is triggered through the exchange rate than if it would be conducted via wage cuts. The devaluation of the euro may thus work as a substitute for wage restraint and structural reforms (Belke et al., 2004, Belke et al., 2006). But the empirical evidence on this is mixed at best. For example, the positive employment effects that were claimed as a result of the UK’s and Italy’s exit of the European Monetary System (EMS) in 1992 should be ascribed to the policy reforms that were implemented in these countries at the time rather than the one-off devaluations of the British pound and the Italian lira after their exit from the EMS (Belke et al., 2004). Belke et al. (2004) therefore argue that:

“Hence, in empirical studies investigating the efficiency of exchange rate movements in terms of employment, the extent of reform has to be modelled as an explaining variable which is
endogenous with regard to the choice of the exchange rate system. Then it will immediately become clear that structural reforms and not, as often maintained, proactive devaluations of the respective home currency are the most efficient way towards more growth and employment. Hence, the euro exchange rate cannot be regarded as an important short-term oriented instrument to prevent path-dependence in unemployment in the presence of negative shocks."

But the political pressures to weaken the euro are mounting currently. Above all, the French government is pushing for weakening the euro as the French economy is steadily losing competitiveness and the growth performance of the country is remaining rather poor. Dumping the external value of the home currency has been a policy tool frequently used already in the past to escape more painful structural reforms (Belke, 2014, p. 11). Draghi took a strong stance on this issue at a press conference earlier this year where he said: “We are hearing more and more complaints from Paris about the strength of the euro. Would you like to respond to them at all?” Likewise Cœuré (2014) responded in an interview with le Mode to French calls for euro devaluation: “There is a particular fascination with the exchange rate in France that is not shared by other euro area countries. No doubt this has something to do with the fact that France is one of the only countries in the euro area whose external accounts are in the red. However, the euro area as a whole is running a current account surplus: the solution for France, therefore, is to improve its competitiveness”.

This “case study” displays only a small part of a more general legitimacy and equal representation problem. As highlighted by Belke et al. (2004), “industry representatives ... often speak out in favour of a devaluation policy probably because they expect a group-specific net gain from this devaluation. By this, the determination of exchange rates and thus also, a significant part of the exchange rate variance comes under the influence of political-economic considerations”.

Global currency wars

The Fed, the BoE and the Bank of Japan have been the target of critics who have argued that the primary aim of their quantitative easing (QE) policies is the weakening of their respective exchange rates. In 2010, Stiglitz branded the Fed’s QE policy as a “beggar-thy-neighbour” strategy of currency devaluation: “President Obama has rightly said that the whole world will benefit if the U.S. grows, but what he forgot to mention is... that competitive devaluation is a form of growth that comes at the expense of others... So I think it is likely to present problems for the global economy going forward” (Frangos, 2010). Indeed, strong money outflows from advanced economies looking for higher yields in emerging markets have caused serious financial stability concerns in the latter, which were maybe articulated most prominently by Brazil’s president Dilma Rousseff, who in March 2012 complained about the “monetary tsunami” that was making its way to emerging economies (Volz, 2012).

As noted by Bénassy-Quéré et al. (2014), conflicts may arise when all countries seek to depreciate (or appreciate) their currency at the same time. While concerted efforts by the ECB to devalue the euro could indeed contribute to a “currency war” with competitive devaluations, it should be noted that the ECB has been the only among the major central banks that has thus far refrained from actively debasing its currency. Not only have the Fed, the BoE and the BOJ all openly tried to devalue their currencies, all major emerging market central banks have for long managed exchange rates in order for their economies to remain “competitive”. In East Asia in particular, China and other countries of the region have maintained “competitive” exchange rates under the “East Asian dollar standard”. Although East Asian economies have weathered the Global Financial
Crisis much better that the Eurozone, their willingness to appreciate their currencies even in when their economies were facing the danger of overheating was limited. Since a resolution of the European debt problems and a sustained recovery of the Eurozone is also in the interest of the rest of the world, as this would ultimately boost the Eurozone’s imports volume from the rest of the world again and reduce financial contagion risk, a modest euro devaluation should not lead to a competitive devaluation spiral.

Draghi (2014b) has brushed aside concerns that QE or other policies adopted by the ECB may cause irritation elsewhere: “You know that there is a G-20 statement that says that exchange rate matters are matters of common concern. And so we will have to reflect on this and see. But in our case, certainly, they have an impact on our objective of price stability, and especially, as I said, at this low level of inflation.”

Conclusions
A strong euro has been a worry for many. For the ECB, it is a concern to the extent that exchange rate appreciation has had a negative impact on import prices and thereby contributed to inflation rates much below the ECB’s target range. A strong exchange rate has also been a concern for policymakers, especially in the European crisis economies which have been suffering from a lack of competitiveness, as it has strained European exporters and dampened growth. Moreover, by contributing to lower inflation and suppressing (export) growth, a strong euro may impede and slow the resolution of European debt problems as low inflation keeps real interest rates high and slow growth lessens debtors’ repayment capacity.

For sure, a devaluation strategy is no panacea to the Eurozone’s problems. Macroeconomic imbalances within the Eurozone need to be resolved primarily by structural adjustments. However, a modest euro devaluation and higher inflation in the core countries will facilitate adjustments in the periphery countries. In conjunction with higher wage rises in Germany—as recently proposed by the Bundesbank (2014)—a weaker euro would diminish the need for nominal wage cuts in the periphery countries so that real adjustment there can process less painfully and more smoothly. At the same time, competitiveness of the German economy vis-à-vis the rest of the world would be unchanged as higher wage growth would be compensated by a weaker euro. Given that a recovery of the Eurozone is also in the interest of emerging economies, claims about ‘unfair devaluations’ are not apt.

References


New pattern of East Asian integration: Rise of China and its currency’s role in the regional financial coordination

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Abstract

The rise of China is one of most spectacular events in the global economic and political landscape. More importantly, it can be seen as an emerging of the China-led East Asian regional integration. This paper employs the “flying geese” theory to examine the unique characteristics of emerging new regional integration in East Asia. In this new East Asian regionalism, the Chinese currency is said to become the “key currency” in the region. Thus, this study used several statistical methods to examine the role of Chinese currency in the regional integration. The empirical analysis detected a stable and long-run co-movement between the Chinese Yuan and the Japanese Yen. As a conclusion, the Chinese Yuan has started playing a role of de facto key currency to influence the movement of other regional currencies. These findings could be interpreted as the new pattern of the East Asian regionalism in which the regional momentary and financial coordination would become a main economic policy agenda.

Keywords

Regional integration, China, East Asia, flying geese theory, key currency

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Introduction

The rise of China can be seen as one of the most spectacular historical events in the international economic and political landscape and the global impact of China’s economic might has the potential to be enormous (Jerden & Hagstrom, 2012). In the context of the East Asian regionalism, the rise of China can be interpreted as the change of leading economy in East Asia, from Japan to China. Since the end of the 1970s, China has emerged as the “world’s factory” due to its successful and effective implementation of numerous economic and modernization policies. By contrast, Japan suffered serious economic downturn which was commonly known as the “lost decades” since the 1990s. In other words, the rise of China can be interpreted as an emerging of the China-led East Asian regionalism.

Moreover, a unique characteristic of the East Asian regional integration, in comparison with other prominent regional integrations, such as the European Union (EU), is its relatively hierarchical structure. The EU’s relatively horizontal structure could be seen as a socio-cultural reflection of the independent and individualistic orientation in the region. By contrast, the relatively hierarchical structure in the East Asian economic integration could stem from Asia’s collective orientation by nature. This is the very reason why there is a need to employ an appropriate theoretical framework to examine the historical evolution of the East Asian regional integration.

Thus, this paper employs the “flying geese” model developed by Kaname Akamatsu to analyse the East Asian regional integration (Akamatsu, 1935). The flying geese model is essentially an economic development theory to describe how the “latecomer” would catch up with more advanced economies by growing through stages of economic development, unleashing the power of trades and investments and transforming itself from an “import-substitution” country to an “export-oriented” one by upgrading their technological capacities and innovation mechanism. However, at the same time, the flying geese theory can be applied to examine a historical pattern of the hierarchical, rather than horizontal, regional integration.

In other words, the Akamatsu model seems to provide a more promising analytical perspective to capture a historical pattern of the hierarchical integration in the region. This is mainly because the flying geese model is able to take account of fundamental dynamics and diversity in regional integration in East Asia that covers countries with different stages of economic development. In the region, there are dynamic interactions and interdependencies among countries with three different stages of development, namely, the advanced industrial economies, the rapidly growing developing economies and the least developed economies. First of all, some East Asian economies have reached the most advanced stage of economic development. Among them are Singapore, South Korea, Taiwan and Japan. Secondly, there are other successful developing countries which have maintained relatively steady economic growth with political stabilities. Among them are Indonesia, China, Malaysia and Thailand. Finally, there are a few remaining least-developed East Asian countries that have suffered from low economic growth and political instabilities. Among them are Myanmar, Laos and Cambodia.

1 This paper employs a broader definition of East Asia. It means that East Asia includes Northeast Asia and Southeast Asia.
2 There are numerous theoretical foundations to examine the European Union which is considered as the most successful economic integration in the world. A well-known German economist, Friedrich List (1789-1846) is considered as the frontrunner of the economic integration in Europe (Levi-Faur, 1997). List stressed the importance of freedom of movement, especially free movement of goods and services, in order to promote the country’s prosperity and well-being of people. This theoretical perspective seems to lay a foundation for the European Common Market.
More importantly, the rise of China seems to signify the emerging pattern of new regional integration or the China-led East Asian regional integration. Despite some similarities between previous attempts for the regional integrations and this new regionalism, the most striking difference and interesting feature is the role of currency in the new regional integration. As financial sector’s increasing dominance in the regional business and economic transaction, the leading economy is expected to stimulate the regional economic development through not only the international transaction of goods and services, but also the international monetary transaction. There is little doubt that there has been a close linkage between the regional economic integration and financial coordination in any regionalism. However, the role of currency can be seen as a key factor in the regional integration in East Asia only during the formation of this new regionalism. During the periods of the previous regional regionalisms, the banking and financial sectors had become underdeveloped in the region. In those days, international monetary transaction was a peripheral business activity while banking and financial institutions in the region had normally focused on the domestic retail banking transaction or additional supporting jobs to assist existing customer’s activities in foreign countries. More recently, many Asian banking institutions grew up to become the multinational banking corporations which have conducted numerous banking services across national boundaries and have operated branches all over the region. With this increasing importance of international finance, the leading economy is expected to play an important role to create and stabilize the regional financial system. In this context, the Chinese currency is set to become the “key currency” in the new East Asia regionalism.

Thus, this paper used several statistical methods to examine whether the Chinese currency has played the role of “key currency” in the new East Asian regionalism. The findings from this empirical research would have important policy implication for economic integration around the world. There are two types of approaches to set up the key currency in regional integration. The first approach is that member countries would have normal discussions to choose and create a new currency for the regional key currency. The most prominent example is the Euro’s role in the European Union. Despite the fact of the Deutsche Mark’s relatively dominant position in the economic transaction in the EU, the member countries decided to introduce the new currency – the Euro – as the official currency for the European Monetary Union (EMU). The second approach is that member countries would select a dominant currency as the “key currency” or the “reference currency” in order to stabilize their own currency. A prominent example of the second approach is the Chinese Yuan’s role in the regional integration in East Asia. Without any formal discussion or signing any treaties, the Chinese currency seems to have emerged as the de facto “reference currency” in the region. If the Chinese currency would successfully play a role of the key currency in the region, this could encourage political leaders and central bankers in other economic groupings to adopt the “Chinese” approach, rather than the “European” approach which has come under strong criticism since the European sovereign debt crisis.

Following the introductory section, Section two will examine the historical pattern of regional integration in East Asia before the rise of China. The next section will analyze the new pattern of regional integration or the China-led East Asian regional. Section four will examine empirically whether the Chinese Yuan can play a role of the key currency in the region. The final section is the conclusion.

“The flying geese” theory and East Asian regional integration

The “flying geese” theory was introduced by a well-known Japanese economist, Kaname Akamatsu, in the middle of the 1930s. Akamatsu aimed to use the multi-tier hierarchical pattern or
the “flying geese” pattern of regional integration to capture the dynamic process of regionalism in which industrialization in relatively developed countries would inevitably spread to the relatively less-developed countries (Akamatsu, 1935). In his “flying geese” theory, Akamatsu’s main intention is merely to describe how Japan, the latecomer in East Asia, is able to catch up with the more advanced economies in the West, such as United States, United Kingdom and France. Yet, this theoretical framework of economic development can be used to examine some unique characteristics of regional integration in East Asia.

In the “flying geese” theory of regional integration, there is the multi-tier structure, namely the “leading developed economy”, the “second-tier developing economy” and the “third-tier least-developed economy”. In this structure, the “leading” economy would lead the “second-tier” developing countries. In turn, the “second-tier” economies would play a role to lead the “third-tier” least-developed countries. In this sense, the most interesting characteristics of this regional integration are its hierarchical patterns. In other word, countries in this regional arrangement are not equal partners. Instead, there is a dominant country and its followers. It implies that there is a patron-client relationship between dominant developed country and minor developing countries. Before the rise of China, Japan was a leading economy in the region. The “flying geese” pattern of the East Asian regional integration may offer some explanation for Japan’s arrogant insistence to lead the regionalism in East Asia. Pempel (1996/1997) criticised Japan’s arrogance and asserted that Japan’s permanent place never seemed to have been challenged.

From a historical point of view, there were three attempts to form the “flying geese” pattern of regional integration in East Asia. The first formation of the “flying geese” is Japan’s cruel and failed attempt to form the gaggle of the “flying geese” before the end of World War II. Then, the second formation is another of Japan’s unsuccessful attempt to establish a regional production network after the war. More recently, China has become the global economic powerhouse and the emergence of this new dominant power in the region can be seen as the formation of the third gaggle of the “flying geese”.

In its first attempt, Japan forcefully integrated East Asia by using brutal and cruel military forces. Before and during the war, Japanese military government implemented harmful expansionist and colonialist policies to form a Japan-led regional integration under the “Greater East Asia Co-Prosperity Sphere”. Before World War II, as the “leading economy” in the region, Japan colonized Taiwan, Korea and Manchuria. These countries were considered as the “second-tier countries” in this regional integration. Then, Japan used military forces to invade the other part of East Asia during the war. These occupied countries were seen as the “third-tier countries”. Under the first “flying geese” pattern of East Asian regionalism, Japan brutally and cruelly suppressed the peoples in East Asia.3

The first attempt to form the “flying geese” pattern of the East Asian region ceased to exist in 1945 when the Japanese military junta unconditionally surrendered to the United States and its allies. As a consequence, Japan lost its all former colonies and occupied countries in East Asia. Instead, Japan was occupied by the United States under the leadership of General Douglas MacArthur during the period of 1945-1952. During World War II, the leading country cruelly and brutally inflicted serious damages on its follower countries. In the end, it also suffered from total devastation and destruction that was brought foolishly upon itself. Yet, a fact seems to remain that Japan’s

3 Akamatsu himself witnessed the brutality of the Japanese military policy during the war. He was dispatched as the director of a research department in the Japanese military authority in the Japanese-occupied Malaya.
totally failed expansion policy can be seen as the first attempt to form a regional integration in East Asia. Pempel (1996/1997) comments that the first bid for Asian integration came with the Japanese military junta’s attempt to create the “co-prosperity sphere” in East Asia.

After World War II, Japan used economic force to create the second Japan-led regional integration in East Asia. In this second attempt, Japan made efforts to establish a production network in the region. Dajin Peng observed that the Japan-led production network in East Asia can be seen as an informal economic integration and this regional integration involves no agreements or specific institutional mechanism. Instead, this regional integration is based on the transnational business logic (Peng, 2000).

In the initial stage of this second “flying geese” in East Asia, as the leading economy, Japan successfully exported numerous manufactured goods to neighbouring Asian countries and other countries in the world in the first stage of regional integration. During this stage, some developing countries in East Asia successfully implemented industrial policies and achieved high economic growth. These countries are known as the newly industrializing economies (NIEs) and among them are Hong Kong, Singapore, South Korea and Taiwan. These countries can be seen as the “second-tier” countries in this regionalism. The leading economy established production bases in these countries through foreign direct investment (FDI). In the next stage of the regional integration, these second-tier economies successfully produced competitive products. These countries would export their manufactured goods to other Asian countries and other parts of the world. In the third stage, second-tier countries themselves used FDI to establish their production bases in least-developed countries (i.e. third-tier countries) in the region. In turn, these third-tier countries also successfully industrialized their economies and started exporting their production. Among them are Indonesia, China, Malaysia and Thailand. World Bank praised them as the “East Asian miracle” economies in the beginning of the 1990s (World Bank, 1993).

In this second round of regional integration, Japan adopted the mercantilist policy to establish economic hegemony in the region by using international trades, foreign investment and economic assistance. Saravanamuttu (1988) asserted that the patterns of trades, investments, and aid between Japan and other Asian countries clearly revealed Japan’s strategy of economic penetration in East Asia. He commented that Japan tried to create economic dependence in Asian countries on Japan and to establish economic hegemony in the region. It should be noted that the Japanese government used foreign aid as an important tool to establish the Japan-led economic integration in East Asia. After the war, Japan needed to pay war reparation to East Asian countries since the 1950s. However, Miyashita (1999) argued that Japan used the war reparation payment to re-establish economic ties with countries under the “co-prosperity sphere”. Since the 1960s, Japan became a major provider of foreign aid to East Asian countries. Yet, Katada (2002) claimed that the main objective of Japanese aid was not humanitarian consideration and Japan used the foreign aid to create the production network in the region.

Despite Japan’s suffering from serious economic recession beginning around the end of the 1980s, the Japan-led production network has functioned well until 1997 when the Asian financial crisis broke out in Thailand and spread through other countries in the region. This meant that the sudden bust of the “East Asian Miracle” seemed to signify the end of the second formation of the “flying geese”. Tay (2002) argued that the Asian financial crisis has scattered the flock of flying geese that followed the Japanese way of economic development.
New pattern of regional integration in East Asia

The rise of China has significantly modified the pattern of East Asian regional integration. It signifies the change in the dominant economy in the region, from the declining Japan to the rising China. The emergence of China as a global superpower could be interpreted as the beginning of the third flying geese. In this third gaggle of the flying geese, China is emerging as the leading economy, followed by the “second-tier” economies (South Korea, Singapore, Taiwan and Japan) and the “third-tier” developing countries (other developing countries in the region). As Ahn commented, with China’s increasing importance in the region, the overall direction of economic interdependence is shifted from the Japan-centred production network to the China centred one. China is emerging as the regional hub of international trade and investment as well as the centre of the regional production network. More interestingly, China is emerging as the centre of the inter-industry and vertical economic integration in East Asia (Ahn, 2004).

In other words, the rise of China could be interpreted as an emergence of new “triangle trade” relations in East Asia. As Richard Baldwin pointed out, there were the Japan-centred “triangle trade” relations in which Japan would produce some high tech goods and materials and export them to ASEAN countries, such as Malaysia, Thailand and Indonesia to assemble them to produce the final produce. These ASEAN countries would re-export the final products to the developed countries in North America or Europe (Baldwin, 2008).

However, the China’s integration into a global economy since the beginning of the 1990s has drastically transformed the business landscape in the region into a new form. Ahn pointed out that China has started playing a dominant position in the new triangular relationship of trade interdependence and business transaction in the region. In this new “triangle trade” relations, China would import intermediate high-tech goods from developed economies in the region, such as South Korea, Taiwan and Japan as well as some other materials and low-tech parts from the developing economies in the region, such as Malaysia, Thailand, and Vietnam. After these countries would assemble them and produce final products, China would re-export them to wealthy countries around the world (Ahn, 2004).

On the other hand, the rise of China may affect the role of the United States in the region. Before the rise of China, Japan was the only economic superpower in East Asia and the country had played a quasi-hegemonic role in East Asia during the flights of the first and second “flying geese”. The situation is metaphorically described by T.J. Pempel (1996/1997) as the “Gulliver (Japan) in Lilliput (East Asian economies)”. In this context, East Asian countries welcomed US involvement in the region as a balancing role to check Japan’s regional ambition (Beeson, 2001). Despite its economic strength in the global economy, Japan never repeated the same mistake as before the war and upheld and supported the international order that was created and maintained by the West. By contrast, according to Ikenberry (2008), some researchers have showed concerned about China’s hegemonic role in Asia and its ambition to reshape the international order to serve its national interest. They predicted that there could be an intense rivalry and possible conflict between the “rising hegemon” (China) and the “declining hegemon” (United States) in Asia. In this scenario, there is a possibility that the new regional integration could pose a threat to the existing international security system. Mearsheimer warned that, as China’s economy would continue to grow, China would try to dominate Asia by maximising the power gap between China and other neighbouring countries while the United States would maintain its hegemonic power over the Western hemisphere. In the end, China and United States would engaging intense security competition (Mearsheimer, 2006).
It should be noted that unity in the previous formations of the “flying geese” pattern of regional integration was maintained through the usage of power. The military power was forcefully used before and during the war. After the war, economic power was used to establish the production network in the region. In the China-led regional integration, another power, international financial power, would play a significant role for the establishment of the regional integration. In other words, the important role of Chinese currency in the East Asian regionalism is a new and unique characteristic of the third flying geese. During Akamatsu’s lifetime, the international finance in the region, especially international monetary transactions between East Asian economies, were still underdeveloped. Akamatsu witnessed the successful performances of the Asian Newly Industrializing Economies and the second “flying geese” and he is able to modify and deepen his theory to fit the economic reality of East Asia at that time. Unfortunately, he was unable to live long enough to witness the rise of China and increasing importance of the international financial transactions in the region to modify his “flying geese” theory that is based on regional movement of trades and investment.

The role of the Chinese Yuan as a key currency drew international media attention. The leading economic newspaper, *The Economist*, published an interesting and thought provoking article entitled “The Rise of Yuan”. The newspaper argued that the Chinese Yuan seems to take over the role of the “key currency” in the Asia after the European currency crisis in the end of the 2000s. There are several Asian currencies which indicated a high degree of co-movement with the Chinese currency (*The Economist*, October 20, 2012). It means, without conducting any formal discussion or signing any treaties, the Chinese currency seems to be emerging as a *de facto* “key currency” in the region. In other words, the leading economy in the third flying geese would lead other countries in the region through not only international trade and investment, but also international monetary transactions. If the Chinese Yuan would play an important role in regional economic integration, this fact could encourage political leaders and central bankers in other economic groupings to adopt a pragmatic and informal “Chinese” approach, rather than the treaty-based and formal “European” approach.

**Can the Chinese Yuan be the key currency in the region?**

This section empirically examines the role of Chinese currency in China-led economic integration in East Asian. In other words, it would analyze whether the Chinese currency could play a role of regional “key currency” in the East Asia. It used the co-movement of the Chinese Yuan (CNY or Renminbi) with major East Asian currencies, such as the Japanese Yen (JPY), the Korean Won (KRW), the Malaysian Ringgit (MYR), the Singapore Dollar (SGD) and the Thai Baht (THB) as a proxy to capture China’s leadership role in the region. In other words, the higher degree of co-movement between the CNY and other East Asian currencies can be seen as an empirical proof that the Chinese Yuan would play a leading role of the “key currency” in the international monetary regime in East Asia.

This paper used the national currency per the Special Drawing Rights (SDRs) from January 2007 to March 2011 to measure the movements of the exchange rates in the Asian countries after the European currency crisis. The main source of data is the International Financial Statistics (IFS) from the International Monetary Fund (IMF, 2014). The data were transformed into logarithms. The co-movements between Chinese Yuan and the other East Asian currencies are shown in Figure 1. This paper used the following statistical methods to examine the possibility of the third

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4 The Special Drawing Rights (SDRs) are foreign exchange research assets maintained by the International Monetary Fund (IMF). SDR is not currency, but it is a claim to currency held by the IMF member countries.
flying geese in East Asia, 1) correlation analysis, 2) unit root analysis, 3) cointegration analysis and 4) causality analysis.

Firstly, the Pearson correlation analysis is used to measure the dependency between Chinese currency (CNY) and other Asian currencies. Empirical findings from correlation analysis are reported in Table 1. The findings clearly indicate that the Chinese currency has a strong relationship with other Asian currencies, except Korean currency. There is an especially strong relationship between Chinese currency and three Asian currencies, namely the Japanese Yen (JPY), the Singapore Dollar (SGD) and Thai Baht (THB).

Secondly, unit root test is used to examine the stationarity of data sets. If there are co-movements between two variables, the order of integration between variables should be the same. This paper uses the augmented Dickey-Fuller (ADF) unit root test to investigate the stationarity (Dickey & Fuller, 1979) of four currencies time series, namely, the Chinese Yuan, the Japanese Yen, the Singapore Dollar (SGD) and Thai Baht (THB). The Korean Won and the Malaysian Ringgit are excluded from analysis because these currencies do not seem to have strong positive association with Chinese currency. The empirical findings from unit root tests are reported in Table 2. The findings clearly indicate that all four currencies, except the Singapore Dollar (SGD) are integrated of order one or $I(1)$. This means that these three currencies, namely, the Chinese Yuan, the Japanese Yen (JPY) and the Thai Baht (THB) have the same order of integration. The Singapore Dollar should be excluded from further analysis due to the fact that the currency did not seem to be integrated of order one.

Thirdly, the Johansen cointegration test is used to examine the long-run cointegration relations or co-movement between three Asian currencies, namely, the Chinese Yuan, the Japanese Yen (JPY) and the Thai Baht (THB). The empirical findings from the cointegration analysis are reported in Table 3(a) and Table 3(b).

According to findings from the Johansen cointegration analysis, there is a long-run cointegration relation between the Chinese Yuan (CNY) and the Japanese Yen (JPY). In other words, there are strong association and co-movement between the Chinese Yuan and the Japanese Yen in the long-run. On the other hand, findings indicate that there is no cointegration relation between the Chinese Yuan (CNY) and the Thai Baht (THB). In other words, empirical finding does not seem to indicate the co-movement between the Chinese Yuan and the Thai Baht. The co-movement between the Chinese Yuan (CNY) and the Japanese Yen (JPY) could be expressed as:

$$\ln CNY = 1.060 \ln JPY + 0.016 \text{Trend}$$

This co-movement equation or the cointegrating vector equation indicates that there exists a positive long-run relationship between the Chinese Yuan and the Japanese Yen. This equation can be seen as another empirical proof for the co-movement between the CNY and JPY. In other words, the Chinese currency could also appreciate against the SDRs if Japanese currency would appreciate against the SDRs. The highly correlated co-movement between the Chinese Yuan and the Japanese Yen is shown in Figure 2.

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5 There are several definitions of the “strong correlation”. The well-accepted definition of the strong correlation is that correlation coefficient between two variable should be equal to or greater than 0.5 (Cohen, 1988).
Finally, this paper examines the causal relationship between the Chinese Yuan and the Japanese yen by employing the Granger causality test (Engle & Granger, 1987). The empirical findings from the Granger causality test are reported in Table 4. The findings show that the error correction term is statistically significant and positive. This means that there is long-run Granger causality between the Chinese Yuan and Japanese Yen. In other words, the long-run Granger causality did confirm that there exists the long-run equilibrium relationship between two currencies. Moreover, as the results of the chi-square tests indicate, the Granger causality between the Chinese currency and the Japanese currency has been detected in the short-run. This means that the change in the exchange rate in the Chinese currency would influence Japanese currency.

In short, the most important and intriguing implication of this empirical analysis is that the Chinese Yuan plays a significant role of key currency to influence the movement of the Japanese Yen. In other words, the findings have provided empirical evidence that the Chinese currency could be considered as a regional key currency that would lead other regional momentary authorities to adopt the Chinese financial policy. These findings could be interpreted as the new pattern of the East Asian regionalism in which the regional momentary and financial coordination would become a main economic policy agenda.

**Concluding remarks**

The fundamental pattern of regional integration in East Asia is its hieratical structure. In other words, there has been a dominant economy that would lead remaining countries in the region, rather than more horizontal regional integration, such as the European Union, in which member countries are equal partner. From a historical perspective, there have been three attempts to integrate the East Asian countries. Before the Rise of China, Japan made two unsuccessful attempts to create East Asian regionalism before and after the Second World War.

The rise of China seems to signify a change of the leading economy in East Asia. More importantly, it can be seen as the formation of the China-led East Asian economic integration. This paper used several econometric methods to examine the possibility of the third flying geese in the East Asia. The empirical findings indicate that there is a long-run co-movement between the Chinese Yuan and the Japanese Yen. As a conclusion, the Chinese Yuan plays a central role as key currency to influence the movement of the Japanese Yen.

The most important policy implication is that the empirical findings confirmed that important role of currency in the regional integrations in East Asia. Since the European sovereign debt crisis broke out, the “European” approach, that introduced a new currency as key currency in the regional integration, came under strong criticism. Instead, East Asian countries’ monetary authorities seem to choose the Chinese Yuan as the de facto key currency which could be a relatively more effective and pragmatic choice for regional monetary integration.

The findings of this paper confirm the importance of China as the leading economy in East Asian economic integrations. For a future study, there is still a need to conduct further empirical analysis on the co-movement between national income, industrial productions, and inflation rates and other macroeconomic variable in order to examine the rise of China in the context of the East Asian regionalism. Furthermore, this paper focused on the hieratical structure of East Asian economic integration. The future may compare and contrast some similarities and differences between Asian and other regions’ regionalisms, such as the European Union (EU), the North American
Free Trade Agreement (NAFTA) and the Southern Common Market Treaty (MERCOSUR). Such comparative research would provide much-awaited insight and understanding of the intricate nature of regional integration in East Asia and beyond.

References


**Appendix 1**

**Figures, Tables and Statistical Tests**

(a) Co-movement of currencies in East Asia

Figure 1: The co-movement of Asian Currencies from 2007 to 2011

![Figure 1: The co-movement of Asian Currencies from 2007 to 2011](image_url)

Notes: The co-movement among six Asian currencies, namely the Chinese Yuan (CNY), the Japanese Yen (JPY), the Korean Won (KRW), the Malaysian Ringgit (MYR), the Singapore Dollar (SGD) and the Thai Baht (THB) from January 2007 to March 2011. Source: IMF (2014)
Figure 2: Co-movement of the Chinese Yuan and the Japanese Yen

Notes: The co-movement between the Chinese Yuan (CNY) and the Japanese Yen (JPY) from January 2007 to March 2011.
Source: IMF (2014)

Appendix 2

Statistical analysis

(a) Pearson correlation test

The Pearson product-movement correlation coefficient can be calculated by:

\[ r = \frac{\sum (X - \bar{X})(Y - \bar{Y})}{\sqrt{\sum (X - \bar{X})^2 \sum (Y - \bar{Y})^2}} \]  

where \( \bar{X} \) is the mean value for \( X \) and \( \bar{Y} \) is the mean value for \( Y \). The Pearson correlation coefficients between the Chinese currency and other East Asian currencies are reported in Table 1.

Table 1: Correlation between Chinese currency (CNY) and other Asian currencies

<table>
<thead>
<tr>
<th>Currency</th>
<th>JPY</th>
<th>KRW</th>
<th>MYR</th>
<th>SGD</th>
<th>THB</th>
</tr>
</thead>
<tbody>
<tr>
<td>Correlation coefficient</td>
<td>0.922</td>
<td>-0.825</td>
<td>0.423</td>
<td>0.702</td>
<td>0.607</td>
</tr>
</tbody>
</table>
(b) Unit root test

The ADF test is based on the following regression,

\[ \Delta y_t = \alpha + \beta t + \gamma y_{t-1} + \sum_{i=1}^{n} \delta_i \Delta y_{t-i} + \varepsilon_t \]  

where \( y \) is variable of interest, \( t \) is a linear time trend, \( \Delta \) is the difference operator, \( \beta \) and \( \delta \) are coefficient parameters, and \( \varepsilon_t \) is the error term. The ADF tests tend to be sensitive to the choice of lag length \( n \) which is determined by minimising the Akaike information criterion (AIC) (Akaike 1974). The AIC criterion is defined as:

\[ AIC(q) = T \ln\left( \frac{RRS}{n-q} \right) + 2q \]  

where \( T \) is the sample size, \( RRS \) is the residual sum of squares, \( n \) is lag length, \( q \) is the total number of parameters estimated. The findings from the unit root analysis are reported in Table 2.

Table 2: ADF unit root test

<table>
<thead>
<tr>
<th></th>
<th>Levels</th>
<th>First Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Constant without trend</td>
<td>Constant with trend</td>
</tr>
<tr>
<td>CNY</td>
<td>-1.717(0)</td>
<td>-2.978(1)</td>
</tr>
<tr>
<td>JPY</td>
<td>-0.784(2)</td>
<td>-3.264(1)</td>
</tr>
<tr>
<td>SGD</td>
<td>1.025(0)</td>
<td>-1.509(1)</td>
</tr>
<tr>
<td>THB</td>
<td>-0.738(0)</td>
<td>-1.713(0)</td>
</tr>
</tbody>
</table>

Notes: Figures in parentheses indicate number of lag structures that minimize the Akaike Information Criterion (Akaike, 1974). Maximum lag length is set as three.

** indicates significance at 1% level, * indicates significance at 5% level.

c) Cointegration test

The Johansen cointegration test is based on maximum likelihood estimation of the K-dimensional Vector Autoregressive (VAR) model of order \( p \),

\[ Z_t = \mu + A_1 Z_{t-1} + A_2 Z_{t-2} + \ldots + A_p Z_{t-p} + \varepsilon_t \]  

where \( Z \) is a \( k \times 1 \) vector of stochastic variables, \( \mu \) is a \( k \times 1 \) vector of constants, \( A_i \) is \( k \times k \) matrices of parameters, and \( \varepsilon_t \) is a \( k \times 1 \) vector of error terms. The model could be transformed into an error correction form:
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\[ \Delta Z_t = \mu + \Pi Z_{t-1} + \sum_{j=1}^{p-1} \Gamma_j y_{t-j} + \epsilon_t \]  

(A5)

where \( \pi \) and \( \Gamma_j \ldots, \Gamma_{k+1} \) are \( k \times k \) matrices of parameters. On the other hand, if the coefficient matrix \( \pi \) has reduced rank, \( r < k \), then the matrix can be decomposed into \( \pi = \alpha \beta' \). The Johansen cointegration test involves testing for rank of \( \pi \) matrix by examining whether the eigenvalue of \( \pi \) is significantly different from zero. There could be three conditions: 1) \( r = k \), which means that the \( Z_t \) is stationary at levels, 2) \( r = 0 \), which means that the \( Z_t \) is the first differenced Vector Autoregressive, and 3) \( 0 < r < k \), which means there exists \( r \) linear combinations of \( Z_t \) that are stationary or cointegrated.

This paper uses the Trace (Tr) eigenvalue statistics (L-max) for the cointegration analysis (Johansen 1988; Johansen and Juselius 1990). The likelihood ratio statistic for the trace test is:

\[ F = -T \sum_{i=r+1}^{p-2} \ln(1 - \hat{\lambda}_i) \]  

(A6)

where \( \hat{\lambda}_{r+1} \ldots, \hat{\lambda}_p \) are the smallest eigenvalue of estimated \( p - r \). The null hypothesis for the trace eigenvalue test is that there are at most \( r \) cointegrating vectors. The null hypothesis for the maximum eigenvalue test is that \( r \) cointegrating vectors are tested against the alternative hypothesis of \( r + 1 \) cointegrating vectors. If trace eigenvalue test and maximum eigenvalue test yield different results, the results of maximum eigenvalue test should be used because power of maximum eigenvalue test is considered greater than the one of trace eigenvalue test (Johansen and Juselius 1990). The empirical findings from cointegration analysis are reported in Table 3(a) and Table 3(b).

**Table 3(a): Cointegration analysis between CNY and JPY**

<table>
<thead>
<tr>
<th>Eigenvalue</th>
<th>Trace statistic</th>
<th>5 percent critical value</th>
<th>Number of co-integrating equations</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.813</td>
<td>37.097</td>
<td>25.872</td>
<td>None*</td>
</tr>
<tr>
<td>0.396</td>
<td>8.594</td>
<td>12.517</td>
<td>At most 1</td>
</tr>
</tbody>
</table>

The results are based on a VAR with one lags, an intercept and a trend in the cointegration equation.

**Table 3(b): Cointegration analysis between CNY and THB**

<table>
<thead>
<tr>
<th>Eigenvalue</th>
<th>Trace statistic</th>
<th>5 percent Critical value</th>
<th>Number of co-integrating equations</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.629</td>
<td>21.586</td>
<td>25.872</td>
<td>None</td>
</tr>
<tr>
<td>0.242</td>
<td>4.728</td>
<td>12.517</td>
<td>At most 1</td>
</tr>
</tbody>
</table>

The results are based on a VAR with one lags, an intercept and a trend in the cointegration equation.
(d) Causality test

The Granger-causality is based on the following Vector Error Correction Model (VECM).

\[ \Delta \ln JPY_t = b_1 + \sum_{i=1}^{n} b_2 \Delta \ln JPY_{t-i} + \sum_{i=1}^{n} b_3 \Delta \ln CNY_{t-i} + b_4 u_{t-1} + \varepsilon_t \]  

where \( u_{t-1} \) is the lagged error correction term and \( b \) is coefficient parameter, \( JPY_t \) is the exchange rate of Japanese Yen at time \( t \) and \( CNY_t \) is the exchange rate of Chinese Yuan at time \( t \). This paper uses the Granger-causality test based on the VECM instead of the standard Granger-causality tests. There are two advantages to using this method rather than the standard Granger causality test, i.e., 1) the \( F \)-test of the independent variables indicates the short-run causal effect, and 2) significant and negative error correction term indicates the long-run causal effects. The findings from the causality test are reported in Table 4.

Table 4: Granger-Causality Test based on VECM

<table>
<thead>
<tr>
<th>Dependent Variable: ( \Delta \ln JPY )</th>
<th>Chi-square statistics</th>
<th>P-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>( \Delta \ln CNY )</td>
<td>3.861</td>
<td>0.046</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Coefficient</th>
<th>t-statistic</th>
</tr>
</thead>
<tbody>
<tr>
<td>( U_{t-1} )</td>
<td>2.042</td>
</tr>
</tbody>
</table>

Note: To test for causality when variables are co-integrated, the following Granger causality test based on the VECM could be used:

\[ \Delta \ln JPY_t = b_1 + \sum_{i=1}^{n} b_2 \Delta \ln JPY_{t-i} + \sum_{i=1}^{n} b_3 \Delta \ln CNY_{t-i} + b_4 u_{t-1} + \varepsilon_t \]

Short-run causality: the joint significance of the coefficients is determined by the F-test

Long-run causality: the level of significance for error correction term is determined by the t-statistics.

The results are based on a VECM with one lag.
Trade Disputes, Inter-Regional Free Trade agreements, and the Ukraine Crisis: The Geopolitical Implications for the EU-China Bilateral Trade Relations

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Abstract

This paper examines three critical issues concerning the EU-China bilateral trade relations. First, it analyzes the contentious dynamics of trade disputes between the EU and China over rare earths and solar panels. Secondly, it discusses geopolitical implications of inter-regional free trade agreements (FTAs) such as the Trans Pacific Partnership (TPP) and the Transatlantic Trade Investment Partnership (TTIP). Thirdly, it explores the impacts of the Ukraine crisis on the bilateral economic development. The paper argues that with China’s growing market power, China has responded to the European Unions’ anti-dumping and anti-subsidy measures in an equally assertive manner by filing retaliatory investigations into several imports from the EU. With the threat of reprisal such as blocking EU access to China’s growing market, Beijing has successfully negotiated compromised solutions to the trade disputes. With regard to the geopolitical implications of TPP, TTIP and the Ukraine crisis, it notes that these events may provide a renewed momentum for China and Russia to forge stronger economic ties among the BRICS (Brazil, Russia, India, China and South Africa) and to rally other nations in Asia and Latin America to join alternative trade blocs.

Keywords

World Trade Organization (WTO); China-Europe Trade; Free Trade Agreement (FTA); Global Governance; Regionalism; Trans-Atlantic Trade and Investment Partnership (TTIP); Trans-Pacific Partnership (TPP)

Introduction

This paper examines the EU-China bilateral trade relations since 2010. The significance of EU-China economic cooperation cannot be overemphasized enough since its bilateral trade amounts to $1 billion per day. Today, the European Union (EU) and China depend on each other as the biggest source of their imports. As for trade balance, China exports more to the EU ($334 billion exports) than it imports ($212 billion imports from EU) (European Commission, July 2, 2014). Although the EU is China’s biggest export destination, the EU accounts for only 14.1 percent of
China’s total foreign trade as of 2012. Concerned with a large trade deficit with China as well as troubled by Europe’s slow economic recovery from the Euro-zone crisis since 2009, EU has been keen on limiting China’s export to Europe while seeking to pry open China’s market for EU investors. While the EU and China began to negotiate an EU–China Investment Agreement in 2013, they were at the same time embroiled in serious trade disputes that at times seriously constrained the bilateral relations. For instance, the EU launched anti-dumping (AD) and anti-subsidy (AS) investigations into Chinese firms on numerous occasions. In 2013 alone, the EU and China had trade disputes over rare earths, solar panels, telecommunication, seamless steel tubes and pipes, wine, toluidine, automobiles, and rice products. Fortunately, most trade disputes, except rare earths, ended with compromises and concessions from both sides in 2014. Notwithstanding the signs of improving bilateral ties this year, two recent geopolitical developments in the international relations will have significant impacts on the EU–China bilateral relations. The first event of geo-political significance is the on-going negotiations for inter-regional free trade areas such as the Transatlantic Trade Investment Partnership (TTIP), the Trans Pacific Partnership (TPP), and the Regional Comprehensive Economic Partnership (RCEP). The second event of international importance is the current Ukraine crisis and EU sanctions against Russia. Many political analysts caution that TPP and TTIP may engender competitive regionalism by pressuring China and other emerging economies to seek an alternative venue for trade expansion. As for the EU sanctions against Russia, many observers note that the sanctions may provide greater business opportunities for China.

Examining the EU–China bilateral trade relations, this paper focuses on the political implications of three issues: the recent trade disputes, inter-regional free trade deals, and the Ukraine crisis. Key contentions of this paper, concerning the implications of the three issues, are as follows. First, in the case of bilateral trade disputes, market power enables a country to use or to resist the World Trade Organization’s (WTO) regulations to its advantage. The WTO has no direct enforcement mechanism but merely authorizes an appropriate sanction to be applied by the complainant. The ability to compel the violator to comply to WTO rules is hinged upon the complainant’s market power. Conversely, the ability to resist WTO rulings deemed unfair is also dependent on the market power of the accused. In other words, market power is the ability of the country to retaliate by limiting the other party’s access to its market. In the case of EU–China disputes over rare earths, China uses its market power to resist WTO decisions. With regard to the solar panel dispute, China used carrot and stick measures (market access or market denial) to induce the EU to make compromises. The second contention is that TPP and TTIP will likely bring out competitive regional trade blocs. The three inter-regional FTA negotiations (including TPP, TTIP and RCEP) boil down to the contest of rule-setting power. As China worries that TTIP will undermine China’s ability to set trade rules in the global economy, Beijing is encouraging competitive regional trade blocs, counter to the EU and US-centered ones. The third contention concerns the impact of the Ukraine crisis on the EU–China bilateral relations. The Ukraine crisis is likely to create more trade opportunities for China and thus it will further strengthen China’s market power. As the Ukraine crisis brings Russia closer to China and other BRICS nations, the EU’s ability to compel China to enter into trade agreements more favourable to the EU seems to be rather limited.

The organization of this paper is as follows. First, with a case study of recent EU–China trade disputes over rare earths and solar panels, this paper discusses the significance of China’s market power in international trade disputes. Secondly, it examines the implications of inter-regional FTAs such as the TTIP (Transatlantic Trade and Investment Partnership) and the Ukraine crisis for
the EU–China bilateral trade relations. In the context of Sino–US rivalry in Asia and EU–Russia rivalry in Europe, it discusses trade challenges and opportunities for the EU and China.

**Trade Dispute I: Rare Earths**

The EU, the USA, and Japan filed a complaint to the WTO concerning China’s export restrictions on rare earth metals in 2010. It is argued that violating WTO rules, China purposely limits the export of rare earths mainly through export quotas. It should be noted that rare earth metals are highly sought minerals for modern technology. Rare earth materials contain unique properties that are essential to produce many consumer products such as “wind power turbines, catalysers (for car and oil cracking), energy-efficient bulbs, engines for electric and hybrid vehicles, flat screens and displays (LED, LCD, plasma), hard drives, car parts, camera lenses, glass applications, industrial batteries, medical equipment or water treatment” (European Commission, 13 March, 2012). Since China supplies 90% of rare earths to the world market, it is not surprising that China’s export control has raised serious concerns among developed countries that are dependent on the export of high-tech goods. As EU Trade Commissioner Karel De Gucht put it,

> China’s restrictions on rare earths and other products violate international trade rules and must be removed. These measures hurt our producers and consumers in the EU and across the world, including manufacturers of pioneering hi-tech and ‘green’ business applications” (European Commission, 13 March, 2012)

The WTO Appellate Body ruled that China violated the WTO regulations concerning export control and thus it asked China to drop its export quotas on rare earths. Despite the WTO ruling and the EU’s claims about China’s unfair trade practice, it should be noted that WTO trade rules on export control are fundamentally unfair for China. With regard to trade in natural resources, WTO has different rules for its members. More than 140 members enjoy almost “complete freedom to restrict exports” (Qin, 2012). Only some new WTO Members, such as China and Mongolia, have been required, as part of the terms of their accession to the WTO, to give up their rights to control the export of certain natural resources. In essence, WTO regulations concerning export control are biased against the late accession members (Karapinar, 2011).

**Table 1. Rare earth reserves and supplies in the world (Source: Global Times, March 27, 2014)**

<table>
<thead>
<tr>
<th>Country</th>
<th>Total World Reserve (%)</th>
<th>Supply (%) to the world market</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>13%</td>
<td>No supply</td>
</tr>
<tr>
<td>China</td>
<td>23% reserve</td>
<td>90%</td>
</tr>
<tr>
<td>India</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>Australia</td>
<td>5%</td>
<td>No supply</td>
</tr>
<tr>
<td>Russia</td>
<td>19%</td>
<td>No supply</td>
</tr>
</tbody>
</table>

As table 1 shows, the USA, Australia and Russia do not supply any rare earths although they have a combined total 37% of the world rare earths reserves. As China provides a disproportionately large amount of rare earths, 90% of the world total supply, it is understandable that China is concerned about environmental and economic implications of its fast depleting precious natural resource.
Since 2010, China imposed strict export quotas on its rare earths on the ground of concerns for environmentally sustainable development.

When China’s market power was negligible, China had to accept the unfair accession requirements imposed by WTO in order to gain access to the world market. With China’s growing market power, however, China’s attitude toward WTO has changed over time from one of passive followers to an assertive challenger. Beijing appealed against the WTO ruling but WTO upheld its initial decision in 2014. China regretted the WTO rejection of China’s appeal and announced that it will continue to adopt necessary measures to ensure China’s sustainable development. The necessary measures are reported to include better administration of rare earth production through technological upgrades and the restructuring of the Chinese domestic rare earth industry as well as resource taxes on rare-earth sales rather than outright quota restrictions (Global Times, August 12, 2014). This means that China is not willing to blindly follow WTO rules at the expense of its own development. It also means that tensions between the EU and China over rare earths will continue in coming years. This not-so-pliant, challenging posture has also shown in other recent trade disputes between China and the EU.

Trade Dispute II: Solar Panels

In November 2012, the EU launched an anti-subsidy (AS) and anti-dumping (AD) investigation into Chinese solar products. As discussed below, the threat of EU’s punitive tariffs (anti-dumping and countervailing tariffs) on Chinese solar panels provoked a series of retaliatory trade measures from Beijing. The prospect of losing EU’s solar market is not something that Beijing would accept without a fight. China is the world largest solar panel supplier and the EU is the world’s largest solar market. As of 2011, China exported $27.89 billion worth of solar products to the EU, accounting for 70 percent of China’s total solar product exports and 7 percent of the total trade volume between China and EU (Beijing Review, 26 June, 2013). Globally, Chinese manufacturers exported a total of 22–23 GW of solar modules in 2013 that accounted for two thirds of the total global demand, 35 GW (Reuters, 9 August, 2013).

According to the WTO, anti-dumping (AD) and anti-subsidy (AS) duties are legitimate measures to reduce exports from a country that allegedly committed dumping practices. Anti-dumping and anti-subsidy claims are, however, highly controversial because evidence data for dumping and subsidy practices can be easily manipulated (Stone, 2011). As Stone put it, “in practice anti-dumping actions have come to be a respectable way for WTO members to apply short-term trade protection” (Stone, 2011, p.89). Many scholars also point out that anti-dumping and anti-subsidy duties are convenient devices for short-term trade protectionism as well as a political tool to garner popular support. For instance, Vermulst and Gatta (2012) find that AS charges are politically palatable to politicians who seek to score easy political points in their domestic constituencies. The main reason is that AD and AS allegations usually invoke the idea that domestic economic losses are mainly due to aggressive and unfair foreign exporters, not due to the lack of domestic

1 According to the Article VI of General Agreement on Tariffs and Trade (GATT), dumping occurs when a country exports products in another country at a lower price than in its own market “and as a direct result, it causes substantial "material injury to" the relevant industry in the importing country. (Lee, Park and Cui 2013) There has been considerable research into multifaceted aspects of AD and AS related actions (Breton 2001; Staiger et al 1994; Harpaz 2011; Vandenbussche and Hylke 2013). As noted by many, government subsidy can lead to dumping practices. Hence, anti-dumping investigation is often accompanied by anti-subsidy investigation. Governments retaliate when the competitiveness is threatened by a subsidy that another country pays domestic producers. A countervailing duty is an additional tariff placed on an imported product that a nation believes is receiving an unfair subsidy.
firms’ competitiveness. Sometimes countries strategically use AD and AS investigations “for the sake of punishing aggressive foreign exporters and sending off warning signs” (Tran, 2012). Relating to the political nature of AS and AD, another equally important fact is power disparity in the use of AS and AD. Many scholars argue that powerful countries find anti-dumping measures “more useful instruments than weak countries, because powerful countries are less subject to retaliation” (Stone, 2011). Not so surprisingly then, the EU and the USA are the most frequent users of anti-dumping laws while China has been and still is one of the most targeted country for antidumping and anti-subsidy investigation. Between 1995 and 2011, the total 4,010 antidumping investigations were initiated globally and 853 cases were laid against the People’s Republic of China (PRC), accounting for 21% of the total number of global antidumping investigations (Lee, Park & Cui, 2013). But in recent years, emerging economies have shown their willingness to resort to WTO anti-dumping laws. Feinberg (2013) finds that between 2008 and 2010, the top three users of antidumping, which filed 43 percent of all global cases, were India, Brazil, and Argentina. Likewise, China’s share of AS/AD filing is on the rise. China’s responses to AD and AS measures have changed over time. Initially, China kept a low profile and did not retaliate nor sought to resort to the WTO Appellate body to resolve disputes. However, with China’s growing market power, PRC’s attitude toward trade disputes has become more assertive. Beijing now retaliates with AS and AD laws enshrined in WTO against countries that initiate AD and AS investigations into Chinese firms. For instance, from 2003 to September 2012, China had launched a total of 131 anti-dumping investigations and five anti-subsidy investigations (Beijing Review, 10 December, 2012).

Reflecting China’s assertive attitude toward WTO (traditionally dominated by the USA and the EU), Beijing has recently used AS/AD measures to settle solar trade disputes with the EU. In response to EU’s initial AS and AD investigations into Chinese solar panels, Beijing decided to launch an anti-subsidy investigation into solar grade polysilicon (the raw material used for making photovoltaic products) from the EU. China argued that large companies in Germany received government subsidy of up to 30 percent for investments in the polysilicon industry, while small and medium-size companies received government aid, up to 40–50 percent of their investments (Beijing Review, 10 December, 2012). In addition, China’s Ministry of Commerce began an anti-dumping and anti-subsidy investigation into wines imported from the EU. Europe has a big (and fast growing) share of China’s wine market. European wine accounted for 67.6 percent of China’s total wine imports at the time of the trade dispute (Beijing Review, 26 June, 2013) As of 2012, China imported $1 billion worth of wine from the EU, mostly from France and Italy (Blanchard & Garascio, 2014). It should be noted that France and Italy supported the anti-dumping tariffs on Chinese solar panels while Spain took a neutral position. Thus, China’s AS charges against EU wine were regarded as retaliatory in political nature as it mainly targeted EU member countries that supported the AD tariffs on Chinese solar products.

In addition to AS charges against wine, Beijing also initiated anti-dumping investigation into toluidine imports from the EU. Toluidine is an organic chemical used in dyes, pharmaceuticals and pesticides. As in the case of wine, the EU has a large share of China’s toluidine market, accounting for 16 percent of the total market share as of 2011. According to Chinese investigators, the average selling price of EU-produced toluidine in the EU was significantly lower than the price of EU products in China. Accordingly, China decided to impose 36.9 percent of the anti-dumping duty rates (Beijing Review, 18 July, 2013). Again, China’s AS charge was regarded as retaliatory mainly against Belgium. European Commissioner for Trade, Karel De Gucht, who was known for his hardline stance toward China on the solar panel dispute, is a Belgian. Given that China’s
toluidine imports comes mainly from Belgium (Beijing Review July 18, 2013), Chinese counter AS investigation was regarded as selectively targeting Belgium that favoured AD tariffs on China. The next item on China’s AS investigation list was European steel tubes. Steel seamless tubes and pipes are widely used in manufacturing advanced thermal power generating units. Annually, over 90 percent of the world steel tubes are sold to China, the largest thermal power market, each year (Beijing Review, 28 May, 2013). The US, the EU, and Japan had over 94 percent share of China’s market for such steel products as of 2012 (Beijing Review, 28 May, 2013). Given the EU’s large share of the Chinese steel market, the threat of hefty AS duties on EU products, if realized, was going to strike a serious blow to the EU economy.

The latest AS investigation from China targeted European automobiles. Beijing hinted that it was going to look into EU automobiles to determine whether the EU violated ant-subsidy regulations enshrined in WTO agreements. The Chinese car market is critically important for Germany which has yielded annual sales of over 327,000 cars in China as of 2012. Some analysts argued that by flexing its market power, China tried to pressure Germany to block further negative trade measures against China from the EU commission (Global Post, 10 June, 2013).

In response to China’s counter-investigations, the EU showed mixed responses. On one hand, the EU escalated the bilateral tension by putting more Chinese firms under AS investigation. In May 2013, the EU filed a complaint against Huawei Technologies and ZTE, China’s two leading telecom companies, for alleged dumping practice and illegal government subsidies. In addition, the EU used non-tariff barriers such as safety measures against Chinese products. The EU announced that it would apply stricter safety measures to rice products imports from China. The inspection requiring a health certificate and analytical report would be “the strictest inspection process in the history of the EU” (Beijing Review, July 18, 2013). Given the EU is the second largest importer of Chinese food stuff, the decision would undoubtedly hamper China’s exports.

On the other hand, a schism resulting from differing national interests within the EU hindered a united EU front against China. For instance, Germany and the United Kingdom opposed the anti-dumping tariffs on Chinese solar products (Beijing Review, 26 June, 2013), while France and Italy supported strict AD and AS measures. The EU eventually retreated from its initial hard-line stance mainly due to China’s retaliatory trade measures against the EU and the differing trade interests within the EU.

After exchanging several rounds of AD and AS charges with the threat of hefty retaliatory duties, both sides calculated the gains and losses if they would follow up on initial law suits. Eventually, Brussels and Beijing sought to defuse the situation of a possible full-scale trade war. With secrete negotiations behind the curtains, both sides reached agreements. First, with regard to solar panels, the EU decided to impose an import quota (a total import cap of 7 GW of solar panels per year) and minimum price (56 euro cents from previous 50 euro cents per watt), effective from 2015 (Reuters, 9 August, 2013). Given that China had exported 12 GW of solar panels to the EU in 2012, the quota will almost halve China’s previous export volume. Together with the minimum pricing, the import cap was generally seen as a compromise, departing from EU’s initial hard-line stance. In the case of solar panel, it was reported that “partly due to pressure from the German government” the EU refrained from applying punitive high tariffs on the solar panels (Dalton, March 13, 2014).
After both sides reached an agreement on solar panel, more compromises followed as other AS investigations were dropped before they formally reached the WTO dispute panel. The timing for ending the trade disputes is noteworthy. Most disputes ended shortly before China’s president, Xi’s visit to the EU to discuss a comprehensive plan to deepen the EU–China bilateral trade relations. In March 2014, Beijing dropped the AS investigation into EU polysilicon and wine. Shortly afterwards, the European Commission decided not to pursue an AD investigation into Chinese telecommunication companies (Huawei and ZTE). Given the secrecy surrounding negotiations, the details of the compromises are not yet available. With regard to the telecommunication case, it is speculated that China would award billions of dollars in contracts to European mobile equipment producers and ensure their access to the Chinese market in return for EU’s withdrawal of punitive tariffs on Chinese telecommunication companies. Given that China is the world’s largest market for mobile data services and smart phones with its annual growth rate reaching over 50 per cent (Blanchard & Guarascio, 2014), the deal is indeed a lucrative business opportunity for European companies. In the case of the wine dispute, European producers would provide technical assistance to the Chinese wine industry in return for China’s dropping of the AS investigation into EU wine (Blanchard & Guarascio, 2014).

As shown in the above trade disputes, China has used its market power to influence EU’s trade policy. By threatening to limit the import of certain products (EU wine and toluidine), China showed that it could punish some EU countries that supported the anti-dumping measures against China. Beijing also warned that if the disputes were not to be resolved in a manner acceptable to China, it could retaliate further by launching more anti-subsidy investigations into a series of EU products (e.g., automobiles).

The EU–China trade disputes show that China’s market power is significant enough to influence how trade rules are practiced in today’s global economy. Reflecting China’s market power, more and more developing and emerging economies turn to China as an alternative source of trade and investment. Traditional economic powers such as the EU and the USA now face increasing economic challenges from the China-led economic bloc of the BRICS nations. As it will be explained below, against this backdrop of the growing South-South cooperation and China’s expanding trade ties with Asian nations, Latin America and Africa, it is argued that the US and the EU seek to forge the largest free trade area to counter the rising China and the BIRCS.

**TTP and TIPP: The Geopolitical Implications**

Currently, the EU and the USA are negotiating an inter-regional free trade agreement (FTA), TTIP (Transatlantic Trade and Investment Partnership), while the USA has recruited several Asian nations to enter into a TPP (Trans Pacific Partnership), an inter-regional free trade agreement connecting Asia and the Americas. Conspicuously, the two mega-FTAs exclude China.

Implications of the two mega-FTAs are manifold. First, it is argued that TPP and TIPP are the efforts of developed countries to create a WTO version 2. If concluded successfully, TPP and TTIP will replace WTO as new global trade rules due to the sheer size of international market shares that the two trade deals will cover in the future. In other words, TTIP and TPP, with a global market coverage, will automatically come to exercise “standard-setting power”. Most importantly, the two FTAs will entail US and EU centric trade rules and thus play an instrumental role in rewriting global trade rules that work in favour of developed countries (van Ham, 2013). As van Ham put it,
TTIP’s standard-setting power would indeed be overwhelming, and even a major competitor like China would almost certainly comply with whatever trade rules and regulations the transatlantic West offered to the world. TTIP would be the best way to beat China (as well as Russia and the Gulf states) at their own economic game (van Ham, 2013).

In this sense, TPP and TTIP resemble the earlier process that brought the WTO into being. The GATT, the first international trade agreement established under the leadership of the USA in 1947, promoted cross-border trade by making a significant tariff reduction. As international trade grew, however, the US and the European Community (the predecessor to the EU) considered the informal and limited GATT regime too inadequate. The scope of tariff reduction under the GATT trade regime was limited to only the manufactured goods and did not cover services, foreign investment, and intellectual property rights. The US proposed new rules in those areas that later became the rules of WTO. Developing countries found the new regulations disadvantageous to their developmental needs and thus tried to block the reform. Their endeavour failed when the US and the EC jointly withdrew from the GATT regime in 1994 and established the WTO instead. The US and the EC made a condition that the continuation of trade privileges of any GATT member is contingent upon joining the WTO. Given that the US and the EC controlled an overwhelming share of world market, developing countries had no option but to accept the new rules by joining the WTO (Stone, 2011).

Since the inception of the WTO in 1994, there had been a number of WTO ministerial meetings to forge a consensus on a multilateral framework of international trade in many contested areas including services and intellectual property rights. Negotiations took place in Seattle (1999), Doha (2001) and Cancun (2008) but no significant progress was made. The main reason for the impasse is the conflicting interests between developed and developing nations. Developed countries seek to liberalize service sectors while developing countries are cautious toward opening up their less competitive industries. International exports of services (banking, insurance, telecommunication, transportation, entertainment, education, professional services) are dominated by the US and some EU countries (Germany, Britain, France). The US is the largest exporter of services in the world, with $4.1 trillion export of services in 2011 (The Economist, July 21, 2012). Given the dominance of the EU and USA in the service sector, it is not surprising to see that the USA and the EU actively seek to dismantle barriers to international trade in services, while developing countries try to resist the pressure for service liberalization.

The resistance from developing countries came from a coalition of developing economies led by China, Brazil and India\(^2\). The coalition blocked the efforts by the US and Europe to adopt a comprehensive agreement on liberalization of service among other issues. The impasse at WTO negotiation rounds has consequently led countries to sign bilateral FTAs as an alternative way to expand trade opportunities. Against this backdrop, the US and the EU seek to reassert its hegemony in the global economy by forging a mega-FTA such as TPP and TTIP (Park, 2014). As many analysts point out, China is concerned that TPP and TTIP may “shape new trade rules and dominate the governance of global trade at the expense of China and other emerging economies” (Liu, 2014).

\(^2\) The BRICS grouping (Brazil, Russia, India, China, and South Africa) is a new “pole” in the global economy. The BRICS group has already established its own Development Bank which will compete against the US-dominated IMF and World Bank. The combined nominal GDP of the BRICS group currently amounts to $15 trillion. According to Goldman Sachs report in 2006, the combined GDP of BRIC countries would surpass the GDP of the G6 countries by 2050. The main driver in the BRICS is China which accounts for 85 percent of intra-BRICS trade. (China Daily, March 27, 2013)
China is especially suspicious of the hidden political agenda of the TPP, the US-led mega trade deal in Asia. Mainstream media outlets in China such as Global Times and China Daily openly characterize the TPP as a US containment strategy toward China. This view is widely shared by many analysts and think-tanks in Asia. For instance, Samsung Economics Institute (SEI), a well-renowned Korean think tank, argued that TPP is aimed at containing rising China and that the USA seek to use TTP and TTIP in order to assert itself as the global rule setter in international trade (Samsung Economics Institute, May 15, 2013) SEI further notes that China perceives TTP and TTIP as an attempt by the USA and the EU to isolate China by forging mega trading blocs and consequently pressure China to open the market to their liking.

What is then the reaction of China and the BRICS, the emerging economic pole in the global economy? China has responded to TPP by encouraging its own intra-regional economic cooperation such as the Regional Comprehensive Economic Partnership (RCEP). RCEP aims to integrate five major sub-regional FTAs, that the Association of South East Asian Nations (ASEAN) signed with its Asian neighbours (China, Japan, South Korea, Australia, and India), into a mega regional economic framework (Park, 2014). The RCEP will be a comprehensive trade agreement, covering trade in goods, services, and investment (Singapore Ministry of Trade and Industry, 2012). Unlike TPP, RCEP takes into consideration different levels of development of participating countries and allows “appropriate forms of flexibility including provision for special and differential treatment, plus additional flexibility to the least-developed” (Singapore Ministry of Trade and Industry, 2012). As China Daily states, “the RCEP, rather than a blanket agreement, should be a phased-in arrangement that accommodates member countries at different levels of development” (China Daily, May 13, 2014). Thus, the flexible RCEP is arguably a more attractive option for developing countries. Additionally, “provisions for technical assistance and capacity building may be made available to the developing and least-developed countries” (Singapore Ministry of Trade and Industry, 2012). Like TTP, RCEP has an open accession clause that allows other external members to join after the conclusion of the RCEP negotiations.

Favouring a more flexible trade bloc, many political analysts and policy advisors call for a free trade area among BRICS. Some Chinese economists have argued that “BRICS members should create a free trade agreement to increase the power and voice of emerging economies in the world economy” (China Daily, March 27, 2013). For instance, Wang Junwen, chairman of the China Association of International Trade, called for such an agreement. Sun Zhenyu, chairman of the China Society for World Trade Organization Studies (CWTO), a think tank of the Ministry of Commerce in China, also said, “BRICS surely needs to strengthen cooperation, and better cooperation will bring about a greater role in global governance” (China Daily, March 27, 2013). In contrast to TPP and TTIP, RCEP and BRICS free trade area are considered as developing countries’ (China and ASEAN) alternative to the US and EU led deep and comprehensive liberalization scheme. Likewise, Russia portrays its Eurasian Economic Union (concluded in May 2014) as Russia’s counter-trade bloc to the EU and US-led regional FTA schemes. As rivalry between traditional economic powers and emerging economies increases, TPP and TTIP are unlikely to merge into a multilateral trade framework that covers the entire global economy. They will more likely trigger power rivalry in the international arena and engender competing regional and sub-regional trade blocs. Dr van Ham, senior research fellow at the Netherlands Clingendael Institute of International Relations, cautions that “TTIP may well turn into a self-fulfilling prophesy, inducing the Global South, Russia and Brazil to rally round the Chinese flag, just to thwart EU-US standard-setting ambitions. TTIP may, in the worst scenario, create a unified anti-Western BRIC-bloc that hardly exists at the moment” (van Ham, 2013).
Unfortunately for the EU and the USA, the Ukraine crisis seems to provide a renewed momentum for the BRICS to consolidate its ties. Equally important is a prospect that the EU sanctions against Russia would further strengthen China’s market power by creating more business opportunities for China.

The Ukraine Crisis: Consolidating BRICS?
To a large degree, the Ukraine crisis has resulted from two conflicting external forces: 1) conflicting economic interests between Russia and the EU and 2) geopolitical rivalry between Russia and USA (via NATO) in the region. It should be also equally stressed that Ukraine has its citizenry equally divided into pro-Russian and pro-EU constituencies closely tied to Russian or EU businesses. Until the Crisis of 2013, Russia was Ukraine’s biggest trade partner, export market and source of energy although the EU was the major source of its foreign investment, a major shareholder in Ukrainian banks, and its second biggest trade partner. While Russia seeks to bring Ukraine to the Russia-led Eurasian Economic Union (similar to the EU), the EU has been negotiating with Ukraine to sign a “deep and comprehensive” free-trade agreement, stopping short of EU membership. Not surprisingly, Russia’s Eurasian Union project was incompatible with the EU’s Eastern Partnership with Ukraine (China Daily, November 29, 2013).

The condition under which the conflicting political forces came to a head was prepared by the IMF. Although in dire financial need due to economic distress resulting from the global financial crisis, in 2013 the IMF refused to lend money to the Ukraine. As a condition of aid, the IMF wanted Ukraine to cut energy subsidies to reduce the country’s budget deficit. President Viktor Yanukovych refused the IMF’s lending conditionality because the energy price hike would undoubtedly anger many Ukrainians and thus jeopardize his bid in the 2015 presidential election (Bloomberg, April 10, 2013). After the Ukrainian refusal of IMF conditionality, the country’s economy was in free fall. International rating agencies such as S&P and Moody downgraded Ukraine’s credit rating and made it difficult for Ukraine to borrow money while forcing it to pay higher interests on its debt. In this context of extreme financial difficulties, Ukraine turned to Russia for aid. Russia agreed to lend money without austerity demanding clauses. In return, Russia wanted Ukraine to reconsider its EU-Ukraine Free Trade agreement and instead to join the Russia-led eastern trade bloc. In this context, Yanukovych decided not to enter into a free trade agreement with the EU. The cancellation of the FTA plan backfired as this mobilized a large number of anti-government protestors who supported closer ties with the EU. The pro-EU street demonstrators, with the help of ultra-Ukraine nationalists, brought down the Yanukovych administration by illegal means, even though Yanukovych promised to reverse his previous trade policies. A majority of the populace in eastern Ukraine and Crimea, however, did not trust the new regime in Kiev, the coalition of pro-EU forces and ultra-Ukraine nationalists. Willfully ignoring the voice of pro-Moscow and anti-Kiev Ukrainians, the EU hailed the illegal ousting of Yanukovych as a victory for democracy. The EU and American approaches have been extremely biased against Russia in the eventual break-up of Ukraine. Ignoring human rights violations and atrocities committed by the new Ukraine regime against its own citizens, the EU and the USA blame only Russia and try to put pressure on their allies to punish Russia with military and economic sanctions. The sanctions will, however, unlikely change Russia’s stance toward Ukraine. The main reason is that the Ukraine crisis is rooted in internal conflicts involving the Russian speaking people in eastern Ukraine and Crimea who do not support the new regime in Kiev. By sanctioning Russia and killing the anti-government protesters in eastern Ukraine, the EU and the USA unlikely win over people in Crimea and eastern Ukraine who harbour deep resentment toward the new government and its allies, the EU and the USA.
The EU sanctions against Russia have provided an impetus to Russia to reach out to the BRICS nations. It should be noted that at the UN general assembly meeting, all members of the BRICS group did not support the EU and the USA-led condemnation of Russia over Ukraine. To counter the sanctions, Russia has moved away from European and American markets and instead turned to Asia and Latin America. So far this year, Russia has made numerous mega-trade deals with BRICS nations as well as some Latin American countries. Russia signed a mega gas deal (worth $270 billion) with China (Russia Today, March 31, 2014). Moscow banned all food imports from the EU, the US, and the countries (e.g. Canada) that impose sanctions on Russia over the Ukraine crisis. Instead, Russia decided to fill the agricultural shortage with imports from China, Brazil, Ecuador, and Turkey.

As for countries in Latin America, many nations that resent US domination in the region welcome trade opportunities with China and Russia in order to move away from their traditional dependency on the American and the EU markets. When President Xi visited Brazil, Argentina, Venezuela, and Cuba (all four countries critical of US foreign policy) this year, the five nations confirmed their commitment to tightening Sino–Latin American cooperation and subsequently established the China–CELAC Forum (CELAC stands for the Community of Latin American and Caribbean States) which will be held next year (China Daily, July 30, 2014). China is the biggest trading nation for Brazil, Chile, and Peru, and the second biggest for Mexico. It is predicted that by 2016 China will surpass the euro zone as Latin America’s second-largest trading partner. (South China Morning Post, 17 March, 2014). As the economic cooperation among BRICS deepens and China’s trade with Latin America and other Asian nations increase, China is in no rush to compromise with the EU on the terms of its market opening.

The implications of the Ukraine Crisis for the EU–China bilateral trade relations are largely positive for China while the opposite is the case for the EU. First of all, the EU will be put under heavy pressure to find a new market for its agricultural exports that were previously earmarked for the Russian market. Russia’s ban on agricultural imports from the EU will cost “Europe more than €12 billion in lost exports, which represents around 10 percent of total EU agricultural sales outside the bloc” (Euobserver, August 11, 2014). Already, the EU sanctions backfired as Russia’s counter-sanction measures began to hurt the EU economy. Economists predict a low economic growth for most European economies this year. Since the Ukraine crisis began in 2012, it is reported that German investor confidence fell to the lowest level (Bloomberg, August 12, 2014). China will be in a better position to exploit new business opportunities with Russia. With new expanded venues for exports, Beijing will less likely enter into any new trade and investment agreements with the EU, if they require too many concessions from China in the area of state sector, agriculture and services. The game changer might be the TPP and TTIP (South China Morning Post, 17 March, 2014). As Van Ham pointed out, for the EU, TTIP is “the only way the two sides (the EU and the USA) can continue to assert their market power and preserve their mutual economic interests worldwide” (van Ham, 2013). If TTIP is concluded, China will come under pressure to accept the new terms of trade liberalization in the traditionally protected areas including services, agriculture, and non-tariff barriers.

Conclusion

This paper has examined three critical issues concerning the EU–China bilateral trade relations. First, it analyzed the contentious dynamics between the EU and China with regard to recent trade disputes over rare earths and solar panels. Secondly, it discussed geopolitical implications
of mega-FTAs such as TPP and TTIP. Thirdly, it explored the impacts of the Ukraine crisis on
the bilateral economic development. The paper argued that with China’s growing market power,
China responded to EU’s AD and AS measures in an equally assertive manner by filing retaliatory
investigations into EU export products. With a threat of reprisal (i.e., blocking EU access to
growing China’s market), China has negotiated compromised solutions to most trade disputes
except the rare earths case. With regard to the geo-political implications of TPP, TTIP and the
Ukraine crisis, it noted that these events may provide a renewed momentum for China and Russia
to forge stronger economic ties among the BRICS and to rally other nations in Asia and Latin
America to join alternative trade blocs.

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