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CHINA'S ECONOMIC ENGAGEMENT WITH SOUTHEAST ASIA: THAILAND

JOHN LEE

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FOREWORD

The economic, political, strategic and cultural dynamism in Southeast Asia has gained added relevance in recent years with the spectacular rise of giant economies in East and South Asia. This has drawn greater attention to the region and to the enhanced role it now plays in international relations and global economics.

The sustained effort made by Southeast Asian nations since 1967 towards a peaceful and gradual integration of their economies has had indubitable success, and perhaps as a consequence of this, most of these countries are undergoing deep political and social changes domestically and are constructing innovative solutions to meet new international challenges. Big Power tensions continue to be played out in the neighbourhood despite the tradition of neutrality exercised by the Association of Southeast Asian Nations (ASEAN).

This series—now revamped and redesigned—acts as a platform for serious analyses written by selected authors who are experts in their fields. It is aimed at inspiring policy makers and encouraging scholars to contemplate over the diversity and dynamism of this exciting region.

THE EDITORS

China's Economic Engagement With Southeast Asia: Thailand

EXECUTIVE SUMMARY

- There is evidence that China engages in 'economic statecraft' in using tools such as trade and investment to influence strategic and political decisions in so-called 'swing states' in Southeast Asia.
- When it comes to Thailand, Beijing's actual or material capacity to use these economic tools to significantly alter decision-making in Bangkok is limited and frequently overstated. Although the economic relationship with China will grow in importance, the relatively open and diverse nature of the Thai economy offers the country significant trade and investment alternatives that are denied to neighbours such as Cambodia.
- Even so, the perception of Thai reliance on China now and into the foreseeable future differs significantly from reality. In over-estimating the importance of the Chinese economy relative to other major economic players in Asia, Bangkok seems to have a disproportionate fear of displeasing Beijing and damaging its political and relationship with China.
- Such a mindset could lead to strains in its security relationship with its American treaty ally, and could inhibit Bangkok's capacity to play a more pro-active role in ASEAN and other multilateral institutions, especially when it comes to regional approaches to addressing awkward but important disagreements vis-à-vis China.

** This is the first in a planned series on the theme of "China's economic engagement with Southeast Asia".*

China's Economic Engagement With Southeast Asia: Thailand

By John Lee[1]

INTRODUCTION

In a private conversation focusing on relationships with Asian allies in Washington DC last November, a senior official within the White House expressed his frustration with Thailand and offered the personal opinion that the security treaty with Bangkok should be 'ripped up' unless Bangkok showed more preparedness to support American security and economic initiatives in the region.

Although not official policy, such sentiments are not rare amongst influential Asia-hands in Washington DC. The view is also shared by many commentators who believe that Thailand is slowly but surely drifting towards China, and away from the United States. Typical examples include analyst David Fullbrook who predicted that "As trade and investment grow… China's economic gravity will wrest Thailand from a century of Western embrace."[2] Bronson Percival argues that Bangkok "eagerly snuggles up to China so as to reap the benefits of an emerging Sino-centric order."[3]

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[1] Dr. John Lee is a visiting fellow at ISEAS. He is also the Michael Hintze Fellow and Associate Professor at the Centre for International Security Studies, University of Sydney; non-resident senior fellow at the Hudson Institute in Washington DC; and Director of the Kokoda Foundation strategic and defence think-tank in Canberra.

[2] David Fullbrook, "Thailand in China's Embrace," *Asia Times Online*, April 9, 2004.

[3] Bronson Percival, *The Dragon Looks South: China and Southeast Asia in the New Century* (Westport, CT: Praeger Security International, 2007), p. 46.

This issue of *Trends in Southeast Asia* examines Chinese commercial activity in Thailand: the nature and scale of such activity; possible political and strategic motivations behind these; and the extent to which Chinese commercial activity is allowing Beijing greater leverage and influence over Thailand's future strategic and political options. The paper argues that although Chinese economic activity in Thailand will continue to grow, the material capacity for Beijing to use economic or commerce to coerce Bangkok into making political or strategic decisions that Bangkok would not otherwise make is limited, and will remain so for the foreseeable future.

Moreover, the capacity of Beijing to use economic and commercial means to *persuade* or else *seduce* Thailand is often overstated even by the Thais themselves. In reality, the relatively open and diverse nature of Thailand's economy offers the country considerable trade and investment alternatives in addition to the significant opportunities presented by China.

Indeed, perception can often deviate from reality. Thailand rightly rejects any emerging strategic or military coalition explicitly aimed against China in the absence of extreme and prolonged Chinese regional provocation. But in overestimating the current and foreseeable importance of China to its own economy, resulting in a growing and possibly overriding fear of displeasing Beijing and/or missing out on emerging economic opportunities, Bangkok could well find itself being viewed as an increasingly disappointing ally for Washington, and an absent and progressively irrelevant player within various ASEAN-led institutions. If that occurs, Bangkok's emerging mindset of seeking the benefits of China's economic rise without pro-actively and constructively addressing the strategic risks could lose Bangkok old and/or contemporary friends, and achieve the opposite of what its risk-minimisation strategy is designed to do.

THAILAND'S STRATEGIC MINDSET

Thailand's status as one of five formal American treaty allies in Asia can give rise to the narrative that Bangkok was, until recently, resolutely in

Washington's strategic camp for over five decades. In reality, the use of skilful diplomacy and engagement with greater powers to protect the Thai Kingdom from external subjugation is deeply embedded in Thai strategic history, culture and mind-set.

It is highly revealing that the Kingdom of Siam (as it was then known) held on to much of its sovereignty during the height of European colonialism in the nineteenth century, bucking the trend of colonisation being imposed on all its Southeast Asian neighbours. The deftness of political, strategic and cultural diplomacy used to manage relations with imperial Russia, Germany, Britain and France during the reign of King Rama V (1868-1910) continues to serve as a source of historical pride, and as a model of small-power statecraft for Bangkok. At the conclusion of World War One, Siam's support for the allies meant that it stood at the victory table during the signing of the Treaty of Versailles despite its token involvement, having only declared war against the Central powers on July 22, 1917. With its standing strengthened as a founding member of the post-war League of Nations, Siam successfully concluded favourable amendments to treaties with colonial powers Britain and France, leading to restoration of its full sovereignty by the mid-1920s. The principles of pro-actively engaging with great powers active in Asia and of responding to changes in the balance of power by hedging accordingly in order to retain its capacity to resist foreign subjugation remains at the heart of Thailand's strategic thought.

Bangkok's strategic decisions after World War Two should be understood in this light. The post-WWII period was dominated by threats of communism and regional instability. In 1954, Thailand became a founding member of the now defunct South East Asian Treaty Organisation (SEATO), the primary objective of which was to contain the spread of communism. The foundations of its ongoing alliance with the US can be traced back to the so-called *Manila Pact* arrangements under SEATO which contained a collective security clause in the event of attack against signatories, and the *1962 Communique* between then Thai Foreign Minister Thanat Khoman and American Secretary of State Dean Rusk which referred to a common Communist threat in the region. Although the current status of the *1962 Communique* is ambiguous in the contemporary environment where a communist threat is lacking, it is clear that the prin-

ciples of the *Manila Pact* remain the framework for the modern application of the US-Thai alliance.

Although keen to preserve the alliance with Washington, Bangkok nevertheless wants to ensure that the alliance does not become an obstacle to improving relations with China – leading to confusion as to where Thailand's loyalty might lie in the future. Despite being one of Washington's five treaty allies in Asia, Bangkok has one of the closest diplomatic and defence relationships with Beijing of all the ASEAN member states even if America remains the more important bilateral security partner of Thailand's by some distance. Thailand is also diversifying its arms suppliers away from American and European sources, even if more advanced arms purchases continue to be from traditional Western companies.[4]

More recently, Thailand has showed a reluctance to take the lead in organisations such as ASEAN when awkward issues with China are raised, despite being one of the founding members. It has also only shown greater willingness to actively support American military actions that are not focused in the Asia-Pacific, such as Bangkok's offer of logistical and refuelling support for coalition forces during Operation Enduring Freedom against the Taliban in 2001 and offer of 447 military personnel to bolster the 'Coalition of the Willing' against the Saddam Hussein regime in Iraq in 2003. Although these measures are designed to manage and preserve

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[4] For example, Bangkok put in an order for 200 T-84 Chinese and Ukrainian produced tanks, with the first shipment completed in May 2013, and the second completing the training unit and fully equipping the first shipment by 2015. In early 2012, Thailand and China disclosed a program to develop rockets and multiple launchers for those rockets. In March 2013, an article in the state-run and state-owned *China Daily* reported that the Thai navy placed an order for a Chinese 053-class frigate, with the article's author boasting that the low-cost reliability of China-made arms are successfully undercutting American and European rivals. See Tamir Eshel, "Main Battle Tanks Moving East," *Defence Update*, January 14, 2013 <http://defense-update.com/20130114_main-battle-tanks-moving-east.html> accessed June 11, 2013; Chen Boyuan, "Chinese arms exporters enjoy growing recognition," *China Daily*, March 5, 2013 <http://www.china.org.cn/china/2013-03/05/content_28136304.htm> accessed June 11, 2013.

It should be borne in mind that the Sino-Thai military-to-military relationship first blossomed from the late 1970s onwards, largely due to the convergence of security interests following the Vietnamese invasion and occupation of Cambodia in December 1978. See Chulacheeb Chinwanno, "Thai-Chinese Relations: Security and Strategic Partnership," *RSIS Working Paper No. 155*, March 24, 2008 <http://www.rsis.edu.sg/publications/WorkingPapers/WP155.pdf> accessed July 19, 2013.

the alliance with America, Bangkok is keen to reinterpret commitments in ways that do not place it in the sights of American strategic rivals, especially China.[5]

Thai statecraft has frequently been described as 'bending with the wind'.[6] Referred to as a 'foreign policy in transition',[7] Bangkok's perceived need to balance between China and America would not be so great were it not for the economic lure, and perhaps coercive economic tools, at China's disposal. In contemporary times, Thai strategic objectives have been redefined to ensure that it adjust to China's rise in ways that will not jeopardise its own economic prospects and opportunities. The Thai desire to "manage its relationship with the United States in a way that facilitates closer ties with China"[8] as Evelyn Goh put it, gained strong momentum after the 1997 Asian Financial Crisis when China decided not to devaluate its currency, even as America did little to assist its ally while capital flows rushed out of the country. The remainder of this *Paper* is therefore devoted to examining the nature and scale of current Chinese economic activity in Thailand, and the strategic and political implications of these for the present and the future.

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[5] For example, the 2012 *Joint Vision Statement for the Thai-US Defence Alliance* signed by then Secretary of Defence Leon Panetta and Thai Defence Minister Sukumpol Suwanatat steers away from the rationale of a major threat in reaffirming the alliance. The Joint Statement "supports Thailand's position as a regional leader" for the maintenance of regional stability and encourages cooperation on softer security threats such as peacekeeping. While supporting an increase in bilateral readiness and interoperability of the two militaries by emphasising multilateral exercises such as Cobra Gold, the statement remains ambiguous on more controversial issues such as Washington's interest in 'flexible basing' throughout the region.

[6] See Ian Storey, "From Strength to Strength: Military Exercises Bolster Sino-Thai Relations,' *China Brief*, Volume XII, Issue 12, June 22, 2012.

[7] "Talk with Pavin: Thailand's Foreign Policy in Transition," *Prachatai*, August 8, 2011 <http://prachatai.com/english/node/2698> accessed June 12, 2013.

[8] Evelyn Goh, "Meeting the China Challenge: The US in Southeast Asian Regional Security Strategies," Policy Studies 16, 2005, p. 26.

CHINESE ECONOMIC STATECRAFT

In September 2010, China halted the export of rare earth metals to Japan during an escalation of an incident in disputed waters in the East China Sea caused by the ramming of a Japanese vessel by a Chinese fishing trawler captain (leading to the latter's detention by the Japanese coast guard.[9]) Over the same sovereignty issues in late 2012, Beijing tacitly supported a widespread boycott of Japanese products over a four-month period, an action which led to a decline in growth of 1% in that quarter for the Japanese economy according to some financial analysts.[10]

Similarly, in May-June 2012, and in the midst of a flare-up between the two countries over sovereignty of the Scarborough Shoal, several tour groups in China cancelled trips to the Philippines while imports of bananas from the Philippines into China were banned on the unusual basis that several crates shipped in April contained pests.[11] Other illustrations of Chinese economic coercion can be located in a study by two academics who found that countries officially receiving the Dalai Lama at the highest political level were consistently punished through a reduction of their exports to China by between 8.1% and 16.9% (depending on the methodology for measurement) for the following two years.[12]

These examples confirm that China is not above the use of overt economic *coercion* to achieve political objectives. However, the use of such coercion entails huge diplomatic costs and can carry negative economic

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[9] See Keith Bradsher, "Amid Tension, China Blocks Vital Exports to Japan," *New York Times*, September 22, 2010 <http://www.nytimes.com/2010/09/23/business/global/23rare.html?pagewanted=all> accessed June 12, 2013.

[10] See "China-Japan Disputes Takes Rising Toll on Top Asian Economies," *Bloomberg*, January 9, 2013 <http://www.bloomberg.com/news/2013-01-08/china-japan-dispute-takes-rising-toll-of-asia-s-top-economies.html> accessed June 12, 2013.

[11] See Roel Landingin, Philippines vs China: Going bananas," *Financial Times*, May 11, 2012 <http://www.ft.com/intl/cms/s/0/24d5edf2-9e80-11e1-a767-00144feabdc0.html#axzz2W01DQn6N> accessed June 12, 2013; "Philippine businesses warn on China stand-off," Financial Times, May 15, 2012. <http://www.ft.com/intl/cms/s/0/24d5edf2-9e80-11e1-a767-00144feabdc0.html#axzz2W01DQn6N> accessed June 12, 2013.

[12] Andreas Fuchs and Nils-Hendrik Klann, "Paying a Visit: the Dalai Lama Effect on International Trade," *Centre for European, Governance and Economic Development Research Discussion Paper 113*, October 2010.

repercussions for China. Japanese firms have already been relocating many production chain operations away from China for commercial reasons such as rising labour costs, and are exploring options in countries such as Thailand, Indonesia and Vietnam. Although Japanese firms will retain substantial manufacturing operations in China – and will need to do so in order to sell to the Chinese domestic consumption market – the aftermath of the Chinese boycott will surely raise the perception of political risk for these and other firms.[13] Indeed, in a survey conducted by the Japan Bank for International Cooperation of Japanese manufacturing firms after the initial flare-up over the Senkaku/Diaoyu Islands in 2012, over 65% of respondents replied that the diplomatic rift had 'substantially' or 'somewhat' affected their business in China. While China was still seen as a promising place to do business, 63.3% of respondents felt the need to 'monitor the situation and act cautiously' or 'rethink' their operations in China as a result of the Sino-Japanese political situation.[14] More generally, and as one commentator puts it in a typical warning about increased political risk in China:

> *"When China has a dispute with another country, it can impact companies from that country that operate inside China as Chinese officials, either overtly or behind the scenes, use the network of Communist Party officials who are still placed in all schools, state companies and other organisations to stir up latent Chinese xenophobia and nationalist rage."*[15]

Less dramatic, but more sustainable and effective is the use of economic tools such as trade, investment and aid to *seduce* or else *persuade* other capitals to gradually adopt ever more China-friendly policies over time.

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[13] See Hiroko Nakata, "Firms move some eggs out of China basket," *Japan Times*, December 19, 2012 <http://www.japantimes.co.jp/news/2012/12/19/reference/firms-move-some-eggs-out-of-china-basket/#.Ublb8_lmhcY> accessed June 13, 2013.

[14] Japan Bank for International Cooperation, *JBIC Today*, March 2013 <http://www.jbic.go.jp/en/report/jbic-today/2012/201303/jtd_201303.pdf> accessed July 3, 2013.

[15] David Lindorff, "Political risk rises in China," *Treasury & Risk*, October 1, 2012 <http://www.treasuryandrisk.com/2012/10/01/political-risk-rises-in-china> accessed July 3, 2013.

In an age where the legitimacy of democratic and authoritarian governments in Asia is based more on economic performance than political ideology, effective Chinese economic statecraft must be built on principles of economic attraction and opportunity rather than outright coercion. Additionally, in a strategic environment within which traditional American alliances and partnerships are being subtly reworked as a hedge against a disruptive China, Beijing knows that it must increasingly rely on a strategy of economic inducement and persuasion rather than coercion since regional security hedging could well evolve into outright balancing if concerns over China's rise increase.

The rule of thumb that one 'catches more flies with honey than vinegar' makes sense when it comes to Thailand, which Beijing sees as a possible 'swing state' within ASEAN despite the country's alliance with the US[16] The argument that China has little need to use coercive economic diplomacy is augmented by the lack of recent historical animosity in China-Thailand ties, the belief by many Thais (particularly the politically, economically and socially powerful ethnic Chinese diaspora) that China's rise is benign,[17] and the reality that many Thai Cabinet ministers have extensive business interests in China. This has all contributed to the apparent ease and intimacy in personal and political relations built up between the two capitals over the past decade.[18]

Before considering the possible political and strategic motivations behind the more subtle, softer use of Chinese statecraft in the form of free trade agreements (FTAs), trade, and investment in Thailand, it is

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[16] For example, see Thitinan Pongsudhirak, "Thailand's Foreign Policy in a Regional Great Game," in Nicholas Kitchen (eds.,) *The New Geopolitics of Southeast Asia* (London: LSE IDEAS 2012); Julius Cesar I Trajano, "Old Allies, new dynamics in US pivot," *Asia Times*, August 31, 2012; Walter Lohman, "Reinvigorating the US-Thailand Alliance," *Heritage Foundation Backgrounder No. 2609*, September 26, 2011.

[17] In a 2003 poll, 76% of Thais surveyed believed that China was Thailand's closest friend, compared to 9% who nominated America and 8% nominating Japan: see Phillip Pan, "Improving Image Challenges US in Asia," *Washington Post*, November 15, 2003 <http://www.defencetalk.com/chinas-improving-image-challenges-us-in-asia-1145/> accessed July 3, 2013.

[18] See Pavin Chachavalpongpun, "Cosy Sino-Thai relations affecting ASEAN unity," *South China Morning Post*, May 21, 2013 < http://www.scmp.com/comment/insight-opinion/article/1242092/cosy-sino-thai-relations-affecting-asean-unity> accessed July 3, 2013.

important to understand the somewhat disorganised and fragmented formation and implementation of economic statecraft through which China engages with countries in Southeast Asia.

Broad and overarching agreements such as the China-ASEAN Free Trade Agreement (CAFTA) can give the misleading impression that Beijing adopts a centralised, well-coordinated and highly integrated framework when it comes to economic relations with Southeast Asia. In principle, central government authorities and agencies establish broad economic (and strategic) objectives and targets for central and provincial entities to pursue. In practice, Chinese economic policy and statecraft towards Southeast Asia is increasingly being broken up in sub-regional segments. In particular, the Chinese government's economic policies towards Thailand are placed more and more within the framework of policies geared for the so-called Greater Mekong Sub-Region (GMS), which encompasses Yunnan Province, Myanmar, Cambodia, Laos, Vietnam and Thailand. The Guangxi Zhuang Autonomous Region formally joined the GMS in 2005.

The GMS provides obvious strategic appeal to Beijing as a continental trading route that connects Southern China with the mainland of Southeast Asia and South Asia (bypassing maritime routes through the South China Sea and the Malacca Straits.) In practice, officials from Yunnan Province have taken a leading role in driving economic policy towards countries such as Thailand, and in managing day-to-day relations, even if provincial officials have no formal powers in determining national policy and must instead lobby and/or convince central officials that their activities are consistent with national strategic and economic objectives.[19] In the case of the GMS, land-locked Yunnan Province and Guangxi Autonomous Region are the second and fourth poorest provinces on a per capita basis in China respectively.[20] Given that officials rely heavily on the prospect of a growing GMS zone of prosperity for its future economic prospects, it is not surprising that Yunnan Province with a population of

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[19] See Li Chenyang and He Shengda, "China's Participation in the GMS Cooperation: Progress and Challenges," in Mingjiang Li and Chong Guan Kwa (eds.,) *China-Asian Sub-Regional Cooperation: Progress, Problems and Prospect* (Singapore: World Scientific Publishing, 2011), pp. 15-36.

[20] National Bureau of Statistics figures.

45 million (and to a lesser extent, Guangxi Autonomous Region with a population of over 50 million) has the greater interest and energy in driving Chinese economic policy towards the GMS, and is playing a leading role within the GMS itself – especially in proposing the alphabet soup of coordination and cooperation agreements that cut across all major economic sectors. Indeed, in an inspection tour of Yunnan in July 2009, then Chinese President Hu Jintao urged the Yunnan provincial government to take the lead in deepening economic cooperation with GMS countries, and establish Yunnan Province as China's key bridgehead into South and Southeast Asia.[21]

This is not to say that it is always a simple matter of the provincial 'tail' wagging the central 'dog'. Yunnan Province proposals for the GMS must be consistent with national guidelines and objectives, while provincial officials have no inherent authority to carry out negotiations or sign agreements with GMS countries. At high profile GMS summits, central officials deliver the keynote speeches, and put forward and negotiate the framework proposals. Importantly, Chinese centralised entities such as the Ministries of Finance, Commerce, Foreign Affairs and National Development and Reform Commission work alongside the Yunnan and Guangxi provincial governments to develop GMS policy, and to coordinate planning with the ADB in the sub-region. Financing for big-ticket projects such as the 1818km Kunming-Bangkok highway which was completed in 2008 must also be cleared through central agencies.

Although central agencies will often delegate authority to provincial governments to streamline processes and utilise on-the-ground knowledge and connections, there is a continual bargaining process between provincial and central entities in formulating and implementing GMS policy. This is brought out to make the point that Chinese economic policy, and by extension statecraft is neither straightforward, elegantly conceived nor seamlessly implemented – even if Beijing generally gets its way over the provinces if the strategic or political stakes are high enough. Provincial and local officials needing centrally approved finance and 'go ahead' need to speak the language of national strategic objectives in

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[21] See Xiaobu Su, "Rescaling the Chinese state and regionalization in the Great Mekong Subregion," *Review of International Political Economy* 19:3, 2012, pp. 501-527 at 518.

making any case. But they generally remain more focused on commercial outcomes and Yunnan Province officials are unlikely to harbour the same enthusiasm as Beijing in using economic levers to probe the possibilities of Thailand as a strategic 'swing state'.

The following sections will focus on Chinese trade and investment in Thailand. Overseas Development Assistance (ODA) - more commonly referred to as aid - will not be considered simply because China is not a major aid donor to Thailand. Unlike substantial Chinese ODA to Myanmar, Cambodia and Laos, Beijing's aid policy towards Thailand is relatively tokenistic and proceeds on an *ad hoc* basis – it is most evident after natural disasters, and is done as a show of goodwill. For example, China offered a modest package of approximately US$5 million of cash remittances and relief materials to Thailand after the floods in 2011. ODA into Thailand is not a major tool of diplomacy used by the Chinese, since the country is the most developed Southeast Asian member of GMS.

CHINA-THAILAND TRADE

In 2006, a survey of elite opinion in eight Asia-Pacific countries (including Thailand but not China) found that 'strengthening diplomatic relations with key trade partners' in recognition of an emerging regionalisation (but not necessarily an emerging regionalism) was the most frequently cited reason for the negotiation of FTAs[22] – a mindset reinforced by the trauma of the Asian Financial Crisis in 1997 and subsequent faltering of World Trade Organisation processes and agreements.[23]

As far as China is concerned, it is widely recognised that Beijing readily uses trade in general, and FTAs in particular, to achieve political and diplomatic goals in addition to economic gains. While the most obvious example is Chinese economic policy towards Taiwan which is designed

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[22] Christopher M. Dent, *New Free Trade Agreements in the Asia-Pacific* (Basingstoke: Palgrave Macmillan, 2006), Chapter 2.

[23] See Christopher M. Dent, "Free trade agreements in the Asia-Pacific a decade on: evaluating the past, looking to the future," *International Relations of the Asia-Pacific* 10, 2010, pp. 201-245.

to win the hearts and minds of the latter's citizens,[24] the political motivations behind Chinese trade policy in the region are also clear. Indeed, Chinese proposals for FTAs and other trade agreements coincided with its era of 'smile diplomacy' and 'win-win' rhetoric from the late 1990s onwards. As many commentators have noted, China's offer of an FTA with ASEAN must be understood within the context of Chinese and Japanese competition for political leadership in East Asia, alongside the desire to assure neighbours that its ascension to the WTO would not cause them economic hardship.[25]

Critical to the success of Chinese diplomacy was the argument that its rise would be peaceful and create opportunities for nervous neighbours. In particular, Beijing has long promoted the CAFTA agreement as evidence of China's peaceful and cooperative commitment to prosperity and mutual gain in the region.[26]

Suspicion that CAFTA was heavily informed by political and strategic considerations on the Chinese side is reinforced by the fact that China voluntarily gave concessions to ASEAN on agricultural trade through the Early Harvest Programme (EHP). Complaints by local officials and farmers in southern China was overruled by central ministries on the basis that the EHP would bring wider (non-economic) benefits for the whole

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[24] See John Lee, "Why Taiwan will fail," *Wall Street Journal*, March 31, 2011 <http://online.wsj.com/article/SB10001424052748703806304576234143900899156.html> accessed June 18, 2013.

[25] See John Ravenhill, "The 'new East Asian regionalism': A political domino effect," *Review of International Political Economy* 17:2, 2010, pp. 178-208; K. G. Kai, "Chinese Changing Occasional on the Development of an East Asian Free Trade Area," *Review of International Affairs* 3, 2004, pp. 584-99; D. J. Zha, "The Politics of China-ASEAN Economic Relations: Assessing the Move towards a Free Trade Area," *Asian Occasional* 26, 2002, pp. 53-82.

[26] For example, see Zheng Anguang, "FTA is selling a bright future," *China Daily*, January 6, 2010 <http://news.xinhuanet.com/english/2010-01/06/content_12763095.htm> accessed June 18, 2013; Zhang Ruiling and Lei Bosong, "China is peaceful rise and peaceful development country: expert," *Xinhua*, November 14, 2010 <http://news.xinhuanet.com/english2010/china/2010-11/14/c_13606068.htm> accessed June 18, 2013; "Chinese, ASEAN leaders meet to boost cooperation," Xinhua, November 24, 2009 <http://news.xinhuanet.com/english/2009-10/24/content_12313602.htm> accessed June 18, 2013.

country.[27] In fact, Thailand was the first ASEAN beneficiary under the EHP framework when tariffs on vegetables and fruits were lifted ahead of time in October 2003.

Although the EHP led to an immediate boom in agricultural trade between China and Thailand with growth in agricultural trade volumes of 36% in 2004 from the year before,[28] the impact of the EHP agreements and CAFTA in general should not be overstated. A 2007 study indicated that only 11% of Thai exports to China took advantage of CAFTA, with even lower rates for exports to China from other ASEAN countries investigated such as Indonesia, the Philippines and Cambodia.[29] This is supported by another 2008 study which indicates that utilisation rates by Thai firms of CAFTA was only 12%,[30] just slightly above the average East Asian utilisation rate of 10% according to an Asian Development Bank study published in the same year.[31] Another 2007 report indicates that the average preferential margin for Thai exports to China based on CAFTA provisions was only 1.03%.[32] When considering the paperwork and other red-tape requirements to make use of CAFTA provisions it is not surprising that CAFTA is far less utilised than is commonly believed.

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[27] See Yang Jiang, "China's pursuit of free trade agreements: Is China exceptional?" *Review of International Political Economy* 17:2, 2010, pp. 238-261.

[28] Xiaobo Yin, "Sino-Thailand Bilateral Trade in Agricultural Products: Competition and Complementation," *Paper presented to First Thai-Chinese Strategic Research Seminar*, Bangkok, August 24-26, 2012 < http://www.nrct.go.th/th/Portals/0/data/%E0%B8%A0%E0%B8%95/2555/10/1stThai-Chinese_doc/Chinese-Presenters/YINXIA~1.PDF> accessed June 12, 2013.

[29] However, Thai exports to other ASEAN countries using CAFTA provisions were higher at 30.9%. See D. K. Hiratsuka, K. Hayakawa, K. Shiino and S. Sukegawa, "Maximising Benefits from FTAs in ASEAN," in J. Corbett and S. Umezaki (eds.,) *Deepening East Asian Economic Integration* (Jakarta: ERIA Research Project Report No. 1, 2008) <http://www.eria.org/publications/research_project_reports/images/pdf/y2008/no1/DEI-Ch11.pdf> accessed June 20, 2013.

[30] Christopher M. Dent, *New Free Trade Agreements in the Asia-Pacific*, at 8

[31] Asian Development Bank, *How to Design, Negotiate and Implement a Free Trade Agreement in Asia* (Manila: ADB, 2008).

[32] A. Prasert, "Thailand" in World Bank (ed.,) *Preferential Rules of Origin: Policy Research Repor*t (Washington DC: World Bank, 2007), pp. 121-27.

To be sure, CAFTA utilisation rates by ASEAN firms have increased over the past two years but still remain low. A 2010 Asia Development Bank study indicated that only 25% of Thai export/import firms used CAFTA provisions,[33] just below an ASEAN average of 28%.[34] Note also that CAFTA also sits alongside multiple FTAs in the region such as ASEAN-Korea, ASEAN-India, Thailand-Japan and Thailand-Australia. While the tariffs that were reduced to zero in 2010 represented about 70% of tariff items, they accounted for only 11% of imports into Thailand and 3% of total supply to the economy.[35]

It may be that the ASEAN-led Regional Comprehensive Economic Partnership (RCEP), which seeks to transform ASEAN's various regional FTAs into an integrated regional economic agreement, will further accelerate trade between China and Thailand. Indeed, one might argue that the RCEP initiative is explicit acknowledgment that regional FTAs including CAFTA are inadequately utilised and have hitherto fallen short of their potential. While initially slated to take effect on January 1, 2015, the ASEAN Economic Community or AEC (which includes the RCEP as one of the AEC's key pillars) is now officially postponed till December 31, 2015. The fact that a survey of 1500 Thai entrepreneurs revealed that nearly all respondents (95.56%) supported the delay – as did other ASEAN economies – in order to enhance the 'readiness' of local businesses suggests that the process will be difficult and complex, and will take some time if a successful and meaningful RCEP eventually comes into force.[36]

The history of ASEAN nations signing genuinely comprehensive 'high quality' FTAs with larger economies is not an encouraging one. Mean-

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[33] Quoted in presentation by Amado M. Mendoza Jr. and Javad Heydarian, "CAFTA Year 1 Review: Filipino Perspective," <http://iis-db.stanford.edu/evnts/6547/MENDOZA_CAFTA_Year_1_Review.ppt> accessed July 18 2013.

[34] See "China-ASEAN Free Trade Area celebrates anniversary," *China.org.cn*, February 28, 2012 <http://cn-ph.china.org.cn/2012-02/28/content_4838867.htm> accessed July 18, 2013.

[35] Siam Commercial Bank, "What is the impact of all these FTAs on Thailand?", *Economic Intelligence Center Insight*, Jan-Feb 2010 <http://www.scb.co.th/eic/doc/en/insight/SCB%20insight_Jan-Feb2010_%20Eng_FTAs.pdf> accessed July 18, 2013.

[36] See "AEC delay to late 2015 hailed by Thai private sector," *Thailand Business News*, March 13, 2013 < http://www.thailand-business-news.com/asean/45141-aec-delay-to-late-2015-hailed-by-thai-private-sector.html> accessed July 19, 2013.

while, the contemporary record serves to support the argument that while CAFTA is significant it is far from being a 'game changing' agreement in advancing a China-led economic (let alone political) regionalism as is sometimes presumed.

a) Volume of China-Thailand Trade

Trade volumes between China and Thailand grew rapidly after China joined the WTO in 2001, with an average growth rate of 26.7% per annum from 2000-2011 (even allowing for a decline in 2009 due to the global financial crisis). Thai exports to China grew from around US$4 billion in 2000, to US$18 billion in 2006, to almost US$27 billion in 2012.[37] Chinese imports into Thailand grew from around US$2 billion in 2000, to over US$21 billion in 2006, to almost $37 billion in 2012.[38] Currently at over US$10 billion, Thailand's trade deficit with China is growing more rapidly than overall growth rates in bilateral trade. Although much fanfare was made of the announcement of the 'comprehensive strategic cooperative partnership' at the heads-of-government meeting in Beijing in April 2012 – including a goal of reaching US$100 billion in bilateral trade between the two countries by 2015 – there are concerns throughout the country that this will simply lead to an even larger trade deficit with China in coming years.[39]

It is also important to note that while trade with China is growing rapidly, Japan remains Thailand's top trading partner with bilateral trade reaching US$73.06 billion in 2012, compared to US$63.86 billion with China and US$35.69 billion with the US.[40] Even so, one might argue that in addition to volumes, 'trade dependency' ratios – the proportion of exports and imports with a particular country as a proportion of overall exports and

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[37] China Customs Statistics; Thai Ministry of Commerce Statistics.

[38] As above.

[39] See Toh Han Shih, "China gaining on top Thai trade spot," *South China Morning Post*, February 27, 2013 <http://news.xinhuanet.com/english/china/2012-04/18/c_131533612.htm> accessed June 19, 2013.

[40] Thai Ministry of Commerce Statistics.

imports respectively[41] – indicate that Thai exporters could well become 'beholden' to China now or in the future.

By this measure, it is clear that China is a far more important market to Thailand, than Thailand is to China. In 2012, Thailand's export dependency to China was about 11.8%, rising from 8.6% in 2006 and 3.8% in 2000; while Thai import dependency from China was 15% in 2012. In contrast, Chinese export dependency on Thailand in 2012 was a mere 1.8%. These numbers suggest that any trade fallout between the two countries, say as a result of political or strategic disagreement, would disrupt Thailand much more than it would affect China's economy.

However, there are persuasive counter-arguments to the hypothesis that China has the levers to 'squeeze' Thailand on trade over non-economic disputes. From a comparative perspective, these dependency numbers are not unusual for countries of vastly different size. For example, Thai export dependency on Japan, the US and the EU was 10.5%, 10.9% and 9.88% respectively in 2012. Japanese, US and EU export dependency on Thailand was a mere 5.3%, 0.5% and 1% respectively.[42] The point is that the dependency imbalance between China and Thailand is not dissimilar to that between Thailand and Japan or the US. China does not *dominate* trade with Thailand when compared to these two other large Asia-Pacific economies.

Second, there is an open question as to the extent to which China is able to exercise any significant political or strategic leverage through trade with Thailand. This is a much more complex question that goes beyond looking at raw trade numbers. Of critical importance is the structure and nature of trade between the two countries. The following subsection will consider this question.

b) Structure of China-Thailand Trade

The export categories that most benefit Thailand's terms of trade are agricultural products, including food and rubber. In 2012, Thailand export-

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[41] This means that if Country A's exports to Country B was worth US$10 billion, and Country A's total export to all countries was US$100 billion, export dependency of Country A on Country B would be 10%.

[42] All calculations done using IMF Trade Statistics.

ed US$5.8 billion worth of agricultural products to China, increasing from around US$1.2 billion in 2000.[43] Chinese exports of similar categories of products to Thailand are not significant.

Even though Thai agricultural products to China have enjoyed strong growth over the past fifteen years, they are far less important to Thailand's overall terms of trade than in the past. In 1995, agricultural products constituted about 40% of all Thai exports to China, dropping to around 21% in 2012. Instead, the category of 'manufacture products' is now dominant, constituting over 68% of all Thai exports to China. Machinery equipment and parts, electronic equipment and parts, chemicals and polymers make up around two-thirds of this category.

Curiously, a large share of Chinese imports into Thailand falls into the same categories. Over US$16 billion worth of Chinese imports fall into the same or similar category of manufacture products, constituting around 45% of Chinese imports into Thailand in 2012. In 2007, the same categories constituted around 42% of total Chinese imports into Thailand. The categories helping to boost China's terms of trade against Thailand are consumer goods such as whitegoods and household electrical goods including computers.

Traditional trade theory assumes that countries produce goods and services according to their national endowments and advantages, and export these to other countries, while trade partners do the same according to their unique endowments and advantages for different products. In an era where production chains are regional and global, the practice of trade is far more complex. Moreover, in an era of cross-border technology and know-how transfer where manufacturing firms can easily relocate production processes from one country to another according to changing cost of inputs (e.g., capital, labour and raw materials,) whatever is produced in middle-income ASEAN countries such as Thailand can also be easily produced in rapidly industrialising China.

In the case of China-Thailand trade, the significant over-lapping of import and export manufacture categories is important because it indicates robust intra-industry (or processing) trade between firms from the two countries and/or competitive manufacturing structures. Indeed, this

[43] Thailand Ministry of Commerce and UN Comtrade figures.

structure replicates trade (and competition) between China and many other Southeast Asian economies such as the Philippines, Malaysia and Vietnam.

Let's first consider so-called processing trade: firms obtaining raw materials or parts from other countries, adding value to the product, and then exporting the semi-completed or completed product to another country. One interesting observation is that while trade has expanded amongst ASEAN+3 economies, it has done so in line with overall economic growth in the region. Calculations done by John Ravenhill reveal that from 1995 to 2006, the share of intra-regional trade in the ASEAN+3 economies as a proportion of their overall trade only increased from 37.6% to 38.3%. Indeed, when a 'trade intensity index' which measures the size of regional trade relative to that region's share of global GDP is applied, one finds that trade intensity in the ASEAN+3 region has remained fairly constant while trade intensity in the EU and US has increased significantly over the past few decades.[44]

To explain these phenomena, one needs to understand the role ASEAN+3 economies continue to play in export-manufacturing, with a large proportion of products destined for still dominant consumption markets in the US and EU. This is clear from figures which show that trade between China and Thailand suddenly contracted 7.24% with the onset of the global financial crisis which plunged the US and EU into recession in 2009, having grown at high double digit rates per annum for the previous decade. This trend was reflected in trade between China and ASEAN where trade contracted by 7.8% that year.[45]

Even after decades of rapid regional growth, it is often overlooked that the domestic consumption markets of the US and EU are over US$11 trillion each, compared to a Chinese and Japanese domestic consumption market of under US$3 trillion and US$5 trillion respectively.[46] Although domestic consumption in China is growing rapidly in absolute (but not relative) terms, export manufacturers have largely outsourced many stages of production to the ASEAN+3 countries and have done so for decades.

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[44] John Ravenhill, "The 'new East Asian regionalism': A political domino effect," at p. 182.

[45] Based on Thai Ministry of Commerce, Thai Customs, and China Customs figures.

[46] Based on IMF and World Bank figures.

This is clear from figures indicating that America's deficit in manufactured goods is almost entirely with Asia, while almost all of America's trade deficit with China is in processing trade (in contrast to ordinary trade where the product is solely produced in the one country before being exported.)[47]

The recent difference – particularly since early this century - is that China's rise has caused many firms to relocate export-orientated manufacturing processes from countries such as Thailand to China's Pearl River Delta region. This is reflected in the fact that around two-thirds of America's trade deficit is with China (and Taiwan), and much of the remaining third with the other ASEAN+3 economies such as Japan, South Korea and Malaysia.[48] The US also had a significant trade deficit of US$14 billion in 2011 with Thailand, on bilateral volume of US$40 billion.[49] Indeed, the Chinese Ministry of Commerce has indicated that foreign enterprises account for over half of China's exports and imports,[50] with the lion-share of foreign-direct-investment (FDI) traditionally going into the export-manufacturing sector.[51] More than 55% of export-manufacturing growth in China is driven by the activities of foreign firms.[52]

Regarding the ASEAN+3 economies as a whole, the evidence is that over two-thirds of the value of exports from the region (once the parts

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[47] Ari Van Assche, Chang Hong and Veerle Slootmaekers, "China's International Competitiveness: Reassessing the Evidence," *LICOS Discussion Papers 20508*, April 25, 2008, pg. 13 <http://www.econ.kuleuven.be/licos/publications/dp/dp205.pdf> accessed June 20, 2013.

[48] See *The Facts About Modern Manufacturing 8th ed* (Washington DC: The Manufacturing Institute, 2009) <http://www.nist.gov/mep/upload/FINAL_NAM_REPORT_PAGES.pdf> accessed June 20, 2013.

[49] Office of the United States Trade Representative figures <http://www.ustr.gov/countries-regions/southeast-asia-pacific/thailand> accessed June 24, 2013.

[50] "Foreign Direct Investment – The China Story," *World Bank news*, July 16, 2010 <http://www.worldbank.org/en/news/feature/2010/07/16/foreign-direct-investment-china-story> accessed June 20, 2013.

[51] See Dan Steinbock, "Foreign Investment Relocates in China and Asia," *Ecomonitor*, February 27, 2013 <http://www.economonitor.com/blog/2013/02/foreign-investment-relocates-in-china-and-asia/> accessed June 20, 2013.

[52] Mohamed Aslam, "The Impact of ASEAN-China Free Trade Area Agreement on ASEAN's Manufacturing Industry," *International Journal of China Studies* 3:1, 2012, pp. 43-78, at 73.

and components are taken into account) eventually end up in the EU and US markets, rising from about half in 2006.[53]

It is clear that export-manufacturers view the ASEAN+3 region as a vast production chain with little discrimination as to where they locate production processes beyond commercial motivations of (capital and labour) cost and reliability. This is important because such a trade structure gives Beijing far less capacity to use trade for political or strategic purposes than is often assumed. If Beijing were to prevent Thai firms from exporting components to China for assembly, this would merely harm its own export-manufacturing sector (which employs around 10% of the workforce or approximately 75 million people[54]) with deleterious consequences for local export-manufacturing employment, export-orientated FDI, and any resulting technology transfer that might occur. Thai firms would simply relocate part of the production process elsewhere. Indeed, given the complexity of intra-firm trade in the production process, it would be extremely difficult for Beijing to quarantine any fallout to just Thai manufacturing firms as these firms are likely to be in partnership with other multinational corporations (MNCs) in the production process.

Instead of intra-firm or processing trade, Beijing could attempt to target Thai exports of commodities to its markets. This would cause a different set of problems. The southern provinces and regions such as Yunnan and Guangxi which purchase much of the Thai agricultural produce would suffer from any disruption.[55] Likewise, China is the largest consumer of natural rubber in the world, accounting for over one third of global rubber consumption in 2011. Over 80% of China's rubber is imported from Thailand, Malaysia and Indonesia which together with India and Vietnam

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[53] John Ravenhill, "The 'new East Asian regionalism': A political domino effect," at 182; Asian Development Bank, *Emerging Asian Regionalism: A Partnership for Shared Prosperity* (Manilla: ADB 2009).

[54] "Foreign Direct Investment – The China Story."

[55] It takes more than 2 weeks for landlocked provinces like Yunnan to import agricultural products from Southeast Asia by sea, but only 2-3 days via the Kunming-Bangkok Highway. See "R3 Road helps increase Thai-fruit export to China," *NNT Time*, August 6, 2012 <http://www.xsbnnews.com/html/2012-08/984.html> accessed 21 June 2013.

account for around 85% of global production.[56] Once again, China can ill-afford any disruption in this commodity.

Moreover, although manufacturing MNCs are the great beneficiaries of regional production networks as this allows them to lower costs and raise efficiencies, wholly Thai-based manufacturers (mainly small and medium-size enterprises or SMEs) are the potential losers; while the loss of local manufacturing jobs is a concern for all Asian governments with still young populations.[57] In this context, there is strong evidence that China-Thailand trade is becoming more competitive rather than complementary in the critical export-orientated sector. Focusing on the electrical and electronic (E&E) sectors, which is important to both Thailand and China, is instructive as the majority of export-orientated products from ASEAN and China are E&E.[58]

In an analysis of Chinese E&E exports from 1992-2005, 'high technology' products now comprise over 30% of exports, with a growth rate of 32% per annum over the period. The second fastest growing category is 'medium high technology' products, having grown at 22% over the same period. Both these sub-categories outpace 'medium-low technology' and 'low technology' sub-categories, giving a strong indication that Chinese exports are moving up the value chain of production.[59]

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[56] *Global and Chinese Natural Rubber Industry Report*, 2012 (San Francisco: Business Wire, 2012.)

[57] On competition in manufacturing jobs between China and Southeast Asian economies such as Thailand, see *Business Trends 2013: Adapt, Evolve, Transform* (Westlake: Deloitte University Press 2013) <http://cdn.dupress.com/wp-content/uploads/2013/03/2013-SO-Business-Trends_vFINAL.pdf> accessed July 3, 2013; Yukon, "China's economic rise: opportunity or threat for East Asia?", *East Asia Forum*, May 20, 2012 <http://www.eastasiaforum.org/2012/05/20/chinas-economic-rise-opportunity-or-threat-for-east-asia/> accessed July 3, 2013.

[58] Mohamed Aslam, "The Impact of ASEAN-China Free Trade Area Agreement on ASEAN's Manufacturing Industry." Note that intra-firm trade in E&E took off in the region from 1996 onwards following the signing of the WTO's Information Technology Agreement in 1996 by all major regional economies. Only Brunei, Myanmar, Cambodia and Laos remain non-signatories.

[59] Ari Van Assche, Chang Hong and Veerle Slootmaekers, "China's International Competitiveness: Reassessing the Evidence."

Even though it is difficult to know the extent to which Chinese-based firms are genuinely adding value to products (as there is also evidence that China is importing more 'high tech' and 'medium high tech' parts and components for assembly before shipping the goods out again,[60]) the point is that Chinese-based firms are becoming direct competitors of Thai-based firms that have traditionally done well in the 'high technology' and 'medium-high technology' sub-categories. These include parts and components from end consumer products such as mobile phones, TVs, computers and computer accessories. A similar competitive situation exists between Chinese and Thai manufacturers in sectors that have traditionally been strong for Southeast Asian countries such as lower-end whitegoods, apparel, footwear, leather, metal products and furniture. Since competition for export-orientated job creation, markets and capital is intensifying rather than subsiding between Chinese and Thai manufacturers, the capacity of Beijing to offer or else retract largesse through levers from the trading relationship appears overstated.

CHINESE INVESTMENT IN THAILAND

In July 2009, then Premier Wen Jiabao urged the audience of Chinese diplomats to "hasten the implementation of our 'going out' strategy and combine the utilisation of foreign exchange reserves with the 'going out' of our enterprises."[61] According to Qu Hongbin, chief China economist at HSBC, "This is the first time we have heard an official articulation of this policy… to directly support corporations to buy offshore assets"[62] even though the modern version of the 'going out' strategy was first officially articulated in the 10th Five Year Plan (2001-2005.) The fact that Chinese

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[60] The same authors above look at China's ordinary exports (exports solely produced in China) and find that the vast majority remain on the 'low-tech' and 'medium low-tech' levels, suggesting that Chinese manufacturing still add far less value to processed E&E products than is generally assumed.

[61] "China to deploy foreign reserves," *Financial Times*, July 21, 2009 <http://www.ft.com/intl/cms/s/0/b576ec86-761e-11de-9e59-00144feabdc0.html> accessed June 22, 2013.

[62] Quoted in above.

state-owned-enterprises (SOEs) – receiving coordination and support from state agencies such as the National Development and Reform Commission, Ministries of Finance and Commerce, and the State Administration of Foreign Exchange – accounted for around 90% of all cumulative overseas or foreign direct investments (FDI)[63] registered at the end of 2011[64] further increases suspicion that political and strategic motivations could be behind some Chinese investment decisions in foreign markets[65] -- even if we accept the sage observation that so-called 'China Inc.,' is not monolithic but comprised of many different entities, interest groups and influences that are often in competition and even conflict with each other.

In assessing motivation and capability, the key is to look at the nature and scale of Chinese FDI in Thailand.

In relative terms, the heyday of Chinese FDI into Thailand occurred from the mid-1990s to around 2003 when it was estimated that cumulative Chinese FDI grew from around US$12 million in the 1980s, to about US$70 million in the 1990s, to approximately US$1.19 billion by 2003.[66] Target sectors were diverse and spread evenly across the Thai economy, with the majority of FDI going into agriculture, textiles, metal products and machinery, E&E parts and products and chemicals.[67]

In recent times, Thailand has become a less important and less significant destination for FDI. According to Bank of Thailand (BoT) figures, outstanding (or still active) Chinese FDI into Thailand in 2011 was US$1.23 billion. This compares with US$46.86 billion from Japan, US$24.11 billion from Singapore, US$13.40 billion from the US, US$9.30 billion from the Netherlands, US$6.12 billion from the UK, US$3.24 from France,

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[63] The IMF definition of FDI is used and is defined as a foreign entity's ownership of a domestic company's equity of 10% or above.

[64] See Jack Perkowski, "Get Ready For More Chinese Overseas Investment," *Forbes*, March 10, 2012 <http://www.forbes.com/sites/jackperkowski/2012/10/03/get-ready-for-more-china-overseas-investment/> accessed June 21, 2013.

[65] For a discussion of this issue, see Charles W. Freeman III and Wen Jin Yuan, "China's Investment in the United States – National Initiatives, Corporate Goals, and Public Opinion," *CSIS Freeman Briefing Report*, November 2011 <http://csis.org/files/publication/111107_Freeman_Briefing_China_Investment_in_US.pdf> accessed June 23, 2013.

[66] United Nations Conference on Trade and Development figures from 2003.

[67] Thai 2006 Bank of Investments figures.

US$3.23 billion from Germany and US$3.21 billion from Malaysia. Counting ASEAN and the EU as whole entities, outstanding FDI in Thailand is US$27.68 billion and US$25.92 billion respectively. (See ***Table 1*** for a summary).

To put the relative insignificance of Chinese FDI in another way, outstanding investment from China constituted about 0.81% of all FDI into the country. Even though Chinese FDI figures tend to be slightly understated for a number of accounting and transparency reasons, and there have been complaints about the accuracy of BoT figures, we can be reasonably sure that Chinese FDI as a proportion of all outstanding FDI into Thailand is not far above 1% of the total.[68]

Table 1: Outstanding (or active) FDI in Thailand in US$ billions

Country/Grouping	**2011**	**2009**	**2006**
ASEAN	27.68	18.80	13.21
EU	25.92	20.64	14.23
Japan	46.86	36.83	27.65
Singapore	24.11	16.08	11.75
US	13.40	10.48	9.13
Netherlands	9.30	7.40	4.82
France	3.23	1.87	1.73
Germany	3.23	2.69	2.48
Malaysia	3.21	2.40	1.27
China	1.23	0.55	0.37
Total	**150.52**	**110.07**	**80.54**

Source: Bank of Thailand (Last updated, October 1, 2012.)

[68] Note that some studies have higher levels of Chinese FDI into Thailand. For example, see Shen Hongfang, "The Economic Relations between China and Thailand under the Context of CAFTA: An Assessment," *Chinese Studies* 2:1, 2013, pp. 52-60. BoT figures have been used because these figures only include known capital that was actually brought into Thailand, not figures based on Memoranda of Understanding or regulatory approvals where actual capital utilisation in Thailand is not known.

These figures should put to rest comparisons between Chinese FDI activity in a much more diverse and open economy such as Thailand's compared to such activity in neighbouring Cambodia which is seemingly being pulled into Beijing's political orbit. From 1994-2011, Chinese FDI into Cambodia had reached a cumulative US$8.8 billion, with South Korea second at US$4 billion and Malaysia third at US$2.6 billion – the Chinese figure being over 22% of all FDI received during that period.[69] Chinese companies (mainly SOEs) are the dominant foreign investors in major 'nation building' projects in the mining, infrastructure, petroleum and energy sectors.[70]

The nature of Chinese FDI into Thailand also suggests that an increasing majority of it is destined for the intra-firm or processing trade sectors. From 2000-2010, 57% of FDI into Thailand went into the manufacturing industry, with finance the next largest at 11%. In 2012, the proportion of FDI that went to the Thai manufacturing was around 61.5%, rising from 55% in 2011.[71] Within the Thai manufacturing sector, the four key subsectors attracting FDI were E&E, chemicals, rubber and plastic products and motor vehicle parts and components (in descending order.) Chinese FDI activity in Thailand does not deviate significantly from these trends. This suggests that Chinese firms (along with most East Asian and ASEAN counterparts) mainly view Thailand as just one option out of several in Southeast Asia (along with the Philippines, Indonesia, Vietnam and Cambodia) with respect to the regional export-orientated manufacturing supply chain.[72]

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[69] Figures from Cambodia Investment Guide and Council for Development of Cambodia 2012. Quoted in Heng Pheakdey, "Cambodia-China Relations: A Positive Sum Game?" *Journal of Current Southeast Asia Affairs* 2, 2012, pp. 57-86 at 61 <http://journals.sub.uni-hamburg.de/giga/jsaa/article/viewFile/545/543> accessed June 24, 2013.

[70] Examples include China Railway Construction Corporation to invest US$11.2 billion over the next four years to build a 400km railway, steel plant and seaport which is the biggest investment in Cambodia to date. China's Perfect Machinery Industry Corp signed a US$2.3 billion contract with Cambodia's Petrochemical Company in 2012 to build the country's first oil refinery plant. China's Guangdong Agribusiness Group committed US$425 million in 2012 towards rubber estates in Cambodia's Kratie and Mondulkiri provinces.

[71] Bank of Thailand figures.

[72] Of these Southeast Asian countries, Thailand has the highest average monthly wages

This is significant because there is little evidence that a significant amount of Chinese FDI into Thailand has strategic or political motivations attached to it.

Unlike in Cambodia, Thai sectors open to FDI do not tend to correspond with the sectors deemed 'strategic' or 'important' by the Chinese Communist Party and enshrined in the 12th Five Year Plan (2011-2015). This is important because institutional, financial and personnel links between 'national champions' in these sectors on the one hand, and CCP and political agencies on the other tend to be the most intimate – raising suspicion that 'national champions' are ultimately tools of the CCP and the Chinese government even if they pursue commercial interests in the vast majority of their transactions.[73] The seven CCP 'strategic sectors' encompass new forms of energy, next-generation information-technology (e.g., cloud computing), bio-technology, advanced equipment manufacturing, aerospace, new materials and advanced vehicles. Traditionally 'important' sectors include finance, high-end services sectors, fossil fuels, mining and minerals, traditionally IT, and aviation and heavy industries. SOEs and especially 'national champions' in these sectors overwhelmingly take the lead in these 'strategic' and 'important' sectors. This is reflected in analyses of Chinese FDI around the world in which sectors such as energy (47%), metals (16%) and transportation (14.7%) dominate in volume as they constitute the largest transactions, while the strategic sectors dominate when it comes to Chinese SOE interest in advanced economies.[74]

When 'strategic' and 'important' sectors for the CCP are not in play – as is the case of SOEs in Thailand – central officials tend to allow provincial authorities to take the lead. The point is that it is rare for Beijing to

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in the manufacturing sector, although Thailand's advantage is strengthened by its relatively well-trained and reliable manufacturing workforce, solid institutions and developed capital markets. See Yifan Hu, "ASEAN: A Hot Destination for Outbound Investment," *PIIE China Economic Watch*, June 5, 2013 <http://www.piie.com/blogs/china/?p=2677> accessed June 23, 2013.

[73] See John Lee, "China's Corporate Leninism," *The American Interest*, May/June, 2012 < http://www.the-american-interest.com/article.cfm?piece=1231> accessed June 23, 2013.

[74] See Heritage China Global Investment Tracker < http://www.heritage.org/research/projects/china-global-investment-tracker-interactive-map> accessed June 24, 2013.

exercise or impose significant oversight over what Chinese central and provincial SOEs do in Thailand.

An even examination of Thai FDI into China reveals that China is far from being a dominant destination for Thai FDI. Cumulative investment rose from US$788.51 million in 2006, to US$1.92 billion in 2009, to US$2.28 billion in 2011. This represented 9.2% of all Thai FDI in 2006, 11.17% in 2009, and 5.62% in 2012 – proving that China is far from being a dominant investment destination for Thai firms while future trends remain uncertain. Given that the majority of Thai FDI into China is destined for the export-orientated industry, Thai FDI figures as a proportion of total FDI could well fall as manufacturing wages in China are now over twice as high as in other developing countries in Asia.[75] Indeed, Singapore remains the single most important FDI destination for Thai firms, with US$5.97 billion in 2011 (14.7% of total Thai FDI.)[76] The rest of ASEAN received US$12.13 billion of Thai FDI in 2011 (29.9% of total Thai FDI.)

CHINA'S PSYCHOLOGICAL CAPACITY TO INTIMIDATE AND SEDUCE

This *Paper* argues that Beijing lacks the economic levers to *coerce* Bangkok towards its political and strategic sphere of influence. Although China is growing in importance as a trade and investment partner of Thailand's, it is also argued here that China's capacity to use economic levers to *persuade* or else *seduce* Thailand to change its political or strategic orientation is still limited, and any such capacity is not likely to eventuate in the foreseeable future.

Reality based on objective numbers is one thing. *Perception* based on the inevitability of China's rise to a position of economic and possibly strategic dominance in Asia is another. Although China is nowhere near as dominant an economic partner (and strategic player in Asia) as

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[75] Yifan Hu, "ASEAN: A Hot Destination for Outbound Investment," *PIIE China Economic Watch*.

[76] Bank of Thailand figures.

is commonly made out, the persistent underlying assumption in conversations with Thai elites encompassing government and bureaucratic officials, business leaders, think-tankers and academics is that China and not the US or Japan will be the more important economic power in the future.[77] This same sentiment was reported almost a decade ago in a confidential 2004 cable (that was subsequently released by Wikileaks) by then American Ambassador Darryl Johnson who observed that Thai experts tend to accept China's growing power as inevitable, are generally positive about China's continued goodwill in the region as its power grows, and see China's rise as an opportunity rather than a threat even if Thai officials are eager to preserve the security alliance with Washington well into the future.[78] More recently and according to a 2013 study, more Thais consider China rather than the US, Japan or Singapore as a 'model' for their country.[79]

As an enormous and fast growing authoritarian state that is already integrated into the existing regional economic order, China also has the greater psychological capacity to *intimidate* and/or *seduce* even if material reality does not support this conclusion. In terms of Beijing's capacity to intimidate, it is telling that there was widespread scepticism and even

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[77] All conversations were off-record and took place from May 27-31 in Bangkok. They were conducted in English. Fourteen conversations took place during this time. Two officials (Director-General and First Secretary levels) were from the Ministry of Foreign Affairs. Three academics were from Chulalongkorn University, and one was from the University of the Thai Chamber of Commerce. Four were researchers from the Thailand Development Research Institute. Three officials were from the Australian High Commission in Bangkok (including the High Commissioner) and one official was from the American Embassy in Bangkok. Conversations covered the Sino-Thai economic, defence and political relationship, the Thai economy and attitude to regionalism and FTAs, and future Thai challenges and responses.

[78] Confidential cable on "Thai views of a more assertive China," October 20, 2004 <http://thaicables.wordpress.com/2011/07/06/04bangkok7313-thai-views-of-a-more-assertive-china/> accessed July 18, 2013.

[79] 16.2% of Thais surveyed considered China as a model, compared to 15,5%, 12.4% and 8.4% for the US, Japan and Singapore respectively. Note that 46% of Thais believed that the country needed to find its 'own' model: Min-Hua Huang and Bridget Welsh, "Follow the Leader? Soft Power of China and the US Compared," *Paper prepared for delivery at conference on 'China's Rise: Assessing Views from East Asia and the United States,' at the Brookings Institution*, March 29, 2013 <http://www.asianbarometer.org/newenglish/publications/ConferencePapers/2013_3conference/paper4.pdf> accessed July 18, 2013.

concern amongst elites and in the Thai media that the US 'rebalance' or 'pivot' to Asia could place Thailand (a US treaty ally) in a difficult position and "spoil Thailand's strong ties with China." This was reflected in a poll conducted just prior to President Barack Obama's visit to Thailand in November 2012 in which more people believed that the American pivot was 'bad' because it would negatively affect Sino-Thai relations (36.09%), than those who consider the 'pivot' a 'good' thing (27.35%.)[80]

More generally, and in the absence of specific threats, as from Communism during periods of the Cold War, Thailand's strategy vis-à-vis great powers has been to maintain a studied stance of neutrality between them, and to only overtly pick a side if it is the winning one. But there is a difference between studied neutrality and gradually drifting towards one side or the other. While US officials remain reluctant to recognise that Bangkok could be drifting away from its strategic orbit, the tendency to pre-emptively appease a diplomatically assertive and occasionally prickly China is effectively allowing Beijing a greater role in redefining and channelling the direction of Bangkok's ostensibly neutral strategic direction.

Further argument that the rise of authoritarian China is both intimidating Thai officials and seducing its other elites is put forward by one commentator who insightfully points out that "When Thailand announced its intention, in 2010, to become a 'strategic partner' of China, there were few, if any, public concerns expressed [as to] how this [new] relationship could potentially damage its [existing] relationship with the United States, Japan, South Korea and other ASEAN members, especially those ASEAN members who are claimants in territorial disputes with China over the South China Sea." As he concludes, "Apart from revealing Thai public ignorance of regional affairs, this also gives an insight into the success of Chinese public diplomacy in Thailand."[81]

In economic matters, the fear and lure of China is also apparent in Thailand's impending decision on its four high-speed train lines from Bangkok to Chiang Mai, Nong Khai, Rayong and Padang on the Malaysia

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[80] NIDA Poll, November 8-9, 2012 < http://nidapoll.nida.ac.th/main/index.php/en/2012-08-06-13-57-45/339-114-2555> accessed July 18, 2013.

[81] Sasiwan Chingchit, "After Obama's Visit: The US-Thailand Alliance and China," *East-West Center Asia Pacific Bulletin Number 189*, December 4, 2012 <http://www.eastwestcenter.org/sites/default/files/private/apb189.pdf> accessed June 24, 2013.

border as part of the government's US$65 billion plan to improve the country's transport infrastructure up to 2019. At least four countries – China, France, Japan, South Korea and Spain – have expressed an interest in bidding for the contracts. Conversations with Thai officials and academics confirm that the future economic and political consequences of *not* awarding the contract to Chinese bidders are being closely considered. No such concern was detected if bidders from the other countries were to fail.

Indeed, the same observation can be made about Thailand's ambivalence towards participating in negotiations for the Trans-Pacific Partnership (TPP) which many in Beijing view as an attempt by America to economically 'contain' China.[82] After apparently expressing interest in joining the TPP in the lead-up to American President Barack Obama's visit in November 2012,[83] Bangkok appeared to subsequently backtrack on its position several months later when pressed by Chinese officials to state Thailand's position[84] –ambiguity which is likely to increase US frustration.[85]

To be sure, a rapidly growing Chinese psychological capacity to seduce is immensely aided by the lack in recent history of enmity between the two countries, the absence of major territorial disputes, and the powerful presence and role of ethnic-Chinese Thais comprising about 20% of the population, many of whom constitute the political, business and social elites. The overwhelming anecdotal evidence shows that many ethnic-Chinese Thais see China's rise more as an opportunity and much less as a threat.[86]

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[82] For example, see "US using rules to contain China," *People's Daily*, February 2, 2012 <http://www.china.org.cn/opinion/2012-02/02/content_24530216.htm> accessed June 24, 2013.

[83] "China to join TPP talks," *Bangkok Post*, November 13, 2012 <http://www.bangkokpost.com/news/local/320886/thailand-to-join-tpp-talks> accessed June 24, 2013.

[84] "Thailand denies being involved in US-led TPP talk," *Xinhua*, April 26, 2013 < http://www.globaltimes.cn/content/777785.shtml#.UcfU7_ImhcY> accessed June 24, 2013.

[85] Petchanet Pratruangkrai, "US wants Thai decision," *The Nation*, April 13, 2013 <http://www.nationmultimedia.com/business/US-wants-Thai-decision-30179907.html> accessed July 3, 2013.

[86] For example, see Tomoyoshi Isogawa, "Deepening economic ties: Thai conglomerate backs Chinese firm's expansion overseas," *The Asahi Shimbun*, April 28, 2013 <http://ajw.asahi.com/article/globe/feature/china/AJ201304280011> accessed July 19, 2013;

The lure of China is confirmed by the fact that there are more Confucius Institutes and classrooms in Thailand than anywhere else in Asia. There are more Thais studying in Chinese universities than from any other ASEAN country, with only the US, Japan and South Korea sending more students than Thailand to China. There are more Chinese students in Thai universities than students from any other country.[87] Despite its greater economic importance, Japan and even the US do not generate the same level of appeal and excitement for many Thais.[88]

CONCLUSION

As a small middle power in the Asia-Pacific, Thailand's record of deft diplomacy vis-à-vis great powers is admirable and impressive. The country's history of amity with China and its currently strong relations with Beijing is an advantage for Bangkok. But in projecting far into an unknowable future, many Thais appear to be ignoring economic facts and foreseeable trends that suggest that Thailand is not now, and will not be as dependent on the Chinese economy as neighbours such as Cambodia and Myanmar have become.

This is not to deny that managing relations with China should be a high priority for Thailand. But positioning itself too early for a China-dominated Asia – and taking an unbalanced view of China's importance to its future – when the material evidence points to a far more diverse and complex strategic and economic reality is a danger. Doing so could jeopardise the future of its treaty alliance with the US, strain relations with still more important economic partners such as Japan, and inhibit

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Patrick Ong, "Chinese Identity in Thailand and Singapore," April 19, 2012 < http://www.catandnat.com/pages/content/chinese-identity-thailand-and-singapore#.Uef1R41mhcY> accessed July 19, 2013

[87] Zhao Xin-Cheng, "Sino-Thai Educational Exchanges and Cooperation in the case of Confucius Institutes," *Paper presented to first Thai-Chinese Strategic Research Seminar*, Bangkok, August 24-26, 2012 <http://www.nrct.go.th/th/Portals/0/data/%E0%B8%A0%E0%B8%95/2555/10/1stThai-Chinese_doc/Chinese-Presenters/ZHAOXI~1.PDF> accessed June 23, 2013.

[88] Min-Hua Huang and Bridget Welsh, "Follow the Leader? Soft Power of China and the US Compared."

Thailand's capacity to play a more constructive and pro-active role within ASEAN vis-à-vis the growing strategic difficulties associated with China's rise – for little additional economic or strategic gain.