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<https://escholarship.org/uc/item/7tz1x1jq>

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### Publication Date

1998-07-01

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# ASSESSING THE POLICY OF ENGAGEMENT WITH CHINA

by *Paul A. Papayoanou and Scott L. Kastner\**



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The simple truth is this: the direction China takes in the years ahead will be one of the most decisive factors that will determine whether the next century is one of conflict and cooperation. The emergence of China as a great power that is stable, open and nonaggressive; that embraces political pluralism and international rules of conduct; that works with us to build a secure international order, the emergence of that kind of China profoundly is in America's interest....The results are far from pre-ordained: inward looking isolation, or outward looking integration? As we create the structures and policies that will become the foundation for security and prosperity into the new century, one of our most critical challenges is to bring China into the effort as a stakeholder, to make the choices ourselves that will make it more likely China makes the right choices.

—U.S. National Security Advisor Samuel R. Berger, 6 June 1997<sup>1</sup>

## INTRODUCTION

China is increasingly seen to be the most significant and potentially troubling great power for the United States in the years to come. China's military and economic power are clearly substantial and on the rise. In East Asia, China has the largest population, most land, and spends the greatest amount on defense expenditures. Its economy is a close second to Japan's, and third in the world.<sup>2</sup> China's economic growth rate has averaged a remarkable 12 percent in recent years, and the Chinese economy is projected to be larger than America's early in the twenty-first century. China also has the third largest nuclear arsenal and the largest army in the world, and its military expenditures are by some estimates growing about 10 percent per year. China's power capabilities clearly make it a serious potential challenger to the international status quo and to the United States (Segal 1996; Zakaria 1997; Goldstein 1997/98).

There are also reasons to be concerned about how China will use its capabilities in the years to come. China has significant territorial interests in Asia and broad geopolitical interests in the world that make conflictual scenarios quite possible. China's territorial interests overlap with those of 24 other countries, and threats or uses of military force in the Taiwan Straits in 1995–96 and in the South China Sea in 1995<sup>3</sup> give reason to be wary of Chinese intentions. China has also engaged in the proliferation of weapons of mass destruction with rogue states such as Iran. And China has not been afraid to flex its muscles in noncooperative ways in international forums, as it did in the UN Security Council in the

winter of 1998 regarding the arms inspections dispute with Iraq. Finally, because China is a nondemocracy, there is reason to worry that its government can act

recklessly in the international arena without regard for public accountability (Segal 1996; Zakaria 1997; Goldstein 1997/98).

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\* We thank Jean-Marc Blanchard, Stephan Haggard, and the participants at the Workshop on Economic Power, Interdependence, and National Security held at The Ohio State University, 3–4 April 1998, for their comments. We retain full responsibility for all errors and shortcomings. Further comments to: <ppapayoa@weber.ucsd.edu> are welcome.

<sup>1</sup> "Building a New Consensus on China," Speech to Council on Foreign Relations, New York, New York. <http://www.whitehouse.gov/WH/EOP/NSC/html/speeches/srb060697.html>

<sup>2</sup> Defense figures and the size of the economy (Gross Domestic Product) are based on purchasing power parity.

<sup>3</sup> This refers to China's seizing of Mischief Reef from the Philippines.

Clearly China is, and will continue to be for some time to come, a great concern to U.S. administrations. The Clinton administration has chosen to pursue a policy of engagement with China, arguing that it is best to try to bring China into “the community of nations” rather than to contain and isolate it. Integrating China through a policy of engagement has meant, most importantly, the maintenance and expansion of American trade with, and the encouragement of investments in, China. There have been some limits to the administration’s policy though, for a tough line has been taken toward China on membership in the World Trade Organization (WTO) and on the piracy of intellectual property (e.g., compact discs and videos).

What are the security implications of such a policy?<sup>4</sup> This paper focuses on the impact that America’s economic relations in the policy of engagement with China have had, and will likely have, on the nature of Chinese foreign policy and on U.S.–Chinese security relations. In short, we argue that a policy of engagement will have beneficial consequences. Such a policy empowers more pacific economic internationalists in China, while containment would likely weaken those forces and might bring to the fore more aggressive political and economic interests. The risks of engagement are also insignificant in the near term. Because U.S. economic stakes in China are fairly small, they do not carry the danger of tying the hands of U.S. leaders should the Chinese pursue conflictual policies that require the United States to balance against China. A policy of engagement thus promises greater benefits than containment, with few risks.

## ECONOMIC TIES AND FOREIGN COOPERATION

Our assessment draws on theory and salient historical examples. Theoretically, we argue that the cultivation of extensive economic ties with nondemocratic great powers will in some cases have dangerous consequences, while in other cases the economic links may foster pacific foreign policies and credible commitments to cooperate. What determines whether economic ties will make a nondemocracy’s foreign policy more cooperative than conflictual is how much influence internationalist economic interests in the nondemocratic state have in the polity. If the

dominant political coalition comprises leaders or groups with internationalist economic interests, the cultivation of economic ties should have positive effects. If internationalist economic interests are not influential, economic ties are far from being a guarantee that a potential adversary will pursue pacific and cooperative foreign policies. Indeed, domestic-oriented economic interests may feel threatened by an expansion of economic links and seek to assert political control to prevent a diminution of their economic benefits and political position, which could lead to conflictual foreign policies. On the other hand, severing economic ties with such a government may insure that aggressive interests dictate foreign policy, for internationalist economic interests would certainly have no chance of becoming empowered. Understanding the dynamics economic ties generate in the domestic political process of a nondemocratic state is therefore crucial to evaluating the relative merits of engagement and containment policies.

We also argue that if a democracy cultivates extensive economic ties with a potential adversary, that will generate domestic political constraints that will make it difficult for democratic leaders to balance against and deter such an adversary should the need arise. Leaders should thus be cognizant that, while opening and closing economic ties are political decisions, creating extensive ties takes a long time and closing them is politically difficult once they are significant. Hence, economic statecraft is best employed when economic ties are minimal, and leaders should have an eye on the long-term security implications of such policies.

To illustrate the argument and offer an assessment of the U.S. policy of engagement, we refer also to two cases of nondemocratic powers that had extensive economic ties with democratic great powers: czarist Russia and its economic and political-military relationship with France in the late nineteenth and early twentieth centuries; and Wilhelmine Germany, which had extensive economic ties with Britain particularly, but also other great powers, before the First World War.

The theoretical and historical discussions, together with an analysis of the Chinese political economy, allow us to evaluate whether U.S. foreign economic policies toward China are likely to have beneficial or potentially dangerous effects on Chinese foreign policy and U.S.–Chinese relations. Our conclusion is that, while it is difficult to get a handle on the precise nature of the Chinese political economy, the available evidence suggests that the United States should continue to pursue the policy of

<sup>4</sup> Much of the debate centers around the effects of engagement versus containment on human rights in China. We do not address that issue, but see Lilley 1994, Bernstein and Dicker 1994, Harland 1994.

engagement at least into the near future. The Chinese leadership and a substantial portion of the “selectorate” in China appear to be committed to, or benefitting from, economic integration. Engagement will foster those interests and make an aggressive, conflictual foreign policy from China unlikely. Containment, by contrast, could weaken economic internationalists and strengthen inward-looking economic forces and those with aggressive motives, making a pacific foreign policy much less likely. Moreover, we argue, the policy of engagement carries few risks. The small size of the U.S. economic stake in China means that U.S. leaders are unlikely to have their hands tied by economic interests in the United States if it is necessary to balance against an aggressive Chinese foreign policy, at least into the near future.

The paper proceeds by first elucidating the analytical argument. We then examine the two salient historical precedents mentioned above, czarist Russia and its economic and political-military ties with France, and Wilhelmine Germany and its relations with Britain. The nature of China’s political economy and its implications for Chinese foreign policy are then explored. Our assessment of the implications for the U.S. policy of engagement and policy recommendations follow.

### **How States' Political Institutions Aggregate Economic Interests**

To determine whether the U.S. policy of engagement will serve to bring China into the community of nations and prevent it from becoming a serious threat in the Asia-Pacific and elsewhere, we focus on how states’ domestic political institutions aggregate economic interests. This process influences whether economic ties are seen as beneficial, pernicious, or inconsequential, which in turn determines whether having extensive economic ties with other states will elicit generally cooperative behavior and a pacific foreign policy.<sup>5</sup>

In democracies, economic interest groups and the society-at-large as voters are fairly powerful in relation to the state. State leaders in democracies will therefore be constrained to pursue policies that are largely consistent with the median preferences of vested interests. Democratic leaders will also need to be concerned with the prospective adjustment costs to their economies in the event of a breakdown in

economic ties, and will be sensitive to the effects of costly security policies on their economies. Democratic states will, therefore, tend to pursue cooperative policies with, and be able to make credible commitments to, those on which they are economically dependent.

Leaders will have similar sensibilities and pursue similar foreign policies in those nondemocracies in which the dominant political coalition comprises internationalist economic interests. This will be the case when the leadership is highly autonomous and sees economic ties as crucial to fulfill its goals or when the most politically prominent societal groups have internationalist economic interests. Nondemocratic leaders in such states, like those in democracies, will therefore be influenced in a strong, positive way by their states’ economic ties. Leaders of such states will tend to pursue cooperative foreign policies with major economic partners that will help preserve the stake that the dominant political coalition has in the economic ties.

Will such states be able to make their commitments to cooperate credible? If the leadership is highly autonomous from domestic economic interests, credibility may be somewhat difficult since the leaders are unconstrained by societal forces. However, this credibility problem will be offset to the extent that the nondemocratic state’s economic policies favor internationalization, for such policies are hard to alter significantly. As discussed below, czarist Russia in the late nineteenth and early twentieth centuries had a government that was quite autonomous from societal economic forces and yet its high dependence on foreign capital to achieve its modernization goals and finance its public debt was readily apparent to the French. Thus, Russian commitments were credible because French leaders saw how dependent the czarist government was on money from France.

In other nondemocracies, by contrast, internationalist economic concerns may play only a small role, if any, in the political process. In many authoritarian regimes, for instance, the leadership is quite autonomous from societal forces and sees nationalistic economic policies as best for development (such as import-substitution industrialization strategies). And in praetorian politics the institutional framework may not effectively assimilate struggles between competing groups; thus, narrow (economic or noneconomic) interest groups with disproportionate influence can capture national policy and shift it away from the preferences of median internationalist economic interests (Huntington 1968, 81–82, 195–198; Gordon 1974;

<sup>5</sup> The argument in this section is adapted from Papayoanou 1996, 1997, and 1998, ch. 2.

Snyder 1990, 1991). In such cases, extensive economic ties will not have salience or will even be seen as threatening by powerful domestic-oriented economic interests.

These states will thus be less inclined to pursue cooperative policies and any commitments to cooperate they make will lack credibility. Great powers with such domestic political institutions may also pursue conflictual policies despite being strongly tied to other great powers in the international economy. If the political institutions have given disproportionate influence to domestic-oriented economic or other narrow interests over internationalist economic concerns, those interests may have an incentive to pursue a noncooperative and aggressive rather than pacific foreign policy even if there are extensive economic ties to other great powers. As discussed below, Wilhelmine Germany pursued aggressive policies despite being highly dependent on the international economy because its political institutions gave domestic-oriented economic and military interests disproportionate influence.

This discussion leads to two concerns for a democracy considering cultivating extensive economic ties with a nondemocracy. First, it is important to understand whether the institutions of the nondemocracy are likely to permit internationalist economic concerns to wield significant influence in the political process. Second, democratic leaders should be concerned with the effects that economic ties will have on their ability to balance a future threat from a nondemocracy. Vested interests with extensive ties to a state deemed by democratic strategists to be a threat, and political leaders with concerns about prospective adjustment costs, will fear that confrontational policies could lead to a severing of economic links. Democratic strategists may therefore be constrained from balancing against a threat with which their state has extensive economic links. This was the case, as discussed below, for British strategists in the period preceding 1914, for they were constrained by internationalist economic concerns stemming from Britain's ties with Germany. As a result, Britain pursued an ambivalent "straddle strategy" (G. Snyder 1984) rather than a firm balancing effort that might have deterred the Germans from launching the Schlieffen Plan. For this reason, and because of the institutional biases of German political institutions, economic ties were not conducive to peace in 1914.

To illustrate the argument, we turn to a discussion of the historical cases mentioned to this point. The argument is then applied in an analysis of

the Chinese political economy. The implications for Chinese foreign policy and the U.S. policy of engagement are then drawn out.

## Czarist Russia versus Wilhelmine Germany

We ground the analytic discussion with an examination of how economic ties influenced czarist Russia and its political-military relationship with France in the late nineteenth and early twentieth centuries, and Wilhelmine Germany and Anglo-German relations before 1914. These cases are useful analogues for the discussion of China's political economy and U.S.–Chinese relations.

First, czarist Russia and Wilhelmine Germany are analogous to China today in several ways. Like China, neither can be considered to have been a democracy. Moreover, both undertook substantial efforts to modernize their economies, and international economic ties were integral to their economic development. Finally, the leadership in both countries wanted to modernize not only for economic reasons, but also because they felt it necessary to improve their relative political-military power. All of these characteristics apply to China today.

The Franco-Russian and Anglo-German dyads are also similar to the U.S.–China relationship in at least two respects. For one, these are all relationships among great powers. Second, they involve the cultivation of economic ties between a democracy and a nondemocracy.

Despite crucial similarities between czarist Russia and Wilhelmine Germany, and in their economic ties with democratic great powers, the two countries pursued different foreign policies, with different implications. Czarist Russia agreed to political-military collaboration with France. Although it pursued some aggressive policies and was seen as having some potential for recklessness, Russia was overall an accommodating and credible ally for France. Wilhelmine Germany, by contrast, undertook highly aggressive behavior in the international arena, while Britain, the pivotal actor in balance-of-power politics in the decade preceding 1914, pursued a somewhat ambivalent policy toward the Germans. Given the parallels between these cases and China and the U.S.–China relationship, an examination of why these particular foreign policies were pursued is crucial to understanding what China's behavior in the world is likely to be in the years to come and the implications for U.S. policy and U.S.–Chinese relations.

The discussion that follows highlights how the particular institutional biases of czarist Russia and Wilhelmine Germany, not simply the fact that they were nondemocracies, affected how economic ties influenced their foreign policies. The cases are not perfectly analogous since China's institutional biases are substantially different than those of czarist Russia and Wilhelmine Germany. Nonetheless, this examination of the historical record illuminates how the direction of institutional biases influence the impact that economic ties have on foreign policies.

### **Czarist Russia and France**

In the late 19th century, the czarist government was strongly committed to modernizing its economy and needed to finance a large public debt. Russia was thus highly dependent on access to foreign capital.

Germany had been the main banker financing Russian industrialization efforts and government debts until November 1887. At that time though, German Chancellor Otto von Bismarck ordered the Reichsbank to stop accepting Russian bonds as collateral security for loans, and to inform its customers that Russian credit was not sound. The order led to a drop in Russian loan stock on the Berlin Börse (Michon 1929, 17–18; Gerschenkron 1943/1989, 44; Calleo 1978, 14–16; Keiger 1983, 11; Bovykin 1979, 24; Feis 1930, 213).

French money was therefore essential for the Russian government to meet its financial needs and industrialization goals, and French bankers were ready, willing, and able to fill the void left by the Germans. After Bismarck's declaration, the chief financial houses of Paris formed a syndicate by which to bring French capital into the Russian market and to assist the czarist government. In November 1888 the first contract between French banks and the Russian government was signed, and two more loans were arranged in 1889 by the Paris Rothschilds. Three more loans followed in 1890. The terms of the deals made the Russian government's external indebtedness more manageable. Moreover, since Russia's system of taxation was ineffective and its available domestic capital insufficient to pursue industrialization, borrowing made that goal possible. Meanwhile, the deals were highly attractive for French investors since they provided high-interest yields and were considered very secure. Thus, these arrangements benefited both French bankers and the Russian government, and France replaced Germany as Russia's main creditor by the late 1880s, a position France held up to World War I (Michon 1929, 17–18; Cameron 1961, 73–74, 254, 300; Keiger 1983, 11;

Feis 1930, 44–52, 210–215; Kennan 1984, 32–33, 75–76; Bovykin 1979, 25; Anan'ich and Bovykin 1991, 259; Trebilcock 1981, 179–80).

As discussed, some nondemocratic regimes will not be sensitive to the effects of international economic ties, while others will. Czarist Russia was in the latter category. Although Russian leaders were not pressured by economic interest groups, they were keenly sensitive to the crucial role that international economic ties played in financing government debt and in achieving industrialization goals. Moreover, French leaders understood Russia's needs and Russian leaders' appreciation of the value of international economic links.

Russia's financial dependence on France was so great and so apparent to French leaders that Russia came to close ranks with France on security matters. Russia perceived Germany as having threatening intentions by 1891, and thought an attack was quite possible. However, the Russians felt that France would probably fight on their side with or without an alliance, and so thought an entente-like understanding was warranted. The Russians also feared that if an alliance were not secret, Germany might declare war preemptively. This possibility was quite ominous for the Russians, who felt they needed a couple of years to build up their forces to thwart an attack. Hence, state strategists in Russia were not convinced that an active and public balancing effort with France was prudent in the short run, though preparing to balance with a secret treaty could help achieve security beyond the near term. From a strategic point of view, therefore, the Russians were not nearly as keen about an alliance as the French were (Michon 1929, 19–20, 52; Keiger 1983, 13; Langer 1929/1967, 181; Bovykin 1979, 26).

Russia nonetheless tilted toward and forged an alliance with France because of the breakdown of financial ties with Germany, leading to Russia's financial dependence on France. Referring to Bismarck's 1887 order that prevented Russia from borrowing in Germany, Russian Foreign Minister Nikolai Giers told the German ambassador at St. Petersburg in 1893, "Bismarck drove us into the arms of France, especially through his financial measures" (quoted in Feis 1930, 214). And Herbert Feis (1930, 217) writes in his examination of the historical record, "A keen awareness of financial need and financial dependence ... must have been among the influences which led the Czar to accept the understanding of August, 1891." Also noteworthy in this regard, Giers wrote in a letter to Paris in 1891: "The cordial agreement which has so happily arisen between France and Russia, represents in our time a

condition necessary not only in view of our common interests, but also for the establishment of a definite counter-weight to the influence of the League of the central powers, which will maintain the most beneficial balance of forces” (quoted in Bovykin 1979, 26; also Kennan 1984, 57, though the translation differs slightly). Giers apparently did not see the agreement of 1891 as first and foremost or exclusively a response to a security threat to the balance of power. Rather, he was alluding to a mutual economic stake as the basis for the relationship.

That the financial links mattered can also be seen in the ways that France successfully used the incentive of financial aid to reach agreement on an alliance. The Russians had security concerns, but they were not as desirous of an alliance as were the French. As Feis (1930, 214) writes, “It was no easy task for these two countries to find and define a jointly acceptable basis for alliance.” As a result, the French government conveyed to the Russians that French financial aid was virtually conditional upon an alliance. The French therefore used the incentive of financial ties to bind Russia militarily. French leaders saw Russia’s desire for money from France as so significant that it could affect Russian strategic policy. They were right (Feis 1930, 214–215, 217 n. 18).

Despite some concerns about Russia’s resolve to fight on France’s side, French leaders saw in Russia a credible partner. It was recognized that Russia was highly dependent on French funding and would do nothing to jeopardize those ties (Michon 1929, 57–64). Indeed, the French government used the “dependence of Russia upon French finance ... to exercise a measure of control or influence over Russian policy, to restrain its actions in the Near East and sustain its opposition to Germany” (Feis 1930, 223). Clearly the French saw that financial ties had a positive influence on Russian policy.

### **Wilhelmine Germany and Britain**

In the period leading up to 1914, Germany pursued highly conflictual policies despite having extensive ties in the international economy. This was because its pseudodemocratic political institutions gave prominence to aggressive socioeconomic, political, and military forces, some of which perceived economic interdependence as entailing pernicious effects, while internationalist economic interests with preferences for a more pacific foreign policy were marginalized in the political process.

Before 1914, Germany was part of a highly integrated great power economy in which national wholesale price levels among the major powers were closely associated, indicating quick economic response in one nation to price changes in any other. Moreover, Germany was becoming increasingly dependent on trade, which was a sizeable and growing proportion (about 38 percent) of its GNP in the years before World War I (Katzenstein 1975, 1024; Rosecrance, Alexandroff, Koehler, Kroll, Lacqueur, and Stocker 1977; Waltz 1979, 212).

Germany had significant bilateral links with the European great powers as well. One-fifth of Germany’s enormous demand for raw materials and foodstuffs was filled by the British empire and financed by London; Lloyds insured much of the German merchant marine. Germany also had considerable economic links with France, while Russo-German trade also rose dramatically. However, beginning in late 1910, and particularly after the Agadir crisis in 1911, Germany’s economic ties with France and Russia worsened, becoming quite fragile by 1914, in large part as a consequence of Germany’s aggressive behavior in the international system (Mitchell 1975, 526, 573 and 1975/1978, 304, 307, 411, 416; Kennedy 1980, 294–295 and 1983, 93–95; Fischer 1975, 323–326; Lieven 1983, 134; Milward and Saul 1977, 394).

Why did Germany pursue such conflictual and aggressive behavior, given its dependence on the international economy? The answer lies in the underlying role of Germany’s political institutions.

From the 1870s to 1914 Germany was governed by “an autocratic monarchy with a few parliamentary trimmings” (Berghahn 1973, 9–11). Although there was a bicameral legislature, including a lower house (the *Reichstag*) elected by universal male suffrage, and upper house (the *Bundesrat*) structured to represent propertied and capitalist interests, that body had no power to unseat government ministers, who were selected by the kaiser. Further, the kaiser had great authority over foreign affairs, including the right to wage war, and supreme command of the armed forces. Moreover, the “Government interfered notoriously in local campaigns, the undemocratic *Bundesrat* had an unlimited power of dissolution, and the electoral districts were increasingly malapportioned against the urban interest” (Rogowski 1982, 9).

Nonetheless, the parliament was not powerless. Although legislation required approval by both kaiser and chancellor for enactment, passage of new bills did require majority votes in both lower and upper houses. Since tariffs, direct taxes, and the budget were



subject to such legislative approval, the executive branch could not simply exercise free will in foreign economic and military procurement policies. Still, legislative power favored the Bundesrat, which had the power to initiate bills, and to block bills or amendments initiated by the Reichstag. Under the 1871 constitution, the Prussian state government, dominated by the landed aristocracy (the Junkers), held primacy in that body; hence, the Reich government often had to reach agreements consonant with agrarian concerns. (Gerschenkron 1943/1989, 25; Berghahn 1973, 10–11).

The Junkers, kaiser, and chancellor could not simply rule without constraint; they had to form coalitions with other groups to pursue their goals. But they also had effective veto power, so coalitions that did not include their interests could not be realized or were doomed to failure. This political system gave rise to a coalition of iron, rye, military, and kaiser—expansionists who saw economic ties as entailing pernicious effects that could be mitigated only by transforming the nature of economic links with aggressive policies. This congruence of protectionist and military interests agreed on an armed mercantilism, while more pacific median economic interests were politically marginalized. As a result, conflictual policies intended in part to alter the nature of economic links and reduce German vulnerability in the international economy were adopted. As a result, interests opposed to democratization and free trade and in favor of aggressive, expansionist policies were prominent, while internationalist economic concerns were largely shut out of the political system.<sup>6</sup>

This was manifest in Wilhelm II and Chancellor Bernhard von Bülow's expansionist policy (*Weltpolitik*) that sought to enhance Germany's international role by gaining access to overseas markets and raw materials in order to achieve economic self-sufficiency and accelerate industrialization. They believed that Germany would have to reduce its economic vulnerability and

promote its growth by transforming economic relationships on the Continent through a German-dominated central European customs union. In these ways, Germany could gain a measure of control over its economic destiny, and augment its political power relative to other (especially Continental) great powers. These goals, and the coalition forged by Wilhelm II, von Bülow, and von Bülow's 1909 replacement, Theobald von Bethmann Hollweg, led to continued or increased tariffs over the next several years and to a dramatic growth in defense expenditures as of the 1890s (Gerschenkron 1943/1989, 58–61; Taylor 1946/1979, ch. 8–9; Fischer 1975, 11–12, 22–25, 33–35, 48–50, 137–138, 234, 237, 363; Geiss 1976, ch. 8–9; Kehr 1977, ch. 2, 55; Calleo 1978, 20, ch. 3–4; Kennedy 1980, ch. 13).

The importance of political structure in determining such an outcome becomes clear when one recognizes that many sectors in Germany disapproved of the tenor of German policy. In particular, the banks, export industry, and finished goods industry profited from, and lobbied for, strong economic links to and better relations with other powers. Bankers saw Germany as unprepared for war financially, and so advocated peaceful approaches to altering the nature of Germany's economic ties. In particular, they favored good relations with Britain (Fischer 1975, 22–25, 121, 134, 140, 199, 203, 231–236, 260; Kennedy 1980, 298–302).

In contrast, the Prussian Junker agrarians and Rheinland heavy industrialists were generally in favor of higher tariffs and more aggressive policies. They felt that maintaining German economic autonomy required Germany to alter the nature of economic ties by having a measure of political control, and this might entail war. Unlike the bankers, who expressed pessimism about financial difficulties, these groups were confident of Germany's ability to pay for war and felt that a compromise policy with Britain was merely wishful thinking (Fischer 1975, 135, 140, 235, 265).

As the agrarians and heavy industry won out politically, military expenditures jumped dramatically, increasing from about 1.3 billion marks in 1911 to 2 billion marks in 1913. Much of the increase funded the Prussian-dominated army expansion as the Junkers successfully sought to bolster their positions in the German political system (Lamborn 1991, 119–120).

All in all, Germany pursued an aggressive and conflictual foreign policy despite its economic dependence on other great powers because of its pseudodemocratic institutional structure. Germany's political system gave the kaiser, chancellor, and

<sup>6</sup> Snyder (1991, 18) makes a coalitional argument similar to this argument, which is also found in Papayoanou (1996, 1998, ch. 2). He contends that logrolling is a function of the "distribution of power and interests in the society and on the character of its political institutions." He too applies this argument to Wilhelmine Germany. However, there is a crucially important difference between the two arguments. Papayoanou points to these pseudodemocratic features as crucial, whereas he characterizes the political institutions as cartelized. For Snyder, cartelization is what is important because it gives prominence to concentrated interests which tend to logroll to pursue expansion and militarism. Papayoanou disagrees with this argument because concentrated interests do not necessarily have expansionist aims (and many in Wilhelmine Germany did not), so a cartelized system will not necessarily give rise to such a foreign policy. What is important is what *types* of concentrated interests have prominence under a particular set of political institutions, not whether there is cartelization.

Junkers so much power that winning coalitions tended to form around their interests, while economic interests advocating closer international economic ties and a more pacific foreign policy had little say in German politics. The most politically prominent forces in Germany saw Germany's economic dependence as a source of vulnerability, and expansionist policies as crucial to reducing that pernicious effect.

### **Britain and Balancing**

Meanwhile, British strategists wanted to oppose firmly the threat they perceived from Germany. However, economic ties generated powerful domestic political constraints that limited the strategists' capacity to balance firmly against Germany and impelled them to pursue some conciliatory policies.

Britain's ambivalent straddle policy in the period leading up to August 1914 included *entente* balancing with France and Russia and a response to the German naval challenge. However, the *ententes* were merely agreements to consult in a crisis; no commitments to come to the aid of France or Russia were made. And while the naval buildup helped insure Britain's survival, it added little to the security of the Continent. Moreover, Britain failed to build up its army's resources or to undertake conscription, and was unwilling to commit to sending the expeditionary force to the Continent. Britain also pursued something of a *détente* with the Germans, negotiating over naval, political, economic, and colonial matters after 1911. And in the crisis of July 1914, Britain pursued mediation and issued only a private, informal warning to Germany. British policy was, in short, a mix of balancing and conciliation.

British policy was the result of the fact that pressure groups, Cabinet ministers, and members of Parliament whose interests were shaped in large part by economic interdependence were significant constraints on the strategists. Divisions in the Cabinet were largely between the strategists and others in the Cabinet, particularly those sensitive to international economic concerns, and those divisions constrained British strategists and even impelled them to pursue conciliatory policies. British policy was also influenced in important ways by direct pressure from economic interests in the policymaking process. In addition, Cabinet and parliamentary political leaders had serious concerns about the costs to the British economy of a war, which would severely disrupt international economic relations. For such

reasons, British leaders pursued the ambivalent straddle policy.<sup>7</sup>

The Germans' decision to risk launching the Schlieffen Plan was influenced strongly by their recognition of the power internationalist economic interests had in Britain. The mixed signals they saw coming from Britain's straddle policy also reinforced their beliefs about the significance of the constraints faced by British leaders. German leaders thus had somewhat optimistic expectations that Britain might stand on the sidelines long enough for a rapid military offensive to work (Papayoanou 1996, 71–74; 1998, ch. 4).

The czarist Russia and Wilhelmine German cases show how nondemocracies can have different institutional biases that affect how economic ties are translated in the policy process and influence foreign policy. The leadership's goals and the power of particularistic economic constituencies are crucial to determining whether nondemocracies opt for a pacific and cooperative foreign policy or an aggressive and conflictual one. Economic ties may also generate constraints on democratic strategists hoping to balance against a nondemocracy with which there are extensive links, as exemplified by the British case.

We now consider what these historical lessons and the theoretical argument tell us about the likely direction of Chinese foreign policy and U.S.–Chinese relations. This first requires an analysis of the nature of the Chinese political economy.

## **THE POLITICAL ECONOMY OF CHINA**

In 1977, on the eve of reforms that would spark two decades of extremely rapid growth and development, China was largely isolated from the world economy. Its total trade in that year was less than \$15 billion, or 0.6 percent of total world trade. By the 1990s, however, China had become a major participant in the world economy—in 1993, its total trade approached \$200 billion, or 2.5 percent of world trade. China's economy has achieved growth rates averaging nine percent for nearly twenty years, leading to improved living standards and making China an attractive site for investment from abroad (Lardy 1994, 1–2). Yet few political reforms have accompanied these impressive economic advances as the Chinese Communist Party continues to control the political system without legal opposition.

<sup>7</sup> On the British case, see Papayoanou 1996, 55–66; 1998, ch. 4 and the cites therein.

The nature of the Chinese political system has led many in the United States—typically those concerned with China’s poor record on human rights—to call for an end to the U.S. policy of engagement. The analysis to this point suggests, however, that the continuation or termination of the policy will have significant implications for Chinese foreign policy and U.S.–Chinese security relations. The dynamics of the Chinese political economy must be analyzed to evaluate adequately the engagement policy’s implications for U.S. national security interests. If the gains China reaps from deeper integration into the world economy are only a source of power, and not of constraint on future behavior, then the engagement policy may come back to haunt U.S. policymakers. But if deeper integration empowers vested interests with a strong stake in that integration and supports the leadership’s economic goals, then Chinese decisionmakers will be less inclined to pursue conflictual and expansionist political-military policies. An evaluation of the engagement policy requires an examination of the relative political clout of those who gain and lose in China from deepening exposure to the international economy.

In the discussion that follows we first consider the extent to which Chinese economic development has depended on integration into the world economy. We then examine the nature of the Chinese political system, focusing on identifying the officials to whom top Chinese leaders are accountable, the “selectorate.” Next we discuss how various blocs within the selectorate are positively or adversely affected by integration into the world economy, showing that there are considerable vested interests in internationalization throughout the Chinese selectorate. On balance, those interests probably outweigh domestic-oriented economic concerns. We also show that the highest leaders in China, including President Jiang Zemin and Premier Zhu Rongji, have made a strong commitment to continued economic reform, and this entails a cultivation of international economic links. For these reasons, we conclude that as long as China’s engagement in the world economy continues, Chinese leaders are unlikely to pursue a foreign policy that is so aggressive and conflictual as to jeopardize China’s economic links and reform efforts.

## The Importance of China’s International Economic Ties

Deeper integration into the world economy, measured in both trade and foreign investment, has been a key

ingredient in China’s recent economic growth. In 1980, China’s total trade amounted to only \$38.1 billion, about 15 percent of Chinese gross domestic product (GDP) at official exchange rates (Lardy 1994, 15, 30). By 1996, the value of China’s foreign trade had grown to \$290.1 billion, over 41 percent of GDP (International Monetary Fund 1997).<sup>8</sup>

Foreign direct investment (FDI) in China has also grown rapidly, particularly since the late 1980s. Before 1984, annual FDI in China amounted to less than \$1 billion per year, or less than one percent of GDP. By 1996, new FDI in China totaled nearly \$42 billion, or 6 percent of GDP, and total accumulated FDI in China approached \$177 billion by the end of that year. Moreover, foreign-invested firms have been behind much of the expansion in China’s exports. Although they produced just one percent of China’s total exports in 1985, foreign-invested firms produced over 41 percent of China’s total exports by 1996. Relative to other countries at a similar stage of development, the importance of foreign investment to China’s economy is large. For example, by 1972 total accumulated FDI in Japan amounted to less than \$3.4 billion, while accumulated FDI totaled only \$2.3 billion as of 1981 in South Korea. Furthermore, foreign-invested firms never produced more than 11 percent of total exports in Japan, Taiwan, or South Korea. Foreign investment, like trade, has clearly played a large role in China’s economic development (Lardy 1994, 63–4, 71–2, 111–12; *China Monthly Statistics*, June 1997).

Integration into the world economy has, without question, been of increasing importance to China’s economy and is crucial to China’s development prospects. But how important the economic ties are perceived to be in China and what role they will play in influencing Chinese foreign policy depends in part on the extent to which Chinese leaders are accountable to the actors who have gained from international economic ties. If leaders are autonomous from these forces and not strongly committed to a reform policy that depends on integration with the world economy, then they will not be constrained from pursuing foreign policies that might endanger China’s ties to the world economy. Indeed, the gains reaped from integration into the world economy

<sup>8</sup> It should be noted that these figures somewhat overstate China’s dependence on foreign trade, since approximately one-half of the country’s trade consists of imports processed into exports—such trade has a relatively limited effect on the domestic economy (World Bank 1997, 85). Nonetheless, the rapid expansion of China’s foreign trade is remarkable, and has certainly contributed substantially to the country’s recent economic growth.

might ultimately help finance an aggressively expansionist foreign policy in the future.

## To Whom are Top Chinese Policymakers Accountable?

Despite two decades of reforms that have transformed China into a largely market economy, the country maintains communist political institutions. The institutional framework clearly stipulates government subservience to the Chinese Communist Party, most notably through a *nomenklatura* system which ensures that “[a]ll positions of real importance in China fall under” party control (Lieberthal 1995, 209). The top leadership position within the Party is the General Secretary, while the Standing Committee of the Politburo and the Politburo represent the Party’s top collective organs (Shirk 1993, 70).

To determine what accountability, if any, the officials who sit in these high-ranking offices have, it is important to consider what actors select them. To whom do high level officials owe their positions? Though the Chinese Communist Party (CCP) constitution gives the Central Committee formal power to choose top party leaders, it is clear that selection authority also manifests itself in informal ways. Specifically, informal power has rested with retired party elders, the military (which exercises more authority than its 42 seats in the Central Committee suggest), and the country’s preeminent leader (Shirk 1993, ch. 4).

During the 1980s and early 1990s, retired, high-ranking party elders held substantial clout within China’s selectorate. Though officially retired, these elders continued to sit atop wide factional networks, and held a large degree of influence over appointment and dismissal decisions (Dittmer 1990). As members of the founding generation of the PRC have continued to pass away in recent years, however, the power of the elders has declined. And in the years to come, the personal clout of newly retiring party leaders will certainly be smaller than that of the revolutionary elders. They will lack the prestige of having played a key role in the revolution. Moreover, unlike the revolutionary leaders who were able to create vast personal connections by serving in numerous bureaucracies and commissions, leaders in later generations have tended to advance within a single organization and thus have been unable to develop networks that are as extensive. The importance of personal authority is therefore shrinking (Shirk 1993, 73–74; Zhao 1995).

The military, in addition to holding formal authority through its Central Committee seats, has

also been an important group with informal authority in China’s selectorate. On occasion, the People’s Liberation Army (PLA) has been very active in Chinese politics. However, the military has become involved politically only upon the initiative of high-ranking political leaders. Nonetheless, since leaders have at times used the PLA against their political opponents, having at least tacit military support has been crucial to any leadership contender. (Jiang Zemin has therefore been careful to prove himself a friend of the PLA.) As with the elders though, the informal influence of the military in the selectorate appears to be declining to some extent. The new generation of military leaders, like their political counterparts, simply lack the clout of the revolutionary generation. In addition, newer political leaders have more limited connections in the military, which makes it more difficult for them to involve the PLA in politics. Still, the PLA continues to play a prominent role in China’s leadership selection process, a role that could intensify should Chinese politics become unstable (Joffe 1996, 307–8; Shirk 1993, 76; Baum 1998, 155).

The preeminent leader also has informal leadership selection authority. Both Mao Zedong and Deng Xiaoping held considerably more sway over selection decisions than their formal positions might indicate. They certainly were able to veto any candidate to a top leadership position not acceptable to them. Jiang Zemin, meanwhile, seems unlikely to be able to amass the personal authority exercised by Deng in part because he has more limited personal connections (though he still wields considerable power) (Shirk 1993, 77; Baum 1998, 149).

While informal lines of authority within the Chinese selectorate have been the most prominent source of leadership selection, the role of formal authority within the selectorate has been increasingly significant. Citing the tendency of elites to cater to constituencies within the Central Committee during the post-Mao era, evidence that the Central Committee acts as “the final veto gate in policy-making,” and formal Communist Party rules, Susan Shirk argues that “it appears that the Central Committee is in the process of becoming the key group in the selectorate in China.” The relationship between the Central Committee and the Politburo and its Standing Committee is one of “reciprocal accountability.” While it is true that top Party leaders appoint the Party, government, and military officials who sit on the Central Committee, members of the Central Committee then have the authority (in conjunction with other members of the selectorate) to choose top Party leaders (Shirk 1993, 72, 79–81).

In summary, a diverse range of actors possess at least some leadership selection authority in China; top party leaders and leadership contenders pursue policies that garner support among these actors—especially during times of leadership succession competition. While we have suggested that the role of informal selection authority appears to be declining, serious disagreements exist among scholars regarding the continued relative importance of formal versus informal authority within the selectorate. Scholars in particular disagree over the extent to which the Central Committee wields real selection power.<sup>9</sup> Such disagreements should be kept in mind as we consider the international economic interests of different elements of the selectorate in the next section. To the extent that constituencies which lose (gain) from international economic ties have more (less) power than we have suggested here, our conclusions should be tempered.

### **Who in the Selectorate Gains and Loses from Integration into the World Economy?**

Influential groups within the Chinese selectorate that have developed interests in continued integration into the world economy include many local officials, and to a lesser extent, the military and some central officials. The path of economic reforms in China has also given some groups that once opposed deeper integration—such as interior provincial officials—less reason to oppose opening to the world economy, while undercutting the influence of other opponents of integration, such as large state-owned enterprises (SOEs).

The group with perhaps the deepest interest in continued integration into the world economy is local party and government officials. These officials comprise a sizeable bloc within the Central Committee—32 percent of the members of the 15th Central Committee (elected in September 1997) are local officials (Institute of Asian Affairs). These officials have both indirect and direct interests in China's international economic ties.

Indirectly, fiscal decentralization—a key component of China's economic reform strategy—has given local leaders a large stake in economic growth. Growth enables such officials to expand their tax base and patronage opportunities (Shirk 1993, 1996). Because deepening integration into the world economy has been an important source

of economic growth in China, fiscal decentralization has given local officials a strong, indirect stake in China's foreign economic relations.

Since local regions have been given increasing autonomy to attract foreign investment over the course of the reform period, local officials are also realizing a more direct interest in China's ties to the international economy. In the late 1970s, Chinese leaders created four Special Economic Zones (SEZs) located in the Guangdong and Fujian provinces. The SEZs were encouraged to attract foreign direct investment, and were allowed to retain a generous portion of their foreign exchange earnings. The SEZs were highly successful, and thus gave officials from those provinces a vested interest in access to the world economy. Officials from other regions, seeing the benefits afforded by the SEZs, began to lobby for similar access. Central officials in 1984 awarded similar deals to fourteen coastal cities and Hainan Island, and even officials from inland provinces were by the mid-1980s lobbying for the autonomy to attract foreign investment.

The number of regions awarded special status continued to expand into the early 1990s. During the early 1990s, moreover, nearly 2,000 Special Development Zones were established throughout China. These zones, which were more localized than the SEZs, were allowed to offer attractive terms to foreign investors. Budgetary difficulties at the local level have made local officials especially anxious to use their increased autonomy to seek expanded inflows of foreign investment. In particular, such officials have sought since the early 1990s to convert unprofitable, locally controlled SOEs into foreign joint ventures to improve performance and relieve pressures on local budgets (Shirk 1994, 35, 38–39, 41; Yang 1991, 56–58; Gu 1997/1998, 46–47, 51, 55–56).

Local officials with the deepest interest in continued access to foreign investment represent coastal provinces, for most foreign investment flows into coastal regions. In 1996, 88 percent of FDI in China went to the nine coastal provinces and three municipalities (*China Monthly Statistics*).<sup>10</sup> But officials representing inland provinces also have a stake in continued access to foreign investments. A not insignificant amount of FDI flows into inland provinces, and these provinces have received considerable trickle-down benefits from foreign investments along the coast. Many enterprises and government organizations from inland areas have, for

<sup>9</sup> Contrast especially Shirk 1993 with Yang 1996 and Teiwes 1995.

<sup>10</sup> The nine provinces and three municipalities are: Beijing, Fujian, Guangdong, Guangxi, Hebei, Hainan, Jiangsu, Liaoning, Shandong, Shanghai, Tianjin, Zhejiang.

example, set up businesses in the SEZs along the coast (Shirk 1994, 42). Thus, many local officials across China, but certainly not all, share an interest in continued access to the world economy.

Other key groups within the selectorate have also developed an interest in China's deepening integration into the world economy. The PLA, for example, has become increasingly involved in economic pursuits. Due to cuts in the military budget in the early to mid-1980s, which prompted Chinese leaders' efforts to find alternative sources of military funding, the PLA essentially went into business. Notes Solomon Karmel (1997, 103), "With China's domestic consumer market and export trade growing, the military concluded that civilian products were its best hope for profits in an environment of decreasing support, and it began to produce more of these goods than ever before." Since 1987, the military's civilian production has been of greater value than military production, even by official statistics. Moreover, by 1994 China's military-run organizations had established over 300 joint ventures with foreign partners (Karmel 1997, 103–04, 109). As Ellis Joffe (1996, 311) puts it, the PLA's business activities constitute an "empire that embraces every major economic activity." Thus, the PLA has, like many local officials, developed a stake in integration into the world economy. As Karmel (1997, 113) argues, "war, or any dramatic upsets to stability in East Asia, would be bad for business."

However, the point should not be overstated. The military's business dealings do not make the PLA's foreign policy outlook unambiguously pacific. For example, the military is in the business of building arms and has been involved in arms smuggling. Moreover, the leadership has recently undertaken initiatives to reduce the military's private business endeavors. In particular, efforts have been made to move production to civilian control. To the extent the leadership succeeds, the military's stake in integrationist policies will decline (Agence France Presse 1998, A6; Faison 1998, A1, A6.)

Important groups within the Chinese selectorate appear to have developed a significant stake in access to the world economy. However, many influential actors in China undoubtedly had strong interests in maintaining their insulation from world markets before the 1980s, and for some of them, isolation remains their preferred policy.

The major source of opposition to economic reform and to integration into the world economy early in the reform process came from inland provinces, heavy industry, and central planning agencies and industrial ministries. Inland provincial

leaders were concerned that opening China to the world economy would widen income gaps between coastal and interior regions, since inland areas would benefit little from integration. Heavy industries were relatively uncompetitive on world markets, and so opposed the prospect of more stringent competition. The heavy industrial ministries that stood atop these industries naturally opposed China's increasing exposure to the international economy as well. Meanwhile, central officials, especially those in planning agencies, tended to oppose the overall reform program because it undercut their power (Shirk 1984).

Do these constituencies in the selectorate continue to oppose integration into the world economy? If so, how powerful are they politically?

Interior provinces initially opposed many reform programs, particularly those which opened China's economy by giving preferential treatment to coastal areas. While coastal provinces benefited considerably from the SEZs and attracted the lion's share of foreign capital, interior provinces received few gains from integration into the world economy. Interior officials were thus concerned with growing regional income disparities. The problem was exacerbated by fiscal decentralization, which "undemined the ability of the central government to transfer resources from richer areas to poorer ones or across regions" (Yang 1991, 47–52).

Interior provincial officials constitute a significant part of the selectorate, holding 37 out of 193 seats in the Central Committee (Institute of Asian Affairs 1997). However, in the 1990s interior provinces have fewer reasons to oppose integration than they did at the start of reforms. They have been given more autonomy to attract foreign capital via Special Development Zones, and have received considerable trickle-down benefits from development along the coast. Hence, interior provinces began in the 1980s and early 1990s to try to "jump on the reform bandwagon" and lobby for access to the world economy themselves (Yang 1991, 55). Still, given their geographical disadvantages in attracting foreign capital, the support of interior provinces for the open policy is more lukewarm than it is for coastal areas.

Local officials across China, including those who generally support and gain from China's internationalization, at times may have interests that conflict with deepening integration into the world economy. These officials are concerned, for example, with local unemployment rates, which can be directly affected by further integration into world markets. Though protection remains high, China has begun to lift some of its barriers to imports—the average

weighted tariff dropped from 28.1 percent to 19.8 percent in 1996—and has pledged to lower tariffs even further if and when it is granted entry into the WTO (World Bank 1997, 85–88). Yet lowering tariffs will bring stiffer foreign competition that will force many industries to downsize or shut down. In turn, the unemployment rate will go up in some regions. Officials from those regions will, no doubt, weigh such disruptions carefully when considering their views toward deeper integration into the world economy.

A second constituency that continues to oppose an open policy is heavy industry, for China is relatively labor abundant and capital scarce. Its most competitive industries on world markets are thus labor-intensive light industries.

Yet heavy industry continues to constitute a large percentage of total industrial output: 55.6 percent of gross industrial output (at current prices) for the first 5 months of 1997, an even higher percentage than in 1985 (52.9 percent) (*China Monthly Statistics* June 1997; World Bank 1997). SOEs continue to produce a large portion of this heavy industrial output. In 1994, SOEs were responsible for 71 percent of total output in resource extraction and 65 percent of total output in utilities. In three scale-intensive industrial groups, metallurgy, chemicals, and transport machinery, SOEs produced 59 percent, 49 percent, and 51 percent of total output, respectively. SOEs produced 40 percent of total industrial output in 1994, and in 1996 employed 17 percent of the labor force (Naughton forthcoming; World Bank 1997, 29).

Heavy industry thus continues to produce a substantial portion of China's total output, and (especially large) SOEs are responsible for a large percentage of that heavy industrial output. Furthermore, since nearly all industrial ministries represent heavy industry in China, and since high ranking ministerial officials sit on the Central Committee, heavy industry has greater direct influence within the government and the selectorate than does light industry (Shirk 1993, 107–110). Since representatives of heavy industry and the SOEs are more likely to oppose integration into the world economy than are the representatives of other sectors, they remain important opponents of open policies. It is, of course, an oversimplification to say that all heavy industry interests oppose China's ties to the world economy, sectors such as resource extraction or utilities would undoubtedly gain from increased foreign investment, but resistance to integration into the world economy is generally likely from heavy industrial sectors. This resistance is significant, for

China's central government institutions give considerable representation to such interests.

Finally, various central government officials have at times opposed economic reforms in general, and integration into the world economy in particular. Fiscal decentralization and movement out of the planned economy have reduced the authority of many central government organs, particularly the State Planning Commission and the Ministry of Finance. The declining profitability of the SOEs (in response to increased international competition) has also undermined a major revenue source for the central government. Indeed, from 1978 to 1995, budgetary revenues dropped from 35 percent of GDP to 11 percent; 62 percent of the decline was the result of decreased revenues from industrial SOEs (World Bank 1997, 24).<sup>11</sup> To the extent that integration into the world economy damages the competitiveness of SOEs, some central officials are likely to be more opposed to open policies.

Recent events in China, however, suggest that concerns over budgetary revenues from SOEs are of less importance than in the past. China has recently embarked on a major fiscal rationalization program that entails a new tax system adopted in 1994. This tax system relies less on state industrial enterprises as revenue sources, spreading the tax burden more equally on all sectors and ownership forms. The system is also designed to lead to a gradual increase in central revenues (Naughton 1996, 293–294). Central officials, in short, are decreasingly dependent on the profits of SOEs for budget revenue. As such, they have less reason to abandon integration into the world economy out of fear of SOE profitability. Moreover, as we note below, central leaders have recently embarked on an SOE restructuring drive; if the drive succeeds, the SOEs' status as cash cows for the central government will cease entirely.

In sum, large constituencies within China's selectorate have a strong interest in China's continued integration into the world economy. Such groups would generally oppose policies that might put continued access to the world economy at risk. Still, some constituencies within China's selectorate are either opposed to, or ambivalent about, continued

<sup>11</sup> Events during the post-Tiananmen conservative resurgence in China appear to underscore the concerns that financial and planning officials have had over China's reform program, and their identification with conservative efforts to roll back the reforms. Proposed policies at the time included strengthened planning, fiscal recentralization, and preferential policies for SOEs; planning and financial officials would, of course, have been among the major benefactors of such a program. Ultimately the program was defeated because of economic shortcomings, but also due to staunch opposition from provincial level officials (Naughton 1996, 277–283).

integration. While the path of reforms in China has reduced the opposition to integration of some of these constituencies (such as interior provinces), and undercut the influence of others (such as SOEs), some interests in China (especially heavy industry) will continue to be hostile to increasing China's openness to the international economy. On balance though, it appears that substantial support from the selectorate exists for pursuing further internationalization.

### **The Central Leadership, Economic Reform, and Internationalization**

The central leadership in China has made a clear commitment to continued economic reform and development. Such reform efforts would be significantly damaged should China pursue policies that undercut its international economic relationships, since China is increasingly integrated into world markets. Top leaders thus have a strong stake in China's continued integration into the world economy. Recent statements and initiatives by President Jiang Zemin and Premier Zhu Rongji underscore their commitment to reform.

For example, in the fall of 1997, Jiang endorsed an effort to sell most of China's large SOEs, a plan that would effectively end the state's position as the primary owner of industry (Faison 1997). The plan certainly involves risks, including rising unemployment and opposition from conservatives. Jiang's backing of the plan indicates that economic reform is among his highest priorities.

Zhu Rongji has been even more explicit about his commitment to SOE restructuring. In a recent report, he stated, "If we cannot achieve this goal [of solving SOE problems by the year 2000], it will prove that I am not worthy of leadership. Since I have been entrusted by the Party and the people for this task, I would have to admit my inability and resign. I would resign from the leadership group" (quoted in *Inside China Mainland* 1998, 47). He further emphasized his commitment to continued economic reform in a March 1998 news conference in which he asserted: "No matter what is waiting in front of me—whether it be land mines or an abyss—I will blaze my trail" (quoted in Eckholm 1998, A1). In short, key elements of the Chinese leadership clearly place economic development and reform among their top priorities. As such, they are unlikely to favor policies that might put China's foreign economic ties, and thus its economy, at risk.

## **ECONOMIC TIES, THE DIRECTION OF CHINA'S FOREIGN POLICY, AND THE POLICY OF ENGAGEMENT**

Key components of the Chinese selectorate have a strong stake in continued and robust foreign economic ties. To the extent that top leaders are accountable to officials in the selectorate, therefore, they are unlikely to pursue policies that put China's foreign economic ties at risk. At the same time, regardless of their accountability to the selectorate, several top leaders have made strong commitments to economic reform in China, and their plans require integration to succeed. Thus, even if its autonomy from the selectorate is relatively high, the leadership is unlikely to pursue policies that undermine foreign economic ties given its own priorities.

This analysis, the analytical argument elucidated, and the historical cases discussed give us good reason to expect that top Chinese policymakers will not pursue an aggressive and conflictual foreign policy that could put China's international economic ties at risk. Doing so would undermine their support within the selectorate (and thus damage their political prospects) as well as their apparent commitment to economic development and reform.

Some qualifications are in order though. While top Chinese decisionmakers are unlikely to pursue aggressively expansionist policies, they still maintain the ability to act autonomously in specific circumstances on the world stage. Indeed, foreign policymaking remains highly centralized in China (Zhao 1995, 240; Shambaugh 1996, 197–201). Hence, if top leaders perceive vital security interests to be at stake, there is little doubt they will act even in ways that could risk damaging foreign economic ties.

One scenario likely to provoke a large-scale military response by China that might jeopardize its economic ties would be movement by Taiwan toward legal independence. Economic concerns would likely take a back seat to the more serious problems a declaration of independence by the island would raise for Beijing. Yet as Thomas Christensen (1996, 50) notes, a military response by China to Taiwanese steps toward independence would not be an indication of an expansionist foreign policy in Beijing. "If Taiwan declared independence and was then attacked by the mainland," he writes, "one could not draw conclusions about Beijing's expansionist designs any more than one could draw conclusions about



American expansionism from the northern states' reaction to the South's secession." Thus, while deepening integration into the world economy will be unlikely to prevent Beijing from responding militarily should leaders perceive China's core security interests to be at stake, such military actions would not necessarily indicate that Chinese leaders are unconstrained by economic ties.

A second qualification concerns general uncertainty about future political scenarios in Beijing. No guarantees exist that Chinese political institutions in 5, 10, or 25 years will resemble those of today. An economic crisis accompanied by social unrest, for example, might lead to greater PLA involvement in Chinese politics or even a coup (see, for example, Joffe 1996). Some scholars have even suggested that China stands on the verge of collapse (c.f., Goldstone 1995). Such scenarios would clearly change the political logic of China's foreign policy behavior.

However complex and uncertain the nature and future of Chinese politics, it would be unwise to conclude that the United States should end its engagement policy because Chinese politics *might* become destabilized and lead to a more aggressive and conflictual foreign policy. Such a rationale for ending engagement holds the danger of self-prophecy, for doing so could help cause the type of crisis that would lead to a coup or hard-liner resurgence, and in turn, an aggressive and noncooperative China. By contrast, continuing the engagement policy will further raise China's stakes in the world economy and likely broaden support for reform and further integration. This would make it less likely that China would pursue conflictual policies in the Asia-Pacific. It would also make it more likely that China would cooperate with the United States and adhere to international norms on various issues.

Because there are uncertainties about China's future it is important to address another concern about the engagement policy, whether U.S. leaders will have the capacity to balance against China should the need arise. As discussed, British strategists were unable to pursue firm balancing policies against Wilhelmine Germany before 1914 because internationalist economic concerns with strong ties to Germany were constraining influences. Will this be a problem for the United States?

At present, the U.S.–Chinese economic relationship is asymmetric. China is highly dependent on the United States (especially with regard to trade), but China is not a very significant partner for the United States. 1996 figures show that trade with the United States amounted to 22.9 percent of

total Chinese trade and 9.5 percent of Chinese GDP. At the same time, trade with China accounted for only 4.6 percent of total U.S. trade and 0.9 percent of U.S. GDP (International Monetary Fund 1997; Euromonitor International 1998). Hence, U.S. strategists are not likely to be highly constrained by economic interests with ties to China into the near future.

As economic ties grow, however, and the U.S. economy becomes more dependent on China, that may not be the case. Thus, over the next several years it is crucial that U.S. policymakers carefully monitor and analyze the dynamics of the Chinese political economy in the ways suggested by this paper. If the balance of power within China begins to shift toward inward-looking concerns, a reevaluation of the policy of engagement would be in order. This is a crucial time for policymakers to analyze and act on the situation in China, for economic statecraft is best pursued when ties are limited, as they are for the United States at present and into the near future. To ignore a reversal in the apparent trends in the Chinese political economy and continue with the policy of engagement could leave U.S. strategists constrained in the long term should the need to balance against China arise.

## CONCLUSION

This article assesses the U.S. policy of engagement with China by employing theory, historical examples, and an analysis of the Chinese political economy. We argue that extensive international economic ties are likely to constrain nondemocratic great powers from acting belligerently in the world arena when economic internationalists are prominent politically and/or when the leadership believes an expansion of international economic ties is crucial to its goals.

Because large segments of the Chinese selectorate benefit from integration into the world economy and key elements of the Chinese leadership have made a strong commitment to internationalist economic policies, we conclude that China is unlikely to pursue aggressive and highly conflictual foreign policies. Thus, by integrating China's economy more closely into world markets, a maintenance of the policy of engagement will make Chinese belligerence even less likely. In contrast, by pursuing a containment policy, the United States would undercut the strength of economic internationalists in China, thereby reducing the

prospects for a pacific and cooperative Chinese foreign policy in the years to come.<sup>12</sup>

Our analysis has significant implications for prominent arguments in the international relations literature. First, our theoretical argument and policy prescriptions are in sharp contrast with realist conceptions. Realists would argue that since China is a potential enemy, the United States is likely to, or should, be reluctant to pursue open economic policies that can empower the Chinese. Doing so carries significant risks in a world in which relative gains matter (Gowa 1994; Waltz 1979; Grieco 1988). Our analysis leads to a much different conclusion. It suggests that economic ties can improve the position of internationalist economic interests within China and thus give rise to a more pacific Chinese foreign policy. Empowering China, therefore, can yield positive security externalities.

Second, our argument suggests a refinement of the finding that regimes in transition from authoritarianism to democracy are war-prone (Mansfield and Snyder 1995a, 1995b). Edward Mansfield and Jack Snyder suggest that the reason such states are war-prone is that national leaders find it necessary to appeal to nationalist forces. However, if a democratizing country has extensive exposure to the international economy and constituents with a stake in economic integration wield considerable power in the political system, nationalist appeals will be unattractive for political leaders and ineffective. Under those conditions, leaders will find it more useful to appeal to internationalists, and so a peaceful transition is quite possible. Thus, if China begins a process of democratization, its integration into the world economy should mitigate the impact of nationalist forces with aggressive designs.



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<sup>12</sup> For an alternative conception and analysis focusing on domestic politics, see Shambaugh 1996.

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