

South China Sea: Changing Dynamics

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Actions taken by China in the South China Sea have alarmed many of the countries in the region. It is China's assertion of ownership of certain islands, islands also claimed by other Southeast Asian nations that contributed to the protest by The Philippines before the Permanent Court of Justice. In 2016, the Court's ruling was rendered. Actions and reactions by the affected parties to the ruling, as well as political events, make 2016 an interesting year. The election of a new president in The Philippines and in the United States adds to the fluid dynamics in the region.

INTRODUCTION

This Land Is My Land

The events set in motion by China in the South China Sea in the last decade or more, whether it involved trade or claims on territory, have alarmed many countries in the area. The trade treaties negotiated with ASEAN point to China trying to integrate the countries in Southeast Asia and the South China Sea through mutual trade and trade-related institutions, and, in this way, restore China's historic sphere of influence in the region. But due to China's historic dominance in the region, there is the fear in many countries of the possibility of "economic colonization" by China (Geib & Pfaff, 2016). In light of China's assertion in regard to ownership of certain islands in the East and South China Seas that fear seems to be justified and is seen as a maritime expansion by China. While the actions and reactions of those affected by China's assertiveness have provoked many of its neighbors to build up their armed defenses, the Philippines opted to bring the case before the International Court of Justice in The Hague (Geib & Pfaff, 2016). Xi Jinping's "Belt and Road" initiative is a major symbol of China's new efforts to expand its influence in Asia. "Belt and Road" is the initiative to revive the ancient silk-road trade route that linked China to Europe and South Asia a thousand years ago (interviews).

Changing Dynamics

Several events in 2016 affected the dynamics in the South China Sea. The case brought by the Philippines before the Court of Justice in The Hague came to a close and the court rendered its decision, condemning the island-building activities by China. But in the meantime a new president, Roberto Duterte, was elected in The Philippines, influencing the diplomatic discourse between the Philippines and China. Later in the year, the presidency changed in the United States with the election of Donald Trump

in November, 2016. These events turned the give and take in the South China Sea into a much more fluid situation.

To better understand the Chinese position in the South China Sea it helps to take a short excursion into the historic background. Historic and cultural aspects are also at the center of the actions and reactions by China's neighbors. Therefore, emphasis will be on the eventual reactions to the events of 2016 and the ongoing rivalries of some of the players in the South China Sea, concluding with a discussion of possible conflict resolution strategies.

METHODOLOGY

This paper employs a research methodology that focuses on political and economic growth in China from 1980 to 2017. The paper also provides a view point on the author's experience and information gathered from interviews with Chinese business professionals. A significant effort has also been made to examine traditional data and documents from a variety of sources when and where they were available. One author most recently did research in Shanghai in the summer of 2017 as well as teaching at Shanghai Finance University in 2013 and 2014. In the summer of 2017 one author spent time in Shanghai and Hong Kong researching our topic. The emphasis of the research was to find the latest trends in globalization strategies. It is important to note that many of the professionals and experts in China wish to have their comments kept confidential. Therefore, we choose to respect their request of confidentiality in all cases. We have referenced and documented dates where they are public.

The methodology for this study where it involves interviews can be described as a focus on the policy views of key stakeholders and influencers. In general, the interviews were conducted with professionals from such organizations as the Economist Group in Hong Kong, Shanghai, and London, the Old Bear Sterns Investment firm, Goldman Sachs, Chase Investment Bank, U.S. Chamber of Commerce, and Boston Consulting Group in at least two locations, Microsoft, and a host of other public and private professionals. The interview format did not include a formal survey but did include structured questions. A significant portion of this research is based on conversations with more than 350 key influencers in Shanghai, Beijing, Hong Kong, Singapore, and Washington, D.C. over a period of 26 years beginning in 1988 and most recently in the summer of 2017.

THE GEOPOLITICAL CONTEXT AND THE RISE OF CHINA

It is clear that China is seeking to re-establish and expand its sphere of influence particularly in Southeast Asia, the South China Sea, and the East China Sea. The core of the maritime disputes stems from China's increasing strong assertion that it should control over 90 percent of the South China Sea. The South China Sea disputes involve both island and maritime claims among several nations including Brunei, the People's Republic of China (PRC), the Republic of China (ROC), Malaysia, Indonesia, the Philippines, and Vietnam. It is important to note that \$5.3 trillion of total trade passes through the South China Sea every year (CFR.org, China's Maritime Disputes). China claims that Chinese seafarers discovered and named islands in the region centuries ago, and the country has ancestral fishing rights. These rights are said to exist within a U-shaped "nine-dash line." This line encircles almost all of the South China Sea. The map, on which the claims are based, dates back to 1947 and reflected a Chinese mapmaker's impression of China's historical claims, but did not reflect the geo-political reality of the mid-twentieth century (Beech, 2016). China has never really clarified what the line means. Does it refer to the bits of land, rocks, reefs, and shoals within the dashes or is it all the waters as implied by official Chinese proclamation about historic fishing grounds close to other nations' coast lines (Beech, 2016). As this research shows there are many factors involved with this new reality. These themes include China's self-perceived humiliation by western colonialism particularly since the opium wars in the 1840s, the protectionism and isolationism of the U.S., the sensitivity of Japan and revisions of the Japanese constitution, the decision of the International Court of Justice, the counter claims of southeast nations, and the counter claims of the U.S. Another relevant historical reality is the rapid economic rise of China since

Deng Xiaoping's market oriented reforms of 1978. Moreover, President Xi Jinping has adopted a policy of outward foreign direct investment particularly in regard to the major initiative re-building and expanding the Silk Road known as "One Belt, One Road." The "One Belt, One Road" initiative by China will invest over 25 trillion dollars from multiple sources to revive the ancient "silk road" trade route from China to Europe (interviews).

Some Important History

After Mao died in 1976, Deng Xiaoping emerged as the paramount leader of China with a new philosophy. Deng's new approach needs to be seen against the background of at least two important historic realities. These realities include two hundred years of Chinese humiliation under the thumb of western colonial powers and Mao's Cultural Revolution from 1966 to 1976.

In the view of the Chinese, China was humiliated for 150 years before the communists took power in 1949. During this period China's economic and political sovereignty was destroyed. The most egregious example of China's humiliation was the "Triangular Trade" practiced by England, punctuated by the opium wars beginning in 1849 and culminating with the period of "unequal treaties" imposed by the foreign powers (interviews).

The "Triangular Trade" imposed by the British simply meant exporting opium from India into China to raise foreign exchange for the purchase of such items as silk and tea for the European and American markets. The British particularly grew enormously rich by selling opium to the Chinese. The center of the trade in China was Canton, now Guangzhou. The central government of China sought for years to close down the opium trade. It finally closed Canton to foreign traders in 1839 (interviews).

The following opium wars were short. The British and Americans sent warships to re-open the Chinese ports to the opium trade. The Chinese government was too weak to prevent the re-opening of the ports. The result was the unequal treaties of the 1840s. The western powers established foreign concessions in China's major cities. The turnover of Hong Kong to the British was another outcome of the opium wars. Hong Kong remained a British colony until 1997. This is the backdrop for Deng's new pragmatism (as example of punctuated equilibrium) meant to re-establish China's historical power through economic development.

A second historical reality influencing Deng's pragmatic vision was Mao's Cultural Revolution from 1966-1976. One can mark the end of Mao's Cultural Revolution and Deng's new pragmatism on at least two levels. The first is the end of ideology. The second level is represented by the initiation of new economic reforms (interviews).

From Mao to Deng's Pragmatism

For years the Chinese Communist Party of Mao tried to substitute communist ideology and organization for traditional Chinese cultural values. The era of dogmatic ideological rigidity culminated in Mao's "Great Cultural Revolution" from 1966 to 1976. Mao unleashed the destructiveness of the Red Guards to make his last effort to create a communist man and woman. The ensuing political chaos caused dramatic economic decline. As a political moderate Mao had imprisoned Deng even though he had been a member of the original Chinese Communist Party. He re-emerged as China's paramount leader in 1976.

To stem the economic decline, Deng initiated sweeping economic reforms. Crucial to these reforms were special economic zones (SEZs). The initial SEZ framework can be characterized in the following way:

- Managed directly from Beijing
- Private ownership control
- Tax incentives and tax holidays based on Chinese established investment priorities
- Freedom to hire and fire business employees
- Partnerships with Chinese entities
- Extensive and updated infrastructure that supported international business activities

The original five special economic zones became a platform of success for China's experiment with market reforms and open trade and investment, and export manufacturing. In the 1980s Deng established ten more special economic zones. They also became rapidly successful further enlarging the platform of successful experimentation (interviews).

INCIDENTS AND INDICATIONS

In 2012 China dislodged the Philippine navy from Scarborough Shoal in the South China Sea. Scarborough Shoal is within the 200 mile exclusive economic zone (EEZ) from the Philippine mainland as established under the UN Convention on the Law of the Sea (UNCLOS). Chinese ships blocked Filipino fishermen from fishing near Scarborough Shoal (*The Economist*, 2016). Reacting to the Chinese blockade of the shoal Benigno Aquino, the president of the Philippines at the time, brought the case in 2013 before the Permanent Court of Arbitration, an international tribunal in The Hague (*The Economist*, 2016). It is important to note that building any kind of military installation on Scarborough shoal would give China an important gateway to the open Pacific (interviews).

What is worry-some is China's rapid island building in the South China Sea. China has engaged in a massive building spree for the past few years. In the Spratly archipelago it has turned seven uninhabited rocks and reefs, submerged at high tide, into artificial islands and has fortified them. The same rocks and reefs are also claimed by Vietnam and the Philippines. Both countries are outraged by China's actions. As mentioned above, China removed the Philippine navy from Scarborough Shoal, north of the Spratlys, and Chinese activities suggest that the Shoal will be the next area of reclamation. According to an interview with the commander of U.S. forces in the Pacific, Admiral Harry Harris, China appeared poised to start construction again but backed off when President Obama and other officials issued private warnings to Beijing. Moreover, Admiral Harris's Pacific command moved additional assets to the area (*WSJ*, 2016). Chinese construction on Scarborough would give Beijing a position 120 miles off the strategic Philippine port of Subic Bay and near the Luzon Strait, a key gateway to the open Pacific.

Under the U.N. Convention on the Law of the Sea, to which China is a signatory, only a naturally formed island that can support human or economic life can justify a claim of "exclusive economic zone" (EEZ), which can extend as much as 200 nautical miles. An EEZ is crucial: it grants a coastal nation sovereign rights to all natural resources within those waters, though other nations' ships are allowed to pass through (Beech, 2016). By turning reefs into islands, China may try to claim the 200 miles exclusive economic zone. If it will be allowed to do so, China could practically control the waters of the South China Sea.

China's hectic building, turning rocks and reefs into islands, has led to protests from several nations in the region, foremost by those which lay claim to the same reefs. Itu Aba, the biggest natural island in the Spratly archipelago, is occupied by a Taiwanese garrison. The island is actually claimed by China, Taiwan, The Philippines, and Vietnam (*The Economist*, 2016). But China has turned three of the rocks in the Spratly's into islands larger than Itu Aba. It has recently landed civilian aircraft carrying "tourists" on one of them. And China has again moved a large oil rig into the waters claimed by Vietnam – as it did in 2014 when it provoked fatal anti-Chinese riots.

Ruling by the Permanent Court of Arbitration

On July 12, 2016 the Hague Tribunal constituted under UNCLOS ruled against China in arbitration instituted by the Philippines (The Hague, 2016). The tribunal found that it has jurisdiction to consider the dispute. The tribunal concluded that the convention allocates rights to maritime areas and that protection for pre-existing rights, basis of China's position, were considered, but not adopted in the convention (Permanent Court of Arbitration). The tribunal concluded "that to the extent that China had historic rights to resources in the waters of the South China Sea, such rights were extinguished to the extent they were incompatible with the exclusive economic zones provided for in the convention." In an even broader inclusion, one finds the following: "The Tribunal also noted that although Chinese navigators and fishermen, as well as those of other states, had historically made use of the islands in the South China

Sea, there was no evidence that China had historically exercised exclusive control over the waters or their resources.” The Tribunal concluded that there was no legal basis for China to claim historic rights to resources within the sea areas falling within the “nine-dash line” (Permanent Court of Arbitration).

The Tribunal also ruled that China violated Philippine sovereignty by the following:

- Interfering with Philippine fishing and petroleum exploration
- Constructing artificial islands
- Philippine fishermen had traditional fishing rights at Scarborough Shoal and China interfered with these rights
- China’s interventions have created serious environmental and traffic problems in the area
- The Tribunal ruled that China had no legitimate control over the Spratly Islands, and has no rights to dredging or island building (Permanent Court of Arbitration)

China’s Reaction

Neighboring countries, and the United States, are waiting to see whether China’s furious rhetoric will be followed by threatening behavior. As a member of UNCLOS, China is supposed to obey the court. Unfortunately, the court has no enforcement mechanism. Now, in the aftermath of the ruling, the biggest question facing the countries of the South China Sea is whether Asia’s oceans will be governed by the rules of UNCLOS or whether those rules will be bent to accommodate China’s rising power.

China’s basic reaction to the U.N. decision was to reject it. Moreover, China views the rising turmoil in the South China Sea as the fault of the United States. China’s leadership sees a pattern of the U.S. and its allies (Japan, Vietnam, and The Philippines in particular) bullying China. The U.S. continues monitoring flights and “sniffer” efforts to try to maintain freedom of commerce lanes open (interviews). Some of the actions taken by China in the aftermath of the ruling are quite disturbing. The maritime authority of Hainan, an island province of Guandong, said it was closing an area in the South China Sea for three days while conducting naval exercises. Beijing has been talking about setting up an Air Defense Identification Zone in the area, requiring incoming aircraft to identify themselves to its authorities (*The Economist*, 2016). However, according to Admiral Harris, since the tribunal verdict “There hasn’t been any demonstrable change in Chinese behavior around Scarborough in terms of dredging or any of that activity. So I think we are at a place where truly we have to wait and see” (*WSJ*, 2016).

Admiral Harris also reported that various aspects of China’s record aren’t as bad as they may seem. For example that some of China’s seemingly aggressive intercepts of U.S. planes were caused by poor airmanship and not some signal from Beijing (*WSJ*, 2016). In actuality, China has been strangely quiescent since the Court rejected its territorial claims in the South China Sea and has made attempts to get along with the neighboring nations, especially Vietnam and The Philippines (*The Economist*, 2017).

Changes in the Philippines

In June of 2016 the presidency changed in the Philippines. Roberto Duterte replaced Mr. Aquino as president. Duterte changed course in the dispute with China. By standing up to China, the Philippines had to pay a price. The support Beijing gave other ASEAN members dried up for the Philippines. Filipino businesses were struggling in China, and very little investment flowed to the Philippines (*The Economist*, 2016).

Mr. Duterte announced he would end joint military exercises with the United States and might cancel the Defense Cooperation Agreement. In October, 2016, on a state visit to China, Mr. Duterte announced that he was distancing the Philippines from the U.S. for closer alignment with China. In return, Beijing promised billions of dollars in loans and investment and ended the blockade of Scarborough Shoal (*The Economist*, 2016). The two countries even expressed their desire for joint exploration for resources, something the Philippines had resisted up to now (*The Economist*, 2017). But what will happen in the next election in the Philippines?

There is a clear message for other Southeast Asian nations which have competing claims in the South China Sea: Cooperate with China and mutual trade will flow. The question for the Southeast Asian nations has always been what will the Chinese do next? Therefore, the existing uneasiness all around and the preference for an American presence in the Pacific. That situation has not changed.

The strife in the South China Sea will certainly continue. Although no side wants to provoke conflict, no one wants China to be the only power to dictate conditions. In the end of his book, *The South China Sea*, Hayton had suggested that if the nine-dash line were to be redrawn, the Sea could become a collectively managed region for the benefit of all (Hayton, 2014). Maybe Hayton's suggestion could be pursued further, if all parties would be willing to compromise.

Political Changes in the U.S.

The American led Trans-Pacific Partnership (TPP), signed in October 2015, was seen by President Obama as central to his foreign policy – the “pivot”, or “rebalance” to Asia and the Pacific. Twelve Pacific Rim countries signed on to this free-trade agreement, among them Canada, Australia, Japan, Singapore, Malaysia, Vietnam, Chile and Peru (*The Economist*, 2015). The treaty was aimed at economic reform. It would give improved access to the American market, lower tariffs, but above all concentrate on bringing down agricultural barriers and freer trade in services. The TPP promised greater access to markets for more service providers.

On November 8, 2016 the United States elected a new president – Donald Trump. Once in office, one of the first actions by the new president was to cancel U.S. membership in TPP. With American withdrawal, the survival of TPP faces an uphill battle. The remaining eleven countries may try to move forward. Japan and Canada have been in talks with other parties, and there is a chance that other countries may join. If the deal goes forward, the U.S. will have less leverage in future trade talks with member countries (*Bloomberg Businessweek*, 2017). According to Martin Wolf, Financial Editor of the *British Financial Times*, the president's withdrawal from the TPP trade pact was a monumental mistake (Wolf interview).

The U.S. led TPP was presented by President Obama as a way of countering China. Chinese President Xi has made free-trade agreements a major part of his strategy to expand China's influence in the South China Sea. The Regional Comprehensive Economic Partnership (RCEP), an ambitious all-Asia free trade deal, aimed to offset the impact of TPP, may now be the regional deal with the best chance of survival (Einhorn, 2015).

Although generally seen as a China-led initiative, the RCEP is under the auspices of Asean with the intent to meld the existing free-trade agreements that ASEAN has with six other countries (*The Economist*, 2017). In regard to trade deals done by China, they tend to focus on securing access to resources and markets and reducing trade barriers such as tariffs. In contrast to the TPP, there are no demands for increased protection of worker rights and environmental standards. According to a professor at Hong Kong's School of Economics and Finance, China will not insist much on anything when forming free-trade agreements (Einhorn, 2015).

A TPP failure will change the dynamics in the Pacific. The TPP had been stressed by President Obama as an attempt to stop China from writing the rules for Pacific countries. Asian nations threatened by Chinese territorial claims in the South China Sea will probably be wary about Chinese trade diplomacy (Einhorn, 2015). “If the RCEP goes through and the TPP fails, it's a huge political message” according to a lecturer at Monarch University in Melbourne (Einhorn, 2016).

The Most Recent Exacerbating Events

The U.S. is intent on maintaining freedom of the seas for commerce in the face of China's claim to 80 percent of the South China Sea and claims over the East China Sea. Moreover, there is the huge added complexity of North Korea's nuclear testing and its relationship to China (interviews). In August of 2017 North Korea fired a missile over Japan further destabilizing the Pacific turmoil (Reuters, 2017). Earlier in August North Korea threatened to fire four missiles into the sea near the U.S. Pacific territory of Guam

(Ibid). In the case of the North Korea-Japan scenario many expert observers suggest Japan will have to strongly react or face more North Korean provocations (Reuters, 2017).

Other recent events have added to the problems. In August of 2017, the USS John McCain was shadowed by Chinese frigates as it sailed in the East China Sea to monitor and perhaps enforce freedom of the seas. In May of 2017 PLA (China) fighter jets intercepted U.S. Airforce nuclear test “sniffer flights” in the East China Sea. The U.S. plane was conducting a routine mission in accordance with international law in international waters. The Chinese continue to view the flights as provocative. China declared an “air defense identification zone” over a large section of the East China Sea in 2013. The U.S. spokesperson refused to say whether the U.S. “sniffer flight” was in the Chinese zone (*Shanghai Daily*, May 22, 2017). In December 2016 a Chinese naval ship seized a U.S. underwater drone collecting oceanographic data for anti-submarine operations off the Philippine coast outside the area claimed by China. This could be considered a clear violation of international law (interviews). In another development in May of 2017 Japan scrambled fighter jets after four Chinese coastguard vessels entered what Japan considers its territorial waters near disputed East China Sea islands (*South China Morning Post*, May 20, 2017).

Competitive Reality

Beijing’s perspective on the maritime disputes is clear and straight forward. The tension is a consequence of U.S. efforts to contain China from attempts to control its historically rightful territory (interviews). The U.S. view is to underline freedom of the seas, the traditional rule of international law, and international political stability in the region (interviews). There are several dimensions to the conflict as we have shown in previous paragraphs including military, legal, political-economic, and diplomatic.

Regarding the military dimension, our research highlights recent events in previous paragraphs. Long term policy orientations represent another important dimension. We can quote Admiral Harry Harris, the commander of U.S. forces in the Pacific, in that respect. He states that the U.S. is advancing toward its goal of placing 60 percent of its air and naval assets in the Pacific by 2020. Moreover, the Navy is building to a fleet of 308 ships from 287 five years ago. Admiral Harris states, “So I can stand in front of anybody and tell them what I believe – the military component of the (U.S.) rebalance is real” (*WSJ*). Meanwhile, the Chinese continue to think long term about re-establishing what they perceive as their traditional sphere of influence including island building with airplane runways in the South China Sea and the East China Sea (interviews).

CONCLUSION: CONFLICT RESOLUTION STRATEGIES

Effective dispute resolution clearly needs to be multi-faceted. It needs to address military, regional, political, legal and economic issues. Most important, resolution strategies need to emphasize diplomatic solutions (interviews). The following suggestions represent our thinking regarding conflict resolution.

Perspective Education

All parties to the maritime disputes need to engage in continuous perspective education. This involves primarily three themes.

- Training in policy and perceptual “self-awareness” in order to better understand the relevant issues and social psychological dynamics of one’s own perspectives. This enables each actor to better understand their strengths and weaknesses regarding conflict resolution.
- Training in “other awareness” to underline the perspectives of other actors – allies and competitors – in the context of the disputes.
- Emphasis on history and culture.

Ethnocentrism and Cross-cultural Communication

The major problem in cross-cultural communication is ethno-centrism. Ethno-centrism is the perspective that one's own cultural orientation is the only "right" way to think and proceed. It is the rejection of other values and policies. The authors suggest the following strategies.

- Constant communication with allies and competitors within the context of strategies to avoid ethnocentrism.
- Constant communication to build relational context.
- Constant training in effective strategies for cross-cultural communication to support continuing negotiation.

Diplomatic Collaboration

The data from interviews of key professional observers suggests that given the military and political tensions the strongest approach to conflict resolution is collaboration (interviews). Conflict resolution strategies can include ignoring, command, competition, compromise, and collaboration.

- Diplomatic collaboration focuses on win-win approaches to maximize joint results. It seeks to create partnering relationships where common ground can be found. For example, it is clear that
- China and the U.S. are competitive on a number of levels but have a huge mutual interest in the peaceful outcome of the disputes. If they can partner enough to dispel distrust they can make progress. Some evidence shows China has already moderated some of its positions, as has the U.S. (interviews).
- Collaboration sees conflict as natural and recognizes that mutually beneficial solutions may best advance commitments to solutions (interviews).
- U.S. collaborations with allies is an important effort that needs to be conducted on the basis of effective cross-cultural communication establishing "self-awareness" and "other-awareness." "Self-awareness" and "other-awareness" needs to apply to collaboration with allies and China (interviews). It also applies to China's efforts as well as U.S. efforts.

Alliances

- Alliances are the path to more effective influence e.g. U.S., Japan and Vietnam; China and Southeast Asia.
- Alliance building and partnering with competitors.
- Constant efforts at teambuilding emphasizing goals, roles, and trust development with potential allies and competitors.
- Need to explore new alliance possibilities, e.g. U.S. and India.
- Understand what is necessary to take off the table regarding alliance building and negotiation strategies.

Collaboration for China Inclusion

It is clear that China is a rising power. Even more broadly it is becoming a multi-polar world. Regarding the maritime disputes, the U.S. and its allies seek to uphold the rule of law and freedom of the seas. Some observers conclude that if the U.S. and its allies push back against China's rise too aggressively it will isolate China. Concurrently, if China asserts itself by ignoring the claims of other nations in the South China Sea and the East China Sea it will engage in self-isolation (interviews).

Isolation is hugely problematic. Admiral Harris recently made several important points about China and its potential isolation. Harris said, "We don't want China to be isolated. Isolation is a bad place to be...it's dangerous." Moreover, he also believes China seeks hegemony in East Asia. He told the U.S. Congress in February of 2016 that China's ambition is not incompatible with the ambition that China become a "responsible stakeholder" in the liberal, rules-based international order. Clearly, Admiral Harris while believing in a strong asymmetric defense capability, he underlines that the "main battle" must be fought on the diplomatic front (*Wall Street Journal*, August 6-7, 2016).

The Compromise Option

We conclude that compromise is a secondary strategy. Compromise differs from collaboration in that involves not as much emphasis on win-win partnering efforts. Compromise occurs when each party gives up something of value to the other. Other conflict resolution options such as ignoring behavior and accommodation are not appropriate for the highly competitive nature of the regional turmoil.

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