

# Assessing China's Rise in East Asia: A Domestic Politics Perspective

By

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## ABSTRACT OF THE DISSERTATION

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Following the direction of the political consideration of domestic factors, I will introduce the domestic politics to explain puzzles on China's foreign policy and the reaction of neighbors to the rise of China. These puzzles can be better answered by including considering domestic politics. Furthermore, three research questions from different directions applying considerations of domestic politics to foreign policies will be asked respectively in the following chapters in order to fully address countries' interactions in East Asia with the rise of China. The first cut is to examine the diversionary theory to China's external conflicts. What is the mechanism for China to post aggressive behaviors on its neighbors? Next, I will examine how China's neighbor signals its true intention to China: Taiwan military expenditure as a signal to Mainland China. Last but not least, I will turn to explain China's rationale for using non-conflict – economic sanctions – behaviors in with its neighbor, including South Korea and Taiwan.

# Acknowledgment

“因為需要感謝的人太多了，就感謝天罷。” \_\_\_\_\_

陳之藩 < 謝天 >

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## Part I

# Introduction

## 1 General Theme:

### Assessing China's Rise in East Asia: A Domestic Politics Perspective

In the recent years, we have witnessed a heated debate on China's rise, peaceful or not, in both media and academia. Xiang, Primiano and Huang (2015) show sharply growing news in the *New York Times* and various studies on the rise of China in academic journals. Although without a general agreement in the debate, scholars (e.g., Mearsheimer, 2001; Johnston, 2003; Wang, 2011) have provided plenty of analyses on how China will rise as a great power in the security dimension after economic reform. For instance, Mearsheimer (2001) argues that great powers will use force to alter the balance of power and thus are "primed for offense"(pp.2-3). This way, "[t]he result would be an intense security competition between China and its rivals, with the ever-present danger of great-power war hanging over them"(p. 4). In contrast, Johnston (2003) disagrees with Mearsheimer and concludes that "the PRC has become more integrated into and more cooperative within international institutions than ever before"(p.49) while comparing China's behaviors as a status quo player. However, he exempts his conclusion from two issues: domestic social unrest and issues regarding Taiwan. Put differently, it is still a question of whether China rises peacefully and also depending on the direction of discussions.

As Putnam (1988) noted, the political consideration of domestic factors is an indispensable condition to explain foreign politics. Quek and Johnston's (2018) on the domestic public opinion and the development of external disputes China involved is an instance. Following this direction, I will introduce the domestic politics to explain puzzles on China's foreign policy and the reaction of neighbors to the rise of China. These puzzles can be better answered by including considering domestic politics. Furthermore, three research questions from different directions applying considerations of domestic politics to foreign policies will be asked respectively in the following chapters in order to fully address countries' interactions in East Asia with the rise of China. The first cut is to examine the diversionary theory to China's external conflicts. What is the mechanism for China to post aggressive behaviors on its neighbors? Next, I will examine how China's neighbor



signals its true intention to China: Taiwan military expenditure as a signal to Mainland China. Last but not least, I will turn to explain China's rationale for using non-conflict – economic sanctions – behaviors in with its neighbor, including South Korea and Taiwan.

## 2 Provoking Disputes for Attention Diversion?

### Policy Choice of Chinese Foreign Policy

As mentioned previously, scholars in international relations often address the rise of China and its foreign policy with international factors, like China's power in international politics. This way, the first cut posits a explanation of China's external conflicts through the lens of domestic politics. This chapter turns to the framework of diversionary theory and conducts multiple empirical strategies to verify this argument to the case of China.

The diversionary theory is popular to both policy and academic discussion connecting domestic politics and foreign policy actions. When facing domestic problems, state leaders have incentives to divert domestic attention to external conflicts to stay in office. Moreover, launching external conflicts is not the only option for government in crisis to secure its regime stability. Based on these arguments, we set up hypotheses to test the diversionary theory on China. We propose multiple empirical strategies to identify the relationship between regime security and suggested policy options respectively with ICEWS data from 1995 to 2015. The results of empirical testing are interesting to the diversionary hypothesis: the case study, which has the similar method to the policy discussion, provides mixed results. However, the systematic measures of China's behaviors firmly rejected it. We also identified the policy substitution in models measuring all categories of conflicts.

The article is expected to contribute to the literature as follows: first, we continue Johnston's (1998) first cut on China via the diversionary argument with up-to-time coverage and more comprehensive analysis; second, the article applies the event data rather than MIDs to traditional diversionary study. The data is expected to provide more detail information on conflicts than MIDs; last but not least, we posit an argument of the policy substitutability between domestic repression and external aggression, which provides a more sophisticated logic to bridge domestic politics and international conflicts.

### 3 Signaling, Trade, and Taiwan's Military Spending Puzzle

The second cut turns to answer the question on how China's neighbor signal its true intention to China. Taiwan will be the case to explore for the following two reasons: first, the Cross-Strait relation is one of exceptions to Johnston's conclusion on China's peaceful rise; second, Taiwan and its international status is one of the most crucial issue to the PRC. A good model explaining cross-strait relations would provide a hint to other neighbors which are also facing asymmetric defense capability with China. However, little attention has been paid to Taiwan's counterintuitive defense spending decrease regardless to extensively studies on how China's rise will shape international security.

While Mainland China has significantly increased military spending since the mid-1990s, Taiwan has been cutting its defense spending. The military gap in Cross-Strait relations increases since the late 1980s in terms of both GDP ratio and constant numbers. With data from SIPRI, it is clear that Taiwan has decreased its defense expenditure from 5% to 2% of its GDP. We put forth an original theory to explain this puzzle. It argues that the significantly expanded cross-strait trade makes Taiwan more willing to cut defense spending to signal Mainland China that Taiwan is not an independence type.

Empirically, we conduct an empirical investigation at both aggregate and legislator levels. The aggregate level of analysis allows a comparative analysis of the competing arguments in one unified framework. Furthermore, we take an innovative approach to empirically test our theory. By investigating the determinants of Taiwanese legislators' pro- or anti-defense spending preferences, this study identifies the causal mechanism directly based on the actors who make decisions on the defense budget. The results at both levels of analysis demonstrate that trade with Mainland China reduces Taiwan's defense spending. In sum, this article provides a new but comprehensive explanation to the unanswered but crucial question in Cross-Strait relations.

### 4 A Rusty but Provocative Knife? The Rationale behind China's Sanction Usage

After South Korea Terminal High Altitude Area Defense (THAAD) deployment in 2016, China has launched a series of "economic sanctions" to South Korea, affecting personal visiting, department stores, and Korean industries in China.

The Global Daily also have called consumers to boycott Korean goods and hotels. Surprisingly, the Chinese Foreign Ministry has never positively announced or affirmed these "economic sanctions" to South Korea on the issue of THAAD. Put differently; the sanctions usages did not reveal strong resolution from Beijing government and its leaders on the issues. In the end, South Korea did not cancel its THAAD implementation because of China's sanctions.

In the paper, I explain China's rationale to impose puzzling economic sanctions, which has a weak resolution, to South Korea and Taiwan. As signaling theory argues, economic sanction with insufficient resolution, which is doomed to fail, is more likely to become a more provocative foreign policy than expected. With the case study of South Korea and Taiwan on China's sanctions, the paper proposes a bureaucratic competition theory to explain the rationale of sanction usage in China: these sanctions are for pleasing the CCP by the domestic agencies. The paper examines position changes of leaders in organizations, including those initiated sanctions and those in charging the disputes, in both cases to support the argument. I additionally address two alternative explanations to the proposed discussion.

## Part II

# Provoking Disputes for Attention Diversion? Policy Choice of Chinese Foreign Policy

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<sup>1</sup>This ia a co-authored paper with Greg.

### **Abstract**

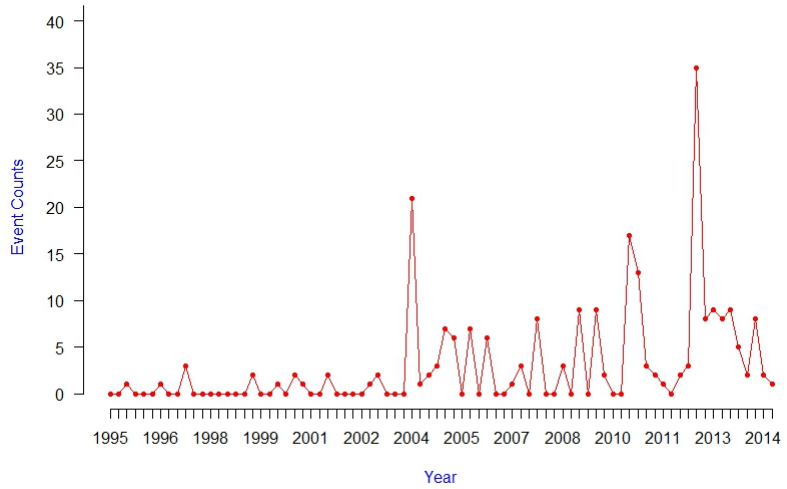
The diversionary theory is popular to both policy and academic discussion connecting domestic politics and foreign policy actions. When facing domestic problems, state leaders have incentives to divert domestic attention to external conflicts to stay in office. Moreover, launching external conflicts is not the only option for government in crisis to secure its regime stability. Based on these arguments, we set up hypotheses to test the diversionary theory on China. We propose multiple empirical strategies to identify the relationship between regime security and suggested policy options respectively with ICEWS data from 1995 to 2015. The results of empirical testing are interesting to the diversionary hypothesis: the case study with the similar method to the policy discussion provides mixed results. However, the systematic measures of China's behaviors strongly rejected it. We also identified the policy substitution in models measuring all categories of conflicts.

# 1 Introduction

Since Sixteenth Party Congress in November 2002, China had begun a top leadership transition from Hu Jintao to Jiang Zemin as Hu became Chinese Communist Party (CCP) general secretary and president in the following year. However, the power transition to Hu was not completed until Jiang resigned from the Party Central Military Commission (CMC) chairman in 2005.<sup>2</sup> At the same time, we observe a dramatic increasing number of military conflicts since late 2003 initiated from China to Japan in the disputed waters in the Figure 1.<sup>3</sup>

**Figure 1:**

*Maritime Disputes from China to Japan, 1995-2014*



In addition to the leadership transition between Hu and Jiang, changes of China's economic performance revealed relative relations to the external conflicts. Chinese economy had a bad performance in terms of inflation and real

<sup>2</sup>Bo (2007) shows that Jiang was unwilling to retire from the CMC position from the Sixteenth Party Congress in 2002 to the Fourth Plenum of the Sixteenth Central Committee in 2004 (pp. 346-347). Hu has finally consolidated his power regarding the national military strategy and position appointments in between 2004 and 2005 (pp. 423-425). See discussions on China's political transition from Jiang to Hu in Bo, 2007.

<sup>3</sup>We use ICEWS data to generate the Figure 1 by setting actors, event intensity and geographic information. The detailed coding will be discussed in the section of the research design regarding the ICEWS data.

GDP growth: the inflation reached a record (4.9%) from 2010 to 2011 since 2000; China's real GDP growth rate suddenly dropped to 11% in 2011 from 17% and 18% in 2009 and 2010, respectively. At the close period, Japan Coast Guard found more frequent and severe Chinese governmental activities in the Senkaku Islands from the third quarter of 2010 to the early 2011<sup>4</sup>. Figure 1 also posits another peak of conflicts in Sino-Japan relations in the similar term.

These episodes on the leadership transition and economic performance lead us to arguments of the well-known but debated diversionary theory (e.g., Rummel, 1963; Zinnes and Wilkenfeld, 1971; Gelpi, 1997; Miller and Elgun, 2010) in international relations: states will provoke external conflicts to distract domestic dissatisfaction. By diverting domestic attention on governances or fostering nationalism to support governments resulting from external conflicts, leaders can increase its probability to survive. In addition to the academic discussions, the diversionary theory is also well-applied to the policy and media domain. For instance, there are claims that Bill Clinton had applied the strike to terrorists in Sudan and Afghanistan to divert public attentions from his White House scandal in 1998.<sup>5</sup> The American strike on Syria in April, 2017 is another diversionary store which Trump want to distract domestic attentions from his health care and immigrations bills.<sup>6</sup> Back to our observation on China's use of force to Japan, the real intention for China to initiate the external conflicts was not to wage war against Japan or other countries, but for domestic distraction, under the assumption of the diversionary theory.

Nevertheless, there should be more options for China's government to secure

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<sup>4</sup>See detail report at [http://www.kaiho.mlit.go.jp/info/books/report2012/html/honpen/p066\\_02\\_01.html](http://www.kaiho.mlit.go.jp/info/books/report2012/html/honpen/p066_02_01.html).

<sup>5</sup>Tierney, Dominic. Jun 15, 2017. The Risks of Foreign Policy as Political Distraction. *The Atlantic*. at <https://www.theatlantic.com/international/archive/2017/06/trump-diversionary-foreign-policy/530079/>.

<sup>6</sup>Gordon, Philip. April 07, 2017. Is Trump Wagging the Dog in Syria? *Politico Magazine*. at <https://www.politico.com/magazine/story/2017/04/why-did-trump-bomb-syria-215001>.

its regime security. By considering literature of the authoritarian regime survival (e.g., Smith, 1998; Enterline and Gleditsch, 2000; Carey, 2010), China's government should be able to choose between policy options to counter domestic pressure on its regime in addition to conventional diversionary theory. With the utility argument on China's regime survival setting up by the diversionary framework, we argue the substitution effect between domestic repressions and external aggressions.

Given that debating empirical findings in the diversionary literature, we have multiple empirical strategies to test the argument and the proposed substitutability relations between these options: a case-study design at the conflict-event level, a series of generalized linear models at the country-dyad level, and a test of substitutability between policy options. In the first two tests, we test the relationship between regime security and proposed policy options respectively with ICEWS data from 1995 to 2015. The conflict-event level analysis examines changes in external conflict before and after major disasters, which can threaten public opinion expectation on governance, in China. On the other hand, the country-dyad level analysis, we fit sets of models with various specifications with the dispute counts or intensities as dependent variables and measures of regime insecurity as critical independent variables. The regime insecurity is gauged by domestic inflation, GDP growth, and levels of domestic unrests. Other variables, for example, trade interdependence and military spending of the countries, are controlled. We also performed robustness checks to ensure consistency of our argument. In addition, we posit a test to identify the substitution relations between domestic repression and China initiated external conflicts.

The results of empirical testing is interesting to the diversionary hypothesis: the case study provide mixed results to the diversionary theory hypothesis but strongly rejected by the systematic measures of China's behaviors. China's gov-



ernment responds to domestic threats of regime stability by domestic repression but not external conflicts. Moreover, we identify strong negative significant correlation between domestic unrests and external conflicts over different robustness checks. This way, we reject the diversionary theory hypothesis with the systematic measures of China's behaviors. In the test of two policy options, we confirm the substitution effect between external conflict and domestic repression measuring by all event categories. Given the nature of internal and external conflicts, it is hard to believe that these small domestic and international frictions could have affected economic conditions of such a large economy like China, so we could almost argue that the story in this paper depicts a causal relation. Indeed, to be fully satisfied with this assertion, we need further investigations with better identification strategy and more sophisticated measurement of the substitutionary relationship of policy tools.

Lastly, the article is expected to contribute to the literature as follows: first; we continue Johnston's first cut on China via the diversionary argument with latest time coverage; second, the article applies the event data rather than MIDs to traditional diversionary study; last but not least, we provide an argument on the substitutability between domestic repression and external aggression, which give a more sophisticated logic to bridge domestic politics and international conflicts.

## **2 Existing Arguments on China's External Conflicts**

With the rise of China's power, scholars posit different analyses of China's behaviors on external conflicts. With the theory of state maximization of its share of world power, Mearsheimer (2001, 2006, 2010) argues China will strive to establish its regional hegemony in Asia. Hence, it is likely "[t]he result would be an intense

security competition between China and its rivals, with the ever-present danger of great-power war hanging over them” (Mearsheimer, 2001, p. 4). In contrast, Fravel (2010a) argues that China has little reason to act as offensive realists and power-transition theory predictions posit because of the limited potential benefits gained from territorial expansion. Empirically, Johnston (1998) examines Chinese military behavior via MID data from 1949 to 1992, and shows that China has been more “dispute prone than many other major powers” (p.17). On the other hand, Xiang, Primiano and Huang (2015) test correlations between Chinese rising material power and militarized interstate disputes, which China involved from 1979 to 2010. However, they found no empirical support the arguments of the non-peaceful rising of China.

In addition to studies on China’s overall patterns on intrastate conflicts, China’s maritime disputes with neighbors attract scholars attentions and debates. For examples, Gurtov and Hwang (1998) refer to China’s actions on Spratlys as tests of “China’s [peaceful] strategic intentions in the region” (p. 266). Moreover, Kaplan (2014) posits China’s recent naval assertiveness in the South China Sea as the trigger to a growing potential arms race among countries involved in maritime disputes. Koo, 2009 argues trade interdependence as the main factor to repeatedly de-escalate maritime disputes conflict between Japan and China from 1968 to 2005. Trade interdependence and the territorial concerns determine China’s behavior in the water. In spite of energy and sovereignty concerns, Wiegand (2009) argues China’s strategic use of the enduring disputes is to gain greater bargaining power with Japan on other issues from 1978 to 2008. In other words, China’s real purpose on these issues is not to settle them down. Instead, it is China’s strategy gain compromise from Japan on other issues by effectively using disputes.

Kaplan, 2011 argues that China’s behavior in the South China Sea as a rising regional power is similar to the United States in the Caribbean Sea in the

late 19th centuries. Thus China's behavior might bring the military competition to the disputed area, especially under the wave of nationalism. Yahuda (2013) explains China's new assertive actions in the South China Sea via its rising military power, nationalism after 2008, and Asian policy of the US. Nevertheless, the economic interdependence between China and other countries constrains further high-level conflicts from happening. On the other hand, Fravel (2011) argues China is most likely to apply delaying strategy instead of compromising to maintain its status quo benefits. However, China may compromise if the issue salience of disputes alters, such as regional countries bandwagoning China and seeking the US participation. Different from arguing China's behavior of external conflicts via international factors, we propose a new direction following diversionary theory to explain China's behavior. It is China's strategy to divert domestic attention to external conflicts and altering between another policy option, domestic repression.

## 2.1 Diversionary Theory

According to the well-known diversionary theory in international relations, states will provoke external conflicts to distract domestic dissatisfaction (e.g., DeRouen, 1995; Gelpi, 1997; Mitchell and Prins, 2004; Miller and Elgun, 2010; Powell, 2012).<sup>7</sup> By studying U.S. presidents' decisions in international crises, (DeRouen, 1995, p. 690) identifies an indirect link between the economy, politics, and the use of force that "the president will continue to have incentives for using force as approval ratings suffer at the hands of a chronically weak economy and the related deficit." In other words, he posits that good foreign policy can compensate for bad domestic outcomes. Gelpi (1997) shows strong supports with models covering 180 states

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<sup>7</sup>The prospect theory, which takes circumstances of risk into decision making (Kahneman and Tversky, 1979), provides another direction to link domestic politics to foreign policy. See applications of prospect theory in explain China's crisis behavior with the expected risk of political survival to China's leader during each crisis in He, 2016.

from 1948 to 1982 under a broader definition of leaders' incentives to externalize domestic conflicts. Miller and Elgun (2010) also suggest a positive relationship between domestic instability and the use of diversionary foreign policy in Latin America. In the case of China, the diversionary theory also attract scholars attentions(e.g., Christensen, 1996; Johnston, 1998; Fravel, 2005; Li, 2013). Christensen (1996) refers to the rally public support to the Great Leap Forward from Mao by initiated Second Taiwan Strait Crisis in 1958. Johnston (1998) estimates an OLS model of effects from sanctions, riots, protests, and executions to MIDs but sees negative relationships between domestic factors and external conflicts.

Nevertheless, not all studies agree with diversionary research method and conclusions(e.g., Rummel, 1963; Levy, 1989; Meernik and Waterman, 1996; Fravel, 2010*c*). Levy (1989) questions the theoretical framework limited to “descriptive correlational analyses” and conditions for states to divert by different threats (p.283). He also suggests that analysis with a smaller number of cases, which can provide “a more careful examination of the motivations of decisionmakers”(p. 284), can be an answer to his critique. Fravel (2010*c*) questions the key assumptions of diversionary theory via mostly likely case study design. He finds the theory can hardly explain both Argentina and Turkey's invasion of the Falkland Islands and Cyprus respectively. Empirically, Rummel (1963) conducted a cross-national study in the period between 1955 and 1957 but found no empirical support for either foreign or domestic conflict.

Policy substitutability is another dimension worthy to mention in addition to the conventional diversionary theory focusing mostly just on external conflicts. It is a concept introduced by Most and Starr (1984), focusing on relations between options that decision maker could have to deal with crisis.<sup>8</sup> Back to the diversionary theory, there is a set of policy options for the decision maker to deal

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<sup>8</sup>See discussions and applications of policy substitutability in Most and Starr, 1984; Starr, 2000; Palmer and Bhandari, 2000.

with regime stability. Launching external conflicts is one of the options. While considering other measures than external conflicts for China to secure its regime stability in crises, we incorporate domestic repression into account for China as an authoritarian country.<sup>9</sup> We are not the first but also not the most to consider domestic repression as an alternative policy option in the diversionary framework(e.g., Gelpi, 1997; Enterline and Gleditsch, 2000; Oakes, 2012). Gelpi (1997) shows strong supports with models covering 180 states from 1948 to 1982 under a broader definition of leaders' incentives to externalize domestic conflicts. He argues that autocratic leaders are more likely to repress than divert the domestic unrest in contrast to democratic government. The democratic system prevents the option for leaders to directly repress unrests. To further testing external conflicts and domestic repression within countries, Enterline and Gleditsch (2000) set up hypotheses on the complementary relations between these policy choices in facing challenges to the ruling leader. However, they find little evidence supporting the complementary effect between two policies with all countries within the COW project from 1948 to 1982. Following the design of including domestic repression into diversionary arguments, we argue that it is China's strategy to divert domestic attentions to external conflicts and altering between another policy option, domestic repression.

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<sup>9</sup>Mentioning supports from winning coalition and selectorates is another option for countries facing the problem of regime security(e.g., De Mesquita et al., 2002; Pickering and Kisangani, 2005). However, we do not include pleasing supporters with public and private goods within the set of policy choice for China for the following reasons: first, the selectorates in China usually refers to the composition of the Central Committee(Hanson and Gallagher, 2012), which the size of the selectorates remain constant. On the other hand, Cao and Ward (2015) also refer to the limited possibility for the government to provide public goods for the size of winning coalitions in China.

### 3 Research Question: the Hypothesis of Diversionary Theory and Policy Substitution

To analysis China's actions of foreign policy, the diversionary theory is an interesting and popular argument begin with. This is expected to break the black box of decision making on China's foreign policy. Following the diversionary theory, domestic unpopularity leads to initiation of military actions abroad or other policy action as the government wants to maximum the possibility to stay in the office. We set the first hypothesis:

- H1: China will respond to threats to its regime stability by either domestic repression or foreign aggression to its neighboring countries.

To verify this hypothesis, we consider not only military actions, but also take verbal conflicts into account, because if the motivation is to divert public attention away from domestic issues, low-level conflicts are sufficient, and militarized disputes are not necessary and could be too costly. To measure domestic instability as threats to the regime insecurity, we use economic indicators, such as GDP growth rate and inflation rate, to measure public dissatisfaction with the regime in the economic dimension. Beside, we also try to proxy the level of domestic unrests directly.

In addition to the test on China's policy reactions to domestic instability, the substitutability effect is another dimension worthy to mention in addition to the conventional diversionary theory focusing mostly just on external conflicts. As Most and Starr (1984); Starr (2000); Palmer and Bhandari (2000) show, domestic repression is another possibility, especially in the authoritarian regime. This way, we have the second hypothesis regarding the relationship between two policy options,

- H2: Substitutability, the negative relationship, exists between domestic repressions and external aggressions.

With the assumption of government capability to choice between options, this argument can be illustrated as a choice model of the Chinese government maximizing its utility of regime survival. Mostly, the government is comparing between allocating optimal efforts on provoking external disputes and committing internal repression vis-a-vis doing nothing in responding domestic turmoils. Given the debating empirical results in the diversionary literature, we propose the following multiple empirical strategy — case-study design at the conflict-event level and systematic quantitative analysis at the country-dyad level — to verify the proposed hypothesis suggested by the diversionary logic.

## **4 Case Studies at the Conflict-Event Level:**

### **A Brief Picture of Diversionary Theory Application to China**

We first provide a brief picture on the argument by comparing numbers of external conflicts before and after particular news related to China's major public safety accidents in 2014 and 2015. The selection of these two years is that it is relatively possible to acquire sufficient news reports on the latest events. With this conflict event level analysis, we can know whether the breakout of an event, which can decrease public supports to China's government, led to more external conflicts or not. Moreover, this case-study design, which focuses on particular incidents, is close to the policy discussions, like those cases on Clinton and Trump mentioned earlier. This way, it is expected to directly strengthen the identification of external conflicts and the diversionary story.

We argue that the events about the significant public safety accidents in China are an ideal proxy to strengthen our diversionary story for the following two reasons: first, it is clear that this event has only negative impacts on China's governance, which is for sure a threat to the CCP's regime security. For instance, Chinese public questions government's reaction and governance right after the 2015 Tianjin explosions.<sup>10</sup> Comparing to the natural disaster such as 2008 Sichuan earthquake, the Chinese public has both positive and negative expression to their government. For the positive one, China's government received 76.2 billion RNB of domestic donations and more than thirty thousand volunteers to support governmental rescuing actions in the Sichuan province.<sup>11</sup> On the other hand, there are also some China citizens questions government's reaction and intention to hide the real causality numbers.<sup>12</sup> In addition to the apparent and one-way influence of public safety accidents to China's governance, the occurrence of this accident category is exogenous from government's controls that government is unable to use this event to manipulate domestic public opinions. A comparison event also with negative impact to the government in addition to our proposed one is the China's anti-corruption movement. China's government has much stronger power on when to initiate an anti-corruption movement than the happening of a significant public safety accident.

To find out the major public safety events, we use keywords include "major accidents," "public safety," and "deaths" in both Mandarin and English. Given that natural disaster usually does not downgrade public expectation on the government, we exclude them from the data. With keywords, searching in the Google News, we identify six major public safety accidents, which are possible to create

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<sup>10</sup>See news at <https://www.rfa.org/mandarin/yataibaodao/meiti/xl2-08142015105333.html>.

<sup>11</sup>See news at <http://www.gongyishibao.com/zhuan/csdh/juanzeng/news1.html>.

<sup>12</sup>See news at <https://web.archive.org/web/20091130165405/http://www1.voanews.com/chinese/news/china/CHINA-EARTH-QUAKE-20091126-74763557.html>.



a negative image of the CCP government, between 2014 and 2015. Moreover, we search again on each case to distinguish its significance to the public for following conditions: (1) at least vice-province level government officials being punished afterward; (2) reporting in the English newspaper, including the English version of People’s Daily; and (3) happened in the first-level significant cities. If a case matches two of three conditions, it will be coded as *High* for *Significance*. By comparing changes of external conflicts before and after the event between cases with different categories of significance, we know that those with stronger impacts to the government performance will lead to more external conflicts afterward and support our diversionary story.

**Table 1: External Conflicts before and after major public safety**

	Events	Significance	D-5	D0	D5
2014/8/2	Explosion, Kunshan	High	31	2	7
2015/1/1	Stampede, Shanghai	High	3	2	12
2015/6/1	Boat Sinking, Hubei	Low	1	2	2
2015/8/12	Explosion, Tianjin	High	8	0	10
2015/11/27	Mining Accident, Heilongjiang	Low	1	0	0
2015/12/20	Landslide, Shenzhen	High	2	0	13

To measure Chian’s use of external conflicts, we use the ICEWS dataset and aggregate the count of events in all categories initiated by China to its maritime neighbors by each day. To demonstrate a simple picture of each event and external conflicts, we select five days before and after each event. From the Table 1, we have the mixed results to support the diversionary hypothesis: numbers of external conflicts increase in all four high significant events but not those with low significance to China’s governance; however, there are more external conflicts right before two out of four high significant events (Kunshan and Tianjin Explosion). It is hard to conclude that these events on major public safety lead to more

use of external conflicts initiated by China. This finding is consistent with the debating result in the diversionary literature. All in all, it is unclear whether the diversionary theory is true in the case of China according to this design in the micro and event-based level. A systematic empirical is useful to further verify the proposed hypothesis.

## 5 Systematic Quantitative Analysis

Following the theoretic framework of this research, we first present a case-study design to have a brief picture of the diversionary theory to China as other policy discussions. However, the case study at the conflict-event level does not give us a persuasive conclusion to the diversionary theory. A systematic empirical might be useful to further verify the proposed hypothesis. Hence, we have a series of generalized linear models at the country-dyad level to identify the relationship between regime security and proposed policy options respectively with ICEWS data from 1995 to 2015. In addition, we posit another regression model to test the proposed hypothesis on the substitution effect between domestic repression and China initiated external conflicts.

### 5.1 Policy Option Identifications

To identify relations of China's diversionary actions, we propose mixed-method empirical strategies: country-dyad level and conflict-event level analysis. In the first approach, we have regressions with external conflicts as the dependent variables and measures of the regime insecurity as independent variables. The regime security is measured by domestic inflation and levels of domestic unrests. In addition to the coefficient between external conflicts and measures of regime insecurity, we investigate five major events of public safety in China in 2015 and compare the

change of external conflict before and after those cases of public safety. The combination of both methods is expected to provide stronger identifications between external conflicts as a policy option to domestic insecurity.

### 5.1.1 Dependent variables

As Fravel (2005) argues, China tends to compromise rather than launching conflicts in land-related territorial disputes owing to concerns of regime security. Put differently, China's government distinguishes the importance of land-related and maritime territorial disputes differently by effects to regime insecurity. As maritime disputes threaten China regime less than land-related, it is an ideal policy option for China government to launch external conflicts on these disputes to divert domestic attention to secure its regime stability. This way, our sample focus on maritime disputes and China's external conflicts with neighbors connecting by the territorial sea in the paper.<sup>13</sup>

We use the Integrated Crisis Early Warning System (ICEWS) dataset<sup>14</sup> spanning from 1995 to 2015 as the data source for dependent variables. Compared to the traditional MIDs, the ICEWS is an event dataset that not only has the latest coverage of conflicts but also provides more detailed information. This includes geographic location, state as well as sub-state actor label, and scales for events. Geographic and actors' information enables us to have more detailed stories on Chinese maritime disputes. Moreover, the coding of event scales using the CAMEO category allows us to generate the event intensity variable via the ICEWS.

To identify the impact regime insecurity to China's choices between initiating external conflicts and committing internal repression, we first have events of

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<sup>13</sup>These countries include North Korea, South Korea, Taiwan, Indonesia, Japan, Vietnam, Malaysia, Brunei, Philippines.

<sup>14</sup>The data is available at <https://dataverse.harvard.edu/dataset.xhtml?persistentId=doi:10.7910/DVN/28075>.

China's domestic repression to domestic Chinese actors and foreign aggression to other states as two separated dependent variables. With the advantages on the detail information of actors in the event data, we generate *Domestic Repression* using China domestic conflict initiated by governmental to non-governmental actors in each quarter. These actors are identities by examining *Target Name* and *Source Name* for all China domestic event, which has both *Source Country* and *Target Country* as China, in the ICEWS. For *Foreign Aggression*, we have the variable for China's external conflicts, which is the quarterly counts of conflicts China initiated in the dyads of all China's neighbors connecting by the territorial sea. In other words, we have conflict event with China as *Source Country* and other countries mentioned in the footnote 12.

Both domestic repression and foreign aggression include all conflicts, which means events with negative intensity.<sup>15</sup> Under the consideration that severer events will pose stronger impacts on governmental choices, we also estimate models which only take material (non-verbal) events into account<sup>16</sup> and are labeled as *NV* in the tables. *No. 107 Demand settling of disputes* and *No. 138 Threaten with military force, not specified below* are examples for the verbal events in the CAMEO coding. In other words, there are four different measures of dependent variables in our model as robustness test. For the convenient of interpretation, we reverse the sign from negative to positive for all variables measuring conflict events.

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<sup>15</sup>See the CAMEO codebook for the detail description of each event category at <https://dataverse.harvard.edu/dataset.xhtml?persistentId=doi:10.7910/DVN/28075>.

<sup>16</sup>See the definition of material and verbal events in the CAMEO coding, which distinguishes event categories into verbal and material actions. The latter usually has a higher intensity than the former.

### 5.1.2 Independent variables

As elaborated above, we argue that weak economy, especially the change of economic conditions, leads to possible regime instability, and government makes policy choices between having internal repressions or initiating external conflicts. Thus the first set of independent variables in this research is common economic indicators using diversionary theory literature<sup>17</sup>:

*Real GDP Growth* is the change of real gross domestic product as percentage change to the previous period from 1994 to 2015 provided by the *International Financial Statistics* (IFS).<sup>18</sup> The IFS has information for each quarter from 2001 to 2014 but only annual one for 1994 to 2000 and 2015. By comparing annual and the quarterly data in the IFS, we know that the IFS annual real GDP growth is the average of all quarters.<sup>19</sup> This way, we first have the change of annual real GDP growth and divide the annual value by four to generate data for each quarter from 1994 to 2000.

*Inflation* is the change of the inflation rate in China for each quarter. We acquire China's consumer price index for 1993 to 2015 from *China Data Online*<sup>20</sup> and convert it to yearly inflation rate from 1994 to 2015.<sup>21</sup> To be consistent with the coding for the real GDP growth, we also divide the annual change of inflation by four to have values for each quarter.

It is difficult to attain applicable measures of China's domestic riots and protests. We use the ICEWS to generate a proxy measuring *Domestic Unrests*, which is the absolute values and counts for domestic conflicts initiated from non-

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<sup>17</sup>See detailed measures of bad economy at Mitchell and Prins (2004) and Miller and Elgun (2010).

<sup>18</sup>At <https://www.library.auckland.ac.nz/databases/record/?record=ifs>.

<sup>19</sup>For example, China's real GDP growth from the IFS for each quarter in 2014 is 9.47%, 10.57%, 9.80%, and 9.60%. The average of each quarter from the IFS data is closer to the 7.3% reported from the World Bank for 2014.

<sup>20</sup>At <http://chinadataonline.org/>.

<sup>21</sup>Inflate rate = (Current Period CPI – Prior Period CPI) / Prior Period CPI.

governmental to governmental actors in China. With actors' specification in the data, this variable has no endogeneity problem with dependent variables for Table 2. To consist of dependent variables, there are four measures of *Domestic Unrests* corresponding to different constructions of dependent variables.

In addition, this study follows suggestions from previous literature (e.g., Miller, 1995; Koo, 2009 and Kaplan, 2011) on how to incorporate measures on the system level, including *Relative Power* and *Trade Salience*. *Relative Power* measures the relative military capability of two countries, ranging from 0 to 1, the higher, the more unbalanced. This relative military capability index is constructed as a ratio of the weaker power over the stronger power. The constant value of military expenditure is from the SIPRI Military Expenditure Database.<sup>22</sup> Given that the SIPRI provides annual military spending, we apply the converging equation using for China's inflation rate and real GDP to create quarterly relative power between China and other maritime neighboring states.

*Trade Salience* is defined as  $\sqrt{\frac{\text{dyadic trade}}{\text{total trade, China}} \times \frac{\text{dyadic trade}}{\text{total trade, other state}}}$ . It is a measure introduced by Barbieri (1996) and employed by many trade conflict studies.<sup>23</sup> In trade-conflict theory, states that trade with each other closely are less likely to engage in a conflict between each other (e.g., Oneal and Russett, 1999; Gartzke, Li and Boehmer, 2001). However, the trade interdependence is also possible to increase the likelihood conflicts.<sup>24</sup> The bilateral trade data is acquired from the Direction of Trade Statistics.<sup>25</sup> Since the DOTS has quarterly numbers of trade flows for China and other countries, we do not have further convergence for the variable. Furthermore, the bilateral trade numbers between China and Taiwan are missing in the DOTS. We acquire the Cross-Strait trade flows at Bureau of

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<sup>22</sup>At <https://www.sipri.org/databases/milex>.

<sup>23</sup>For instance in Barbieri and Schneider, 1999; Xiang, 2010.

<sup>24</sup>See discussions on the revised conflict-trade relations in Barbieri, 1996; Barbieri and Levy, 1999.

<sup>25</sup>At <http://data.imf.org/?sk=9D6028D4-F14A-464C-A2F2-59B2CD424B85>.

Foreign Trade, ROC.<sup>26</sup> They provide annual data from 1994 to 2013 and monthly data from 2014 and 2015. Thus, we convert the trade flows from annual/monthly to quarterly data by the consistent method with the real GDP growth and inflation. Lastly, we lag all independent variable by a quarter to avoid potential endogenous problems.

### 5.1.3 Baseline Model at the Country Level

In this section, we present empirical results on the country level with four measures of each policy option, the domestic repression and the external aggression respectively, for China to secure its regime stability. Compared to the analysis in the event level, we have systematic measures for threats to China's regime. In Table 2, we have China's domestic repression as the dependent variable. For the dependent variables in the model 2 (Count, all) and 4 (Count, NV) being the count models, we have the negative binomial regression for these two and the OLS for the others.<sup>27</sup> Since there is no variance between each dyad on China's domestic repression, the unit of the analysis in Table 2 is data in each quarter instead of country-year dyad. To ensure the robustness of our results, we include the quarterly fixed effect and robust standard errors. In addition, we have the Fisher-type test for each variables in both Table and reject the null hypothesis at 1% that all panels contain unit roots for all variables.

In the domestic level, as expected, we find that the higher level of domestic unrests is associated with a higher possibility for China to use repression options, controlling for other covariates. These results are robust among all measures of

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<sup>26</sup>At <https://cus93.trade.gov.tw/?menuURL=FSC3000F>.

<sup>27</sup>In both model 2 and 4 in the Table 2 and Table 3, the likelihood ratio test of  $\alpha$  are strongly rejects the null hypothesis of no overdispersion for the Poisson regression model.

**Table 2: Domestic Repression as an Option**

	Scale,all	Count,all	Scale,NV	Count,NV
	(1)	(2)	(3)	(4)
Real GDP	45.443 (836.469)	.173 (.447)	45.443 (836.469)	.259 (.497)
Inflation	70.403*** (18.701)	.046*** (.013)	70.403*** (18.701)	.087*** (.014)
Domestic Unrests(scale,all)	1.448*** (.209)			
Domestic Unrests(count,all)		.006*** (.001)		
Domestic Unrests(scale,NV)			1.448*** (.209)	
Domestic Unrests(count,NV)				.008*** (.002)
Cons	966.039*** (246.415)	5.123*** (.161)	966.039*** (246.415)	4.928*** (.170)
Fixed Quarter	Yes	Yes	Yes	Yes
N	80	80	80	79

Note: Robust standard errors are in parentheses.

\* $p < .10$ , \*\* $p < .05$ , \*\*\* $p < .01$ .

We have OLS for scale models (1,3) and negative binomial regression for count models (2, 4).

events in all models. *Inflation* has positive significance to uses of domestic repression in China: when it becomes more difficult to the daily living, there will be more repression from China's government to its people. *Real GDP* is insignificant and show mixed results among different measures of conflicts. One possible explanation is that it takes longer time for Chinese public to understand the bad economic situation reflected by the real GDP growth.<sup>28</sup> In other words, the gloomy economic measured by this variable will transfer the threat to China's government later than another measure. Overall, it is clear that domestic repression is a policy option for China to deal with threats to its regime insecurity.

Table 3 presents the results of China using external conflict as another policy option to deal with threats to its regime security with the country-year dyad as the unit of analysis. In contrast to the results in the Table 2, variables measuring bilateral relationships, including relative power ratio and trade salience, are both statistical significant at 1% across all models: if the neighboring country has

<sup>28</sup>The results of real GDP is positive and significance at 1% for all models if we lag the variable by two instead of only one quarter.



**Table 3: External Conflicts as an Option**

	Scale, all	Count, all	Scale,NV	Count,NV
	(1)	(2)	(3)	(4)
Real GDP	119.582 (77.814)	.313 (.468)	33.073 (44.395)	-.363 (.648)
Inflation	2.654 (4.415)	.028 (.024)	1.735 (2.354)	.032 (.032)
Domestic Unrests(scale, all)	-.048** (.023)			
Domestic Unrests(count, all)		.00009 (.0008)		
Domestic Unrests(scale,NV)			-.019 (.014)	
Domestic Unrests(count,NV)				-.00002 (.001)
Relative Power	-236.430*** (88.358)	-.690 (.666)	-87.812* (53.318)	-1.347* (.812)
Trade Salience	2357.809** (973.541)	16.958*** (3.676)	1054.058* (581.177)	15.102*** (4.632)
Cons	132.698** (66.819)	3.277*** (.239)	22.060 (40.878)	1.559*** (.402)
Quarter Fixed Effect	Yes	Yes	Yes	Yes
Country Fixed Effect	Yes	Yes	Yes	Yes
N	599	599	599	593

Note: Robust standard errors are in parentheses.

\* $p < .10$ , \*\* $p < .05$ , \*\*\* $p < .01$ .

We have OLS for scale models (1,3) and negative binomial regression for count models (2, 4).

larger power difference with China, China is more likely to initiated to it. The positive coefficient of trade salience posits that the probability for China to launch conflicts is higher with those having trade dependence with China. Given that we measure the trade salience with Barbieri's definition, we suspect this is the reason to explain the positive direct between trade and conflicts. Furthermore, we find no significant results among all measures of regime insecurity for all models.<sup>29</sup> With the robustness check over time series issues, time and panel fixed effects, the diversionary hypothesis is unable to stand on the China initiated external conflicts.

## 5.2 Testing the Substitutability between Policies

As our second hypothesis indicated, there is a substitutability between policies that the use of foreign aggressions increases when the domestic repression decrease.

<sup>29</sup>The only exception is the domestic unrest in the model 1.

The model design for dependent variables and regression model selection is similar to those in Table 3. Instead of focusing on the effect of the domestic instability to China initiated conflicts, we have the use of domestic repressions from China as the key independent in order to identity the proposed substitution effect between two options. We also include two control variables, trade salience and relative power, to measure China's external cost of initiated external conflicts.

**Table 4: Testing the Substitutability between Policies**

	Scale, all	Count, all	Scale,NV	Count,NV
	(1)	(2)	(3)	(4)
Domestic Repress(scale, all)	-0.015** (.007)			
Domestic Repress(count, all)		-.001** (.0005)		
Domestic Repress(scale,NV)			-.005 (.003)	
Domestic Repress(count,NV)				-.0005 (.0007)
Relative Power	-274.635*** (62.825)	-4.115*** (.925)	-92.077*** (32.882)	-3.358*** (.942)
Trade Salience	2081.573*** (371.070)	21.575*** (1.674)	864.922*** (225.735)	22.244*** (1.964)
Cons	-18.204 (22.215)	1.585*** (.345)	-12.308 (12.300)	-.007 (.477)
Quarter Fixed Effect	Yes	Yes	Yes	Yes
N	623	623	623	623

Robust standard errors are in parentheses.

\* $p < .10$ , \*\* $p < .05$ , \*\*\* $p < .01$ .

We have OLS for scale models (1,3) and negative binomial regression for count models (2, 4).

The negative signs in all models in Table 4 confirm our theoretical expectation with the hypothesis on relations between two policy options. The increase of each policy option negatively responds to the other in all models, which have a different measure of conflicts. Put differently, the decreasing marginal effect of repression will lead to more external conflicts initiated by China. However, we have statistical significant at 5% for model 1 and 2, which includes all types of conflicts, but not for model 3 and 4, whose measures of conflicts are limited to material actions. In other words, the substitution relationships between two policies options does not exist in material conflicts. Since our assumption to the substitution is China's government being able to choice, it is possible to explain the absent of policy

substitution on material (non-verbal) conflicts by arguing insufficient capability for the government to choose.

## 6 Conclusion

Based on our observation of China's behavior in maritime disputes, we propose a hypothesis that the true intention for China to initiate the maritime conflicts was not to wage war against Japan or other countries, but because it would be an effective strategy for China to avert on domestic pressure. Different from explaining China's aggressive behavior in those waters via external factors, this research suggests that initiating these disputes is one of China's tools to divert domestic attention for gloomy economic situations to external conflicts. The application of this policy tool alternates with another prominent policy tool, domestic repression. In other words, China could respond to threats to its regime stability by either domestic repression or foreign aggression to counter-parties involved in territorial disputes, and there is a substitution between these policy options as an autocratic country.

With the ICEWS data from 1995 to 2015, we have multiple empirical strategies to test the argument and the proposed substitutability relations between these options to China government: case studies at the conflict-event level, a series of generalized linear models at the country-dyad level, and a test of substitutability between Policies. The results of empirical testing is interesting to the diversionary hypothesis: the case study provide mixed results to the diversionary theory hypothesis but strongly rejected by the systematic measures of China's behaviors. China's government responds to domestic threats of regime stability by domestic repression but not external conflicts. Moreover, we identify strong negative significant correlation between domestic unrests and external conflicts over different

robustness checks. This way, we reject the diversionary theory hypothesis with the systematic measures of China's behaviors. In the test of two policy options, we confirm the substitution effect between external conflict and domestic repression measuring by all event categories.

The article extended Johnston (1998)'s study on China on the diversionary argument with the new event dataset in addition to MIDs. Moreover, we provide an argument on the substitutability between domestic repression and external aggression, which give a more sophisticated logic to bridge domestic politics and international conflicts.

## Part III

# Signaling, Trade, and Taiwan's Military Spending Puzzle

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<sup>1</sup>This is a co-authored paper with Prof. Jun Xiang.

### **Abstract**

Scholars have extensively debated how the rise of China will shape international security. Surprisingly, little attention has been devoted to Taiwan's counterintuitive defense spending. While confronting a rising Mainland China, Taiwan has been constantly cutting military spending since the early 1990s. We put forth an original argument to explain this puzzle. The significantly expanded trade with Mainland China makes the Taiwanese government more willing to cut defense spending to signal that Taiwan is not seeking independence. In addition, we conduct an empirical investigation at both aggregate and legislator levels. The aggregate level of analysis allows a comparative analysis of the competing arguments in one unified framework, and the legislator level of analysis identifies the causal mechanisms based directly on the actors making decisions on the defense budget. The results at both levels of analysis demonstrate that trade with Mainland China reduces Taiwan's defense spending.

# 1 Introduction

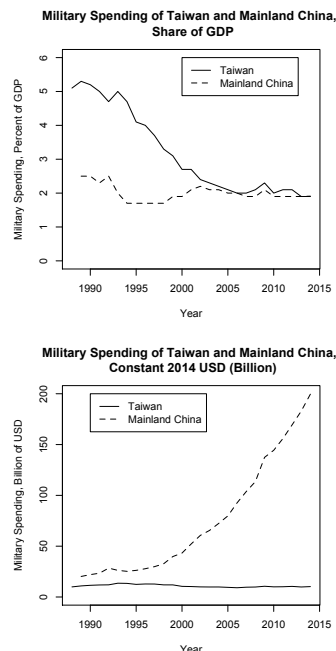
In recent years, scholars have extensively debated how China's rise will shape international security (e.g., Johnston 2003; Fravel 2010*b*; Mearsheimer 2010; Shambaugh 2011). Surprisingly, little attention has been devoted to Taiwan's counterintuitive military spending. While perceiving Mainland China as the primary security threat,<sup>2</sup> Taiwan has been constantly cutting military spending since the early 1990s. Based on the SIPRI Military Expenditure data, Figure 1 provides a clear illustration of the comparison between Taiwan and Mainland China's annual military expenditures. The top plot demonstrates that while Mainland China's military spending stayed around 2% of GDP since the late 1980s, Taiwan's defense budget as share of GDP plummeted from 5.1% in 1988 to 1.9% in 2014. When measured in constant 2014 USD shown in the bottom plot, Taiwan's spending trend was quite flat during this time period. In sharp contrast, Mainland China's military spending skyrocketed from 20.2 billion in 1989 to 199.7 billion in 2014. In short, Figure 1 poses a puzzle that contradicts the conventional wisdom in the military spending literature. Since Taiwan and Mainland China constitute a pair of rivals (e.g., Rider, Findley and Diehl 2011), it is predicted by the well-known rivalry and arms race argument that Taiwan's defense spending *positively* responds to Mainland China's spending. On the contrary, Figure 1 demonstrates that Taiwan contracts instead of expanding the defense budget in response to Mainland China's significantly inflated defense spending.

In this study, we put forth an original argument to explain Taiwan's military spending puzzle. This argument is two-fold. First, Taiwan's defense spending level signals to Mainland China the likelihood of Taiwan declaring independence. When

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<sup>2</sup>It is clearly stated in the Taiwan Ministry of National Defense Reports that Mainland China is Taiwan's primary security threat. Furthermore, Mainland China has been the imaginary enemy in Taiwan's largest annual military drill (i.e., the Han Kuang Exercise).

**Figure 1: Military Spending of Taiwan and Mainland China**



its defense spending is low, it is a costly signal to Mainland China that Taiwan's likelihood of declaring independence is low, which in turn implies a lower probability of cross-strait war. Second, the significantly expanded cross-strait trade provides a strong incentive for the Taiwanese government to avoid a cross-strait war, and the proposed signaling mechanism predicts that Taiwan cuts military spending to reduce the probability of war. In short, the expanded trade with Mainland China reduces Taiwan's military spending through the signaling mechanism.

Furthermore, we conduct an aggregate level and a legislator level analyses to empirically assess the proposed argument. As the conventional approach that uses Taiwan's annual military spending as the dependent variable, the aggregate level of analysis allows a comparative analysis of the competing arguments from



the military spending literature in one unified framework. The legislator level of analysis is a rather innovative approach that examines Taiwanese legislators' preferences on defense spending, and argues that factors contributing to legislators' anti-military spending preferences will increase the likelihood of a defense budget cut. This approach identifies the causal mechanisms based directly on the actors making decisions on the defense budget, and thereby opening the "black box" of decision-making at the aggregate level. Based on these two distinct and complementary analyses, all findings demonstrate that trade with Mainland China reduces Taiwan's defense spending.

In addition to contributing to the military spending literature, this study sheds light on several important debates in international security. First, since Taiwan falls within Mainland China's core national interests and is vital to the stability of U.S.-China relations, our analysis of Taiwan's military spending makes a significant contribution to the heated debate on the rise of China. Moreover, this study introduces a novel signaling mechanism—signaling type through varying military spending—to the fast-growing costly signaling literature. Finally, it demonstrates trade reduces military spending, which adds further evidence to the enduring debate on how economic interdependence affects international security.

## **2 Existing Arguments for Military Expenditures**

In the literature, little attention has been devoted to explaining Taiwan's military spending. One strand of studies uses military spending as an independent rather than dependent variable, and examines how military spending influences economic growth in Taiwan (e.g., Heo and DeRouen 1998). Another strand of lit-

erature argues that Taiwan's defense strategy is not to defeat but rather to deter and delay PLA's invasions, and as a result, Taiwan maintains a minimum "threshold" level of defense spending (e.g., Lin 1996; Wu 2014). However, this defense strategy argument cannot be utilized to answer why Taiwan has been cutting defense spending since the early 1990s, because it does not explain how the threshold level of defense spending responds to the changing levels of Mainland China's military expenditures during this time period.<sup>3</sup> In short, existing research does not offer an explanation for Taiwan's military spending puzzle. This study proposes and tests an innovative argument for Taiwan's military spending. Towards this goal, in the remaining of this section, we conduct a review of the literature on military spending to identify potential competing arguments. We examine four important explanations in the literature, which include rivalry and arms race, alliance, democracy, and wealth.

Arms race models are among the most important explanations of military spending. In a seminal work, Richardson (1960) proposes a simple two-country model to explain the logic of arms races. He shows that a state's defense spending level positively responds to its opponent state's military spending level, and when certain conditions are met, an arms race arises. His two-country model demonstrates a good prediction of the arms race of 1909-1914. Other scholars have proposed to use rivalry as an alternative conceptualization of arms race for conflict studies (e.g., Diehl and Crescenzi 1998; Diehl and Goertz 2001). Generally, rivalry consists of "spatial consistency," "duration," and "militarized competitiveness" (Diehl and Goertz 2001, 19). In other words, rivalry is a relation between at least two states that are involved in militarized competition or arms race for

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<sup>3</sup>Moreover, this argument is challenged by the Taiwan National Security Survey data that shows between 2005 and 2015, about 80% of the Taiwanese voters view Taiwan's defense spending to be insufficient.

a certain time period. Many studies have empirically investigated how rivalry affects military spending. Williams and McGinnis (1992) use a time series model to examine the defense expenditures of the U.S. and the Soviet Union during the Cold War period. They show that “a shared dynamic structure of the rivalry system” increases both states’ defense budgets (91). Based on a cross-sectional and time-series analysis that includes all states from 1886 to 1989, Goldsmith (2003) finds a positive effect of enduring rivalry on defense spending.

Another important explanation of military spending is joining alliances. A state can strengthen its military power internally by increasing defense spending or externally through forming alliances. Trade-offs exist between these two different methods. For example, Allen and DiGiuseppe (2013) examine this trade-off by analyzing a country’s access to financial credit. Based on an analysis covering the years from 1817 to 2002, they show that states with “debt crises, high debt burdens, or poor credit ratings” are more likely to join alliances (647). In addition, scholars have analyzed how allies’ military expenditures affect a state’s defense spending. Hill (1978) argues that when a state has a higher commitment to allies or is involved in Cold War alliances, it is likely to spend more on the military. He conducts an empirical test of 109 countries in 1965, and shows that compared to other alliances, NATO and Warsaw Pack states on average spend more on defense. In a reexamination of the free-ride within alliances argument, Gates and Terasawa (1992) propose that defense spending generates both “public goods” and “private benefits.” Based on a joint production model, deterrence is a pure public good while protective, and mixed weapons provide some private benefits. Furthermore, their commitment-based model suggests that fully committed resources are public goods, and as the level of commitment reduces, private benefits increase. It is expected that an increase in private benefits reduces the free-rider problem and

raises member states' defense expenditures.

It is generally agreed that due to a keener competition for resources among different interest groups, democracies tend to spend less on the military. Russett and Oneal (2001) argue that political leaders in democracies are strongly influenced by domestic interest groups. Since the increasing economic interdependence strengthens the bargaining power of pro-trade interest groups, political leaders are likely to allocate more resources to non-military sectors. As an illustration, they show that Brazil and Chile end the arms race with Argentina after these two countries become democracies in 1980s. Russett (1990) proposes that in a democratic country such as the United States, public opinion is likely to have an effect on the government's defense budget. He shows that during the period from the post-WWII to the late 1980s, when the public has an anti-defense spending preference, the U.S. Congress responds by a cut in the defense budget. A large number of studies have empirically investigated whether democracy reduces military spending in a global setting. For example, based on a sample from 1816 to 1997, Fordham and Walker (2005) demonstrate that democratic states are likely to spend less on their militaries. Goldsmith (2007) hypothesizes that democracies spend less on defense during peace time but more during war time. He conducts several regression analyses covering the years from 1885 to 1997, and finds strong empirical evidence to support his hypothesis. Furthermore, he empirically identifies that "competitive political environment rather than institutional factors" explains these findings (189).

Finally, scholars cite wealth or economic growth as an explanation for military spending. A number of studies argue that faster economic growth leads to a higher level of defense spending. Hewitt (1992) investigates the determinants of

military spending for 125 countries covering the years from 1972 to 1988. Based on a public choice model designed to understand leaders' choices between military spending and other forms of government spending, his study shows that defense spending positively responds to both GDP and GDP growth. Furthermore, his analysis demonstrates that indebted countries reduce defense spending over time. Rasler and Thompson (2002) examine this relationship for Britain during 1831-1913 and 1950-1980. They find that economic growth, investment, and non-defense public expenditure all positively affect military spending during the post-war period. Goldsmith (2003) provides further evidence by demonstrating that defense spending increases in countries with growing economies but reduces in countries with economic recessions. On the other hand, some scholars suggest that economic growth has no or a negative effect on military spending. Both Smith (1977) and Benoit (1978) argue that economic growth exerts either no effect or at most a weak influence on military expenditures. Instead, they propose that external security threats are the driving force of military spending. Based on a sample of more than 130 countries from 1963 to 2000, Töngür, Hsu and Elveren (2015) show that real GDP growth has a negative effect on military spending (measured as percent of GDP).

### **3 Explaining Taiwan's Military Spending Puzzle**

#### **3.1 A Signaling-Based Theory**

In this study we propose an original explanation for Taiwan's military spending puzzle. It is based on a signaling argument that Taiwan's defense spending level signals to Mainland China the likelihood Taiwan will declare independence. When its defense spending is low (high), it is a costly signal to Mainland China that Tai-

wan's likelihood of declaring independence is low (high), which in turn implies a lower (higher) probability of cross-strait war. Utilizing this signaling mechanism, we offer a rationalist explanation for Taiwan's decision to cut defense spending. The significantly expanded cross-strait trade provides a strong incentive for the Taiwanese government to avoid a cross-strait war, and the proposed signaling argument predicts that Taiwan cuts military spending to reduce the probability of war. In short, the increasing trade with Mainland China reduces Taiwan's military spending through the signaling mechanism.

The proposed signaling argument is an application of the costly signaling theory. Introduced by Spence (1973) to examine signaling in labor markets, the costly signaling theory has found many important applications in international relations (e.g., Schultz 2001; Kydd 2005; Weeks 2008; Weiss 2014). Due to the prevalence of asymmetric information, it is often difficult to differentiate between different types of players in the analysis of international relations. In costly signaling models, a costly signal conveys useful information by separating different types in equilibrium. In our case, Taiwan's true intent, which is whether to keep status quo or to declare independence, is asymmetric information to Mainland China.<sup>4</sup> However, it is common knowledge that Mainland China prefers status quo to independence. Since Taiwan will be rewarded for keeping status quo, it has an incentive to pretend to be a status quo type when it is an independence type. Due to this asymmetric information and Taiwan's incentive to misrepresent, Mainland China cannot differentiate a status quo type from an independence type in the absence of costly signaling. In this study we propose a costly signaling mechanism arguing that Taiwan's defense spending level serves as a costly signal to inform

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<sup>4</sup>In theory, unification is a third possibility. However, when compared to status quo and independence, it is an unpopular alternative in Taiwan. Therefore, it is omitted from our analysis.

Mainland China of Taiwan's true intent.

Based on this signaling mechanism, when Taiwan's defense spending level is low (high), it is a costly signal to Mainland China that its likelihood of declaring independence is low (high). The essence of a costly signaling model is that when one type imitates the other type, they incur different costs (e.g., Spence 1973). In the proposed signaling mechanism, when compared to a status quo type, the cost of losing a war or the benefit of winning a war against Mainland China is higher for an independence type. Therefore, although a cut in military spending reduces Taiwan's probability of winning a war and thereby the expected payoff of war for both types, it incurs additional costs for an independence type. Due to these additional costs, an independence type will be less likely to imitate a status quo type. Put differently, when Taiwan cuts defense spending, it sends a costly signal to Mainland China that Taiwan is more likely to be a status quo type rather than an independence type. Since Mainland China prefers status quo to independence, the likelihood of a cross-strait war is significantly reduced in this case.

The proposed signaling mechanism provides a useful analytical framework to understand Taiwan's decisions on military spending. It predicts that the Taiwanese government increases or decreases defense spending in response to its varying willingness to signal (due to different types or incentives). Utilizing this signaling mechanism, we offer a rationalist explanation for Taiwan's decision to cut defense spending since the early 1990s. We argue that the significantly expanded cross-strait trade provides a strong incentive for the Taiwanese government to avoid a cross-strait war,<sup>5</sup> and the proposed signaling argument predicts that

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<sup>5</sup>It is well understood that trade with Mainland China is of critical importance to Taiwan's economy. For example, in the year 2012, exports accounted for two-thirds of Taiwan's GDP, and 40% of Taiwan's exports went to Mainland China and Hong Kong. See <http://www.mof.gov.tw/public/data/331814228923.pdf>.

Taiwan cuts military spending to reduce the probability of war. Based on the well-known opportunity costs argument (e.g., Polachek 1980; Oneal and Russett 1999; Polachek and Xiang 2010), since war disrupts trade, Taiwan is strongly motivated to avoid a war with Mainland China to maintain the benefits from trade. However, the trade relationship between Taiwan and Mainland China is highly asymmetric. While Mainland China is Taiwan's largest trade partner and Taiwan receives a significant surplus from the cross-strait trade, exports to Taiwan account for only a small percentage of Mainland China's total exports. As a result, the opportunity costs of cross-strait war are much less significant for Mainland China. In short, a growing cross-strait trade does not itself prevent a war, but rather Taiwan has to send a costly signal to decrease the probability of war.

Two clarifications are important here. First, our argument that trade reduces Taiwan's military spending is different than the opportunity costs argument. To be more explicit, the dependent variable is probability of war in the trade conflict literature, but our argument examines military spending. Although the opportunity costs argument constitutes an indispensable part of our reasoning, a full explanation of Taiwan's military spending puzzle requires that we utilize the proposed signaling mechanism. In short, the relationship between trade and military spending is an important yet under-researched topic, and this study provides an original argument of how trade affects military spending. Furthermore, a higher level of cross-strait trade implies more military spending cut. When the benefits from trade are significant enough, an independence type also acquires an incentive to signal. To differentiate itself from an independence type, a status quo type is expected to implement a larger defense spending cut.

In addition to explaining Taiwan's military spending puzzle, the proposed sig-



nalizing mechanism sheds light on the different defense spending policy preferences of parties in Taiwan. Between the two major Taiwanese parties—the Kuomintang (KMT) and the Democratic Progressive Party (DPP), although the true type of each party is private information, it is publicly known that the KMT is more pro-status quo while the DPP is more pro-independence. However, these two parties’ defense spending policy preferences are counterintuitive. Contrary to the expectation that the DPP is likely to be more pro-defense spending since it is more pro-independence and military spending is essential for fighting a war, the KMT is indeed more supportive of defense spending in Taiwan. The conventional wisdom cites the historical tie between the KMT and the military as an explanation.<sup>6</sup> Nonetheless, it cannot account for why the DPP does not adopt a more pro-defense spending policy to gain the support of the military.

Our signaling mechanism, on the other hand, offers an interesting and much more compelling explanation. When Mainland China receives identical signals from these two parties (i.e., same amounts of military spending cut), the DPP will be less (more) credible to be a status quo type (an independence type) than the KMT. Since Mainland China holds a “biased” belief, the DPP has to cut more defense spending to convince Mainland China that Taiwan is a status quo type instead of an independence type. Put differently, when the KMT rather than the DPP adopts a policy more supportive of military spending, it will be less likely to be interpreted by Mainland China as a signal for independence. The proposed explanation is in the same vein as the Nixon-goes-to-China argument, which proposes that “when President Richard Nixon said that peace with China was in U.S. interests, this was more credible than if the message had come from a leader with less obvious anticommunist credentials” (Schultz 2005, p. 4).

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<sup>6</sup>The KMT and the DPP were founded in 1919 and 1986, respectively. Between 1949 and 1987, the KMT was the only major political party in Taiwan under the Martial Law.

### 3.2 An Illustrative Case

As an illustration of the proposed argument, we examine the strategic interaction between Taiwan and Mainland China during the DPP leader Chen Shui-bian's presidency from the year 2000 to 2008. Based on this illustrative case, we demonstrate that Mainland China interprets an increase in Taiwan's military spending as a signal for independence, particularly when the DPP is in power, and that trade with Mainland China reduces Taiwan's defense spending.

The DPP leader Chen Shui-bian's presidency from 2000 to 2008 has been perceived by many as an era of heightened tendency for Taiwan to declare independence. One *The New York Times* article published in 2008 wrote that "Taiwan's departing president, Chen Shui-bian, has spent much of the last eight years baiting Beijing, talking about independence and pressing for international recognition. Beijing has been more than eager to take offense" (NYT March 26, 2008). Nonetheless, Taiwan's true type (i.e., independence or status quo) during this time period remained private information. Surveys have consistently shown that the majority of Taiwanese voters preferred the status quo to independence,<sup>7</sup> and as such, Chen Shui-bian assured the Taiwanese voters during his 2000 presidential campaign that "he would not push for Taiwan's formal independence from China" (Eckholm January 31, 2000).

In 2004, Chen Shui-bian proposed to the Taiwanese Congress a 610.8 billion NT dollars (i.e., 18.25 billion USD) special arms acquisition budget to purchase

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<sup>7</sup>Based on the Taiwan National Security Survey that covers the period from 2002 to 2015, on average more than 80% of the respondents preferred to maintain the status quo.

advanced weapons from the United States, and in this case his proposition was unambiguously taken by Mainland China as a strong signal that Taiwan was likely to seek independence. For example, Yuan Peng, a Chinese scholar affiliated with the Chinese Academy of Contemporary International Relations, pointed out that “the Taiwan authorities’ recent budget for arms procurement from the United States has exceeded 600bn new Taiwan dollars ... markedly speeding up the pace of seeking “independence” by force” (BBC August 7, 2004). In addition, it was emphasized that “Beijing is particularly agitated about the prospect of Taiwan importing advanced weapons with Chen at the helm because he has been a long-time proponent of Taiwanese independence” (Boese November 1, 2004). That is, as suggested by our proposed argument, Taiwan would more likely to be an independence type when a DPP leader proposed to increase defense spending.

In Taiwan, Chen’s arms procurement proposition provoked strong protests from the opposition parties, numerous civil organizations, and many Taiwanese voters. One central criticism warned that the proposed defense spending budget would escalate the tension across the strait and push Taiwan to the edge of war with Mainland China (e.g., Lu September 24, 2004; Lin September 26, 2004). In the event of the outbreak of war, the cross-strait trade would be disrupted and Taiwan had to forego the benefits of trade. It was demonstrated that Taiwan has considerably benefited from the cross-strait trade during this time period. The Taiwanese government adopted a new economic policy towards Mainland China, changing from “no haste, be patient” to “proactive liberalization with effective management” (BBC August 15, 2001), and as a result, the cross-strait trade has significantly expanded. When measured in current USD, Taiwan’s annual exports to Mainland China (including Hong Kong and Macau) increased from 37 billion in 2000 to 100 billion in 2008. When combined with imports from Mainland

China, the total cross-strait trade grew from 45.64 billion to 132.91 billion over this eight-year time period.<sup>8</sup> Furthermore, Mainland China replaced Japan to become Taiwan's largest trade partner in 2005. In short, Chen Shui-bian's arms procurement proposition could lead to a significant loss of the benefits of trade for Taiwan.

As a result of the strong domestic oppositions, the proposed arms acquisition budget was rejected by the Taiwanese Congress. Put differently, to protect the benefits of trade, Taiwan cut military spending to reduce the likelihood of being perceived as an independence type. Furthermore, the SIPRI military expenditure data demonstrated that when measured as share of GDP, Taiwan's annual defense spending decreased from 2.7% to 2.1% over Chen Shui-bian's eight-year presidency from 2000 to 2008. To sum up, the above case supports our argument that Taiwan's defense spending level signals to Mainland China of Taiwan's likelihood of seeking independence and the significantly expanded cross-strait trade reduces Taiwan's military spending.

## 4 Empirical Analysis

In this section, we empirically assess the proposed explanation of Taiwan's military spending puzzle. Towards this goal, we design our empirical investigation at both the aggregate level and the legislator level. The aggregate level of analysis employs Taiwan's annual military spending as the dependent variable, and is the conventional approach in the literature. It allows a comparative analysis of the competing arguments (i.e., trade, president's party affiliation, rivalry and

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<sup>8</sup>For trade data, see <http://web02.mof.gov.tw/njswww/WebProxy.aspx?sys=100&funid=defjspt2>.

arms race, alliance, democracy, wealth) in one unified framework. On the other hand, the legislator level of analysis uses an individual Taiwanese legislator's defense spending preference as the dependent variable. It is expected that factors contributing to legislators' anti- (pro-) military spending preferences will increase (decrease) the likelihood of a defense budget cut. The legislator level of analysis is a rather innovative approach that has been adopted by a small number of International Relations scholars to examine how constituent interests influence legislators' decisions in areas other than defense spending (e.g., Kleinberg and Fordham 2013). The main advantage is that it identifies the causal mechanisms based directly on the actors making decisions on the defense budget, and thereby opening the "black box" of decision-making at the aggregate level. In short, the proposed two levels of analysis make distinct and complementary contributions to explaining Taiwan's defense spending.

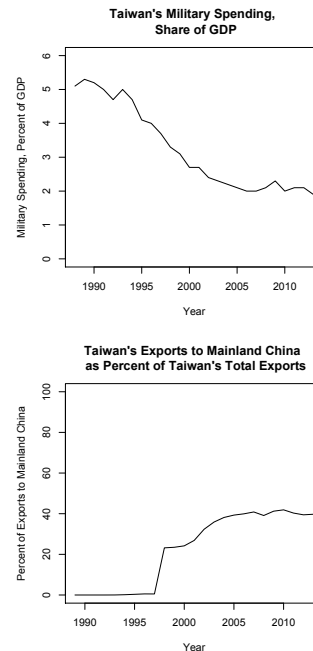
## 4.1 Analysis at the Aggregate Level

Since trade is the proposed explanation of Taiwan's military spending puzzle, it is useful to first present a visualization of the relationship between annual trade and military spending. The plots are given in Figure 2. In the figure, Taiwan's military spending and exports to Mainland China are plotted side by side: the top plot shows Taiwan's military spending as share of GDP and the bottom one illustrates Taiwan's exports to Mainland China as percent of total exports.<sup>9</sup> The horizontal axis indicates year in both plots, showing that both variables start from the late 1980s.<sup>10</sup> Figure 2 clearly demonstrates that during this time period, trade has

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<sup>9</sup>Here exports are used to measure Taiwan's benefits from the cross-strait trade since Taiwan is an export-oriented economy. In addition, Taiwan holds a large surplus from the cross-strait trade, suggesting Taiwan's exports dominate the cross-strait trade.

<sup>10</sup>More specifically, the SIPRI military spending data starts from 1988 and Taiwan's official trade with Mainland China begins in 1989.

**Figure 2: Taiwan's Military Spending and Exports to Mainland China**

been increasing whereas military spending has been declining. A closer scrutiny reveals that a significant jump in trade with Mainland China and a sharp drop in military spending occurred simultaneously in the late 1990s. In short, these two plots demonstrate a remarkable negative correlation between trade and military spending.<sup>11</sup>

Furthermore, the start of the cross-strait trade predates Taiwan's military spending cut. Due to the potential economic benefits arising from Mainland China's newly opened market, the Taiwanese government began to remove restrictions on the cross-strait trade in the early 1980s (e.g., Sutter 2002). As a first step, third-party exports through Hong Kong were introduced in 1985 (e.g., Fuller 2008). As a result of several important changes in policy, the cross-strait trade was officially launched in 1989. On the other hand, Taiwan's military spending

<sup>11</sup>The calculated correlation coefficient is equal to  $-0.96$ .

cut was initiated in the early 1990s. This discussion suggests that trade induces military spending cut is a plausible causal relationship.

The above bivariate analysis provides some preliminary evidence on the relationship between trade and military spending. Next, we perform a multivariate analysis to formally examine whether trade reduces Taiwan's military spending after having controlled for other explanations. In addition to our argument, this analysis tests several competing arguments from the literature, including rivalry and arms race, alliance, democracy, and wealth. As previously mentioned, the dependent variable for the aggregate level of analysis is Taiwan's annual military spending, and it is calculated as share of GDP. We employ two different data sources to measure military spending: the SIPRI Military Expenditure Database covering the years since 1988, and the statistics from the Directorate General of Budget, Accounting and Statistics in Taiwan.<sup>12</sup> A major difference between these two measures is that the former, but not the latter, includes foreign arms purchases, and as will be shown below, this distinction is crucial for our empirical investigation.

The independent variables employed for the aggregate level of analysis are *Trade*, *DPP President Dummy*, *Mainland China's Military Spending*, *U.S. Arms Sales*, *Social Welfare Spending*, and *Economic Growth*. To show the robustness of our results, we construct two measures of trade: *Trade, % of Total Trade*, and *Trade, % of GDP*. *Trade, % of Total Trade* is calculated as Taiwan's exports to Mainland China over Taiwan's total exports, and *Trade, % of GDP* is equal to Taiwan's exports to Mainland China over Taiwan's GDP.<sup>13</sup> Once again, exports

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<sup>12</sup>We do not use the military expenditure data from the Correlates of War dataset because its data is not available for the years since 2007.

<sup>13</sup>Exports from Taiwan to Hong Kong and Macau are added to Taiwan's exports to Mainland China after 1997 and 1999, respectively.

are used to measure Taiwan's benefits from the cross-strait trade since Taiwan is an export-oriented economy and holds a large surplus from the cross-strait trade. We obtain the trade data from the Bureau of Foreign Trade in Taiwan, and as previously discussed, the official trade data starts in 1989. As suggested by the proposed signaling argument, to reduce the likelihood of Taiwan being perceived as an independence type, the DPP will be less supportive of defense spending. To control for this effect, we create DPP President Dummy to indicate whether a DPP president is in power. Since Taiwan perceives Mainland China as the primary security threat, Mainland China's Military Spending is used to examine the rivalry and arms race argument. This variable is measured as Mainland China's annual defense spending as share of Mainland China's GDP, with the defense spending data from the SIPRI database covering the years since 1989. U.S. Arms Sales is employed to test the alliance argument. The United States is Taiwan's single most important ally,<sup>14</sup> and it provides military support through constant arms sales to Taiwan. U.S. Arms Sales is measured by U.S. arms sales as share of Taiwan's GDP, and the arms sales data is taken from the SIPRI Arms Transfers Database. Because the argument of democracy emphasizes the domestic competition for resources, in particular between military spending and social welfare, we utilize Social Welfare Spending to examine this argument. This variable is calculated by the percentage of government spending on education, health, pension, and unemployment, and we obtain the data from the Directorate General of Budget, Accounting and Statistics in Taiwan. Finally, the wealth argument is empirically tested using Economic Growth, a variable based on real GDP growth

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<sup>14</sup>Although the United States ended its formal alliance relationship with Taiwan when it established diplomatic relations with Mainland China in 1979, the United States has promised to continue to assist Taiwan's security. The Taiwan Relations Act (TRA) stipulates that the United States will provide necessary assistance to Taiwan to "maintain a sufficient self-defense capability" (Article 1 of Section 3) and should react to "any threat to the security or the social or economic system of the people on Taiwan" (Article 3 of Section 3). See [http://photos.state.gov/libraries/ait-taiwan/171414/ait-pages/tra\\_e.pdf](http://photos.state.gov/libraries/ait-taiwan/171414/ait-pages/tra_e.pdf).



with the data from the Directorate-General of Budget, Accounting and Statistics. To mitigate the potential endogeneity problem, all independent variables are lagged by one year. Summary statistics of all the variables are reported in Table 1.

**Table 1: Descriptive Statistics, the Aggregate Level**

	Number of Obs.	Mean	SD	Minimum	Maximum
Taiwan's MS, SIPRI	25	3.024	1.159	1.9	5.2
Taiwan's MS, Taiwanese Gov.	25	2.817	.909	1.965	4.582
Trade, % of Total Trade	25	22.699	18.095	0	41.895
Trade, % of GDP	25	12.633	10.896	0	26.867
DPP President Dummy	25	.32	.476	0	1
Mainland China's MS	25	2.004	.246	1.7	2.5
U.S. Arms Sales	25	.181	.197	0	.771
Social Welfare Spending	25	33.576	5.010	24.1	41.4
Economic Growth	25	5.273	2.966	-1.57	10.63

Our aggregate-level analysis covers the years from 1989 to 2014, and it is based on OLS regression. The results are presented in Table 1. In the table, we examine two different measures of the dependent variable: models 1 and 2 use the SIPRI data that includes foreign arms purchases, and models 3 and 4 are based on the Taiwanese government statistics excluding foreign arms purchases. The purpose of this research design is to have an appropriate test of the effect of U.S. Arms Sales. Since arms purchases from the United States are part of Taiwan's total defense budget, U.S. Arms Sales is omitted from the analysis in models 1 and 2. Instead, we include this variable in models 3 and 4 in which the dependent variable excludes U.S. arms sales. In addition, for each measure of the dependent variable, we employ two different measures of trade to show the robustness of our findings.

As clearly demonstrated in Table 2, the proposed argument that trade reduces Taiwan's military spending receives strong empirical support from all the model

**Table 2: Determinants of Taiwan's Military Spending, the Aggregate Level**

	SIPRI		Taiwanese Gov. Statistics	
	(1)	(2)	(3)	(4)
Trade, % of Total Trade	-0.046* (0.006)		-0.036* (0.009)	
Trade, % of GDP		-0.072* (0.015)		-0.061* (0.018)
DPP President Dummy	-0.347* (0.125)	-0.597* (0.149)	-0.252 (0.172)	-0.449* (0.171)
Mainland China's Military Spending	1.407* (0.238)	1.388* (0.322)	1.223* (0.378)	1.063* (0.440)
U.S. Arms Sales			-0.675 (0.540)	-0.963 (0.596)
Social Welfare Spending	-0.017 (0.021)	-0.006 (0.032)	-0.018 (0.030)	-0.007 (0.036)
Economic Growth	0.035 (0.019)	0.059* (0.024)	0.014 (0.027)	0.031 (0.028)
Constant	1.749* (0.583)	1.220 (0.813)	1.914 (1.151)	1.840 (1.241)
Number of Observations	25	25	25	25

Notes: Standard errors are in parentheses. \* $p < 0.05$ .

specifications. After having controlled for other important determinants of military spending, trade is negative and statistically significant. Substantively, when we increase Trade, % of Total Trade from 0% to 42%,<sup>15</sup> the predicted military spending decreases by 1.9% in model 1 and 1.5% in model 3. Likewise, when Trade, % of GDP increases from 0% to 27%,<sup>16</sup> military spending is expected to reduce by 1.9% in model 2 and 1.6% in model 4. These are substantively significant changes, since Taiwan's military spending during this time period varies by 3.3% from the SIPRI data and 2.6% from the Taiwanese government statistics. In short, trade is both statistically and substantively significant in explaining Taiwan's decisions on defense spending. Furthermore, DPP President Dummy shows a negative effect on the dependent variable, and is statistically significant for three out of the four models. When a DPP president is in power, Taiwan is expected to

<sup>15</sup>These are the minimum and maximum values for Trade, % of Total Trade in our data.

<sup>16</sup>Again, these are the minimum and maximum values for this variable.

reduce defense spending by an amount varying from 0.3% to 0.6% of GDP. These results of Trade and DPP President Dummy empirically demonstrate that our signaling-based argument provides a compelling explanation for Taiwan's military spending puzzle.

Surprisingly, based on our multivariate analysis, Taiwan's military spending positively responds to Mainland China's military spending. This variable is statistically significant from all the models in Table 2. Substantively, when Mainland China's military spending increases from 1.7% to 2.5%, which are the minimum and maximum values in the data, Taiwan's military spending increases by 1.1% in models 1 and 2, 1.0% in model 3, and 0.9% in model 4. This interesting finding revises the conclusion based on bivariate analysis, and suggests that the rivalry and arms race argument indeed holds for Taiwan and Mainland China. Furthermore, our multivariate analysis demonstrates it is essential to take into account trade and the other independent variables to uncover this positive effect of Mainland China's military spending. Nonetheless, Table 2 suggests that Trade, together with DPP President Dummy, is substantively more important than Mainland China's Military Spending in explaining Taiwan's military spending.

On the other hand, U.S. Arms Sales and Social Welfare Spending fail to show an effect on military spending. Here we employ U.S. arms sales to examine the U.S.-Taiwan alliance because other forms of military support such as military aid and military installations were not provided by the United States during this time period. The finding of this variable suggests that the alliance argument does not explain Taiwan's decisions on military spending.<sup>17</sup> Although the Taiwanese

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<sup>17</sup>In addition, the argument that Taiwan has an incentive to free-ride since the United States will provide necessary assistance to defend Taiwan is not well grounded. No significant changes have been made to the U.S.-Taiwan alliance since 1979, and therefore an unchanged alliance relationship cannot explain why Taiwan started to cut defense spending since the early 1990s

government has steadily increased the share of welfare spending since Taiwan transitioned to democracy in 1996, the empirical evidence from Table 2 demonstrates that the decrease in defense spending is not caused by the increase in social welfare spending. As a result, while seemingly a plausible explanation, the democracy argument does not contribute to the understanding of Taiwan's military spending. Lastly, Table 2 provides some weak evidence to support the wealth argument. Economic Growth shows positive coefficients, and out of the four model specifications, it is statistically significant in model 2. In short, the findings from Table 2 demonstrate that trade is the most important explanation of Taiwan's defense spending puzzle.

As a final note, the end of the Cold War does not constitute a cause for Taiwan's military spending cut. First, Mainland China has been Taiwan's primary security threat during both the Cold War and the post-Cold War periods. The rise of Mainland China in recent years implies an increased level of security threat to Taiwan when compared to the Cold War period. In addition, after the Cold War, the Clinton administration not only reduced U.S. military forces in East Asia, such as Japan and South Korea, but also requested more defense burden sharing from its East Asian allies (e.g., Brands 2008). As a result, the end of the Cold War does not generate a more secure environment or more U.S. military support for Taiwan.

## 4.2 Analysis at the Legislator Level

At the legislator level of analysis, we explain Taiwan's military spending budget by investigating the determinants of Taiwanese legislators' pro- or anti-defense spending preferences. The dependent variable in this analysis is a legislator's preference

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instead of the beginning of the U.S.-Taiwan alliance.

on defense spending, and is estimated by the widely applied ideal point estimation technique (e.g., Poole and Rosenthal 1997; Clinton, Jackman and Rivers 2004). This study identifies 50 defense expenditure bills voted between 2008 and 2014 in the Legislative Yuan in Taiwan, which include 29 bills on veteran affairs, 17 bills on military personnel, 2 bills on military budget, and 2 bills on other related issues.<sup>18</sup> These bills account for the majority of Taiwan’s defense budget,<sup>19</sup> and as a result, they provide sufficient information to estimate legislators’ preferences on military spending. Since Taiwan adopts a parallel voting system at the congressional level (e.g., Rich 2012; Huang, Wang and Lin 2013), we focus on the 73 districts whose legislators are elected by popular vote from single-member constituencies.<sup>20</sup> Based on these 73 districts, our sample identifies 113 legislators.<sup>21</sup> We employ the `MCMCirt1d` command from the R package `MCMCpack` to estimate legislators’ ideal points. For the estimated ideal points, the KMT legislator Lin Yu-fang’s positive ideal point is used to identify pro-defense spending preference.<sup>22</sup> Therefore, a larger (smaller) value of the dependent variable indicates a more (less) pro-defense spending position.

Since district-level trade data measuring Taiwan’s exports to Mainland China is not available, we propose to use district population working in manufacturing as a proxy. We argue it is a good proxy that captures a district’s degree of trade

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<sup>18</sup>We conduct a search based on combinations of the keywords (in traditional Chinese) “defense,” “military,” “budget,” and “expenditure” through the Library of Congress of Taiwan (accessed July 2014). Our sample period includes the 7th and the first half of the 8th Legislative Yuan.

<sup>19</sup>For example, in the year of 2014, the specified bills cover about 60% of Taiwan’s military spending budget. See <http://budget.gov.tw/budget/4814021900>.

<sup>20</sup>Put differently, 40 of the 113 districts are excluded from our sample of analysis, since district level information cannot be applied to estimate legislator preferences for these 40 districts.

<sup>21</sup>If a district elects a new legislator during the specified time period, both legislators are included in our sample and we estimate a separate ideal point for each legislator. Out of the 115 legislators from these 73 districts, two legislators did not vote on any of the specified bills and are omitted from our sample.

<sup>22</sup>Lin Yu-fang is a member of the Foreign and National Defense Committee, and he voted to support defense spending on all the bills in our sample.

connection with Mainland China. First, Taiwan is an export-oriented economy, and as such the majority of its manufactured goods are exported. For example, the Ministry of Economic Affairs in Taiwan shows that 66% of Taiwan's manufactured goods were exported in 2013.<sup>23</sup> In addition, Mainland China has been Taiwan's largest trading partner since 2005. In the same year of 2013, Mainland China accounted for nearly 40% of Taiwan's total exports.<sup>24</sup> Put together, in 2013 there was about a 25% chance that goods produced by a *random* worker employed in Taiwan's manufacturing industries were exported to Mainland China.<sup>25</sup> In other words, a significant number of Taiwan's manufacturing jobs hinge on the cross-strait trade, and it is expected that due to competition for employment opportunities, manufacturing workers in Taiwan would all value a stable trade relationship with Mainland China. In short, we argue that a district with more manufacturing employment is likely to develop stronger trade ties with Mainland China. Two variables are created to measure a district's level of manufacturing employment. *Trade, % of Employment* is equal to district population working in manufacturing over total district employment, and *Trade, % of Voters* is calculated as district manufacturing population over total district voters. All data are taken from the 2010 Population and Housing Census in Taiwan.

One might argue that a district's manufacturing population can also represent a proxy for other variables. Since manufacturing jobs tend to concentrate in urban instead of rural areas, a district's manufacturing population and urban-rural status are expected to be highly correlated. As a result, we include a variable *Urban Area* to control for the effect of urban-rural status on a legislator's defense

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<sup>23</sup>See data at [http://www.moea.gov.tw/Mns/dos/content/ContentLink.aspx?menu\\_id=9433](http://www.moea.gov.tw/Mns/dos/content/ContentLink.aspx?menu_id=9433).

<sup>24</sup>The 12.1% exports to Hong Kong were added in this case, because Hong Kong reunited with China in 1997. See data at <http://cus93.trade.gov.tw/FSCI/>.

<sup>25</sup>This probability is calculated as  $0.66 \times 0.4 = 0.26$ .

spending preference. The inclusion of this variable rules out the possibility that manufacturing population serves as a proxy for urban-rural status in our analysis. Based on the district population density data from the 2010 Population and Housing Census, Urban Area is coded one if a district's population density is at least 1,500 inhabitants per km square, and zero otherwise.<sup>26</sup> In addition, one argument proposes that if the demand for social welfare spending is higher among manufacturing workers, manufacturing population and social welfare spending in a district can be positively correlated. However, this argument is not well supported. First, the National Health Insurance provides equal access to healthcare for all Taiwanese citizens. In addition, free primary and secondary education are offered in Taiwan.<sup>27</sup> Finally, between manufacturing and non-manufacturing sectors, there are no significant variations in the government's provision of unemployment insurance and pension benefits. In short, in Taiwan manufacturing and non-manufacturing employees receive similar social welfare benefits, and therefore manufacturing population does not represent a proxy for social welfare spending.

To reiterate, the proposed signaling argument suggests that to reduce the likelihood of Taiwan being perceived as an independence type, the KMT instead of the DPP adopts a policy more supportive of defense spending. Therefore, we include a dichotomous variable *DPP Party Dummy* to indicate a legislator's party affiliation. This variable is coded one if a legislator is a member of the DPP, and zero for being a KMT member.<sup>28</sup> In addition, a legislator's gender and age are included in the analysis to control for the effects of personal attributes. *Gender*,

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<sup>26</sup>This cutoff value is based on OECD's definition of urban area used for Japan, Korea, Mexico, and member countries in Europe (OECD 2012, p. 26).

<sup>27</sup>Our legislator level of analysis includes an education variable to control for the effect of higher education on the dependent variable.

<sup>28</sup>Taiwan has a multi-party system where the KMT and the DPP are the two major parties holding the vast majority of seats in the Legislative Yuan. In our sample, there are three independent legislators and one legislator from the People First Party (PFP). These four legislators are assigned a missing value for this party variable.

*Legislator* is a dichotomous variable that equals one if a legislator is male, and zero otherwise. *Age, Legislator* is calculated as a legislator's median age when serving in the Legislator Yuan during the time period from 2008 to 2014. The data for these three variables are taken from the Legislative Yuan and the Citizen Congress Watch in Taiwan.

In addition to the district-level Trade and Urban Area variables, we include several other district-level variables to examine how a legislator's voting on defense spending is influenced by constituency preferences. Since 29 out of the 50 defense expenditure bills address veteran affairs, it is critically important to control for the number of veterans in each congressional district. Based on the data from the Veterans Affairs Council in Taiwan, we create a variable *Veterans*, which is equal to the number of veterans in each district over the total number of veterans in Taiwan. *Education* examines whether voters with higher education hold different preferences on defense spending. This variable is calculated as the proportion of district population with a bachelor's degree or higher. Furthermore, we investigate whether gender and age influence preferences on military spending. *Gender, District* is given by the percent of male population in a district, and *Age, District* divides district population into six age categories and calculates the percent of population within each category.<sup>29</sup> The calculations of these three variables are based on the population 15 years or older, and we obtain the data from the 2010 Population and Housing Census. As usual, summary statistics of the dependent variable and the independent variables are reported in Table 3.

At the legislator level, we conduct a cross-sectional analysis to examine how legislators' defense spending preferences are influenced by personal attributes and

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<sup>29</sup>These six age categories are 15-24, 25-34, 35-44, 45-54, 55-64, and 65 and above.



**Table A2: Descriptive Statistics, the Legislator Level**

	N	Mean	SD	Minimum	Maximum
<i>Legislator Attributes</i>					
Legislator Ideal Points	113	.225	1.241	-1.758	1.366
DPP Party Dummy	109	.358	.482	0	1
Gender, Legislator	113	.779	.417	0	1
Age, Legislator	113	52.128	8.348	30	78
<i>Constituency Preferences</i>					
Trade, % of Employment	113	26.858	12.924	4.065	51.770
Trade, % of Voters	113	14.990	7.496	2.457	30.793
Urban Area	113	.584	.495	0	1
Veterans	113	1.278	.648	.075	3.375
Education	113	35.399	11.185	15.982	69.903
Gender, District	113	50.310	5.085	43.327	82.921
Age (15-24), District	113	17.259	5.366	11.291	52.641
Age (25-34), District	113	20.538	2.669	15.763	25.584
Age (35-44), District	113	18.360	1.971	9.316	23.518
Age (45-54), District	113	18.092	1.801	8.001	20.863
Age (55-64), District	113	12.885	1.929	5.007	17.554
Age (65 and above), District	113	12.866	3.750	4.450	22.021

constituency preferences. Since the estimated ideal points are a continuous variable, we run an OLS regression and show the results in Table 4. In this table, two regression models are estimated based on the two measures of trade. In each model, the three personal attribute variables are listed at the top of the table, and the variables measuring constituency preferences occupy the bottom part. Once again, a larger (smaller) value of the dependent variable indicates a more (less) pro-defense spending position.

As shown in the table, DPP Party Dummy is both statistically and substantively significant. The negative coefficients indicate that when compared to a KMT legislator, a DPP legislator shows a less pro-military spending position. In addition, the marginal effect of this variable (i.e., the size of the coefficients) is 2.5, which is close in magnitude to the range of the estimated ideal points.<sup>30</sup> These results provide strong support for the proposed signaling argument that the DPP

<sup>30</sup>This range is equal to  $1.366 - (-1.758) = 3.124$ .

**Table 4: Determinants of Taiwan's Military Spending, the Legislator Level**

	(5)	(6)
<i>Legislator Attributes</i>		
DPP Party Dummy	-2.497* (0.065)	-2.494* (0.066)
Gender, Legislator	0.001 (0.075)	0.002 (0.076)
Age, Legislator	0.001 (0.004)	0.001 (0.004)
<i>Constituency Preferences</i>		
Trade, % of Employment	-0.016* (0.004)	
Trade, % of Voters		-0.026* (0.007)
Urban Area	0.116 (0.107)	0.117 (0.109)
Veterans	0.178* (0.057)	0.181* (0.057)
Education	-0.009 (0.006)	-0.008 (0.006)
Gender, District	-0.002 (0.019)	0.003 (0.019)
Age (25-34), District	0.057* (0.027)	0.057* (0.029)
Age (35-44), District	-0.045 (0.030)	-0.047 (0.030)
Age (45-54), District	0.052 (0.047)	0.062 (0.048)
Age (55-64), District	-0.098* (0.039)	-0.097* (0.040)
Age (65 and above), District	0.028 (0.025)	0.029 (0.026)
Constant	-1.279 (2.491)	-1.770 (2.531)
Number of Observations	109	109

Note: Standard errors are in parentheses. \* $p < 0.05$ .

adopts a policy less supportive of defense spending to signal Mainland China that Taiwan is unlikely to seek independence. After having controlled for the party effect, other legislator attributes do not contribute to explaining the dependent variable. Put differently, the results suggest that a legislator's gender or age exerts no effect on his or her position on defense spending.

When a district has a higher degree of trade connection with Mainland China, it will be more likely to elect an anti-defense spending legislator. The coefficients of both trade measures are negative and statistically significant. Furthermore, both trade variables are substantively significant. If a district increases manufacturing employment from 4% to 52%,<sup>31</sup> it is expected to elect a more anti-defense spending legislator with an ideal point 0.8 units lower than his or her predecessor. Similarly, when manufacturing population as the percent of voters increases from 2% to 31%,<sup>32</sup> its newly elected legislator is expected to possess an ideal point 0.8 units lower than his or her predecessor. Since the entire range of the dependent variable is 3.1 units, 0.8 units represent a substantively important effect. In short, based on the evidence from Taiwanese legislators, Table 2 demonstrates that trade with Mainland China reduces Taiwan's military spending.

One important point is worth mentioning. Since the finding of trade reducing military spending at the legislator level is based on a cross-sectional analysis, it cannot directly explain the temporal trend in Taiwan's defense spending budget. Nonetheless, this gap can be bridged by the strong temporal trend of trade shown in Figure 2, which demonstrates a nearly perfect negative correlation with the trend in Taiwan's defense spending. That is, as trade with Mainland China has become increasingly important since the early 1990s, more anti-defense spending legislators have been elected to cut military spending in Taiwan during this time period. To sum up, the legislator level of analysis reinforces the finding of trade from the aggregate level of analysis.

The remaining district-level variables measuring constituency preferences show

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<sup>31</sup>These are the minimum and the maximum values of Trade, % of Employment.

<sup>32</sup>Once again, these are the minimum and the maximum values of Trade, % of Voters.

several interesting results. When a district has more veterans, the elected legislator is likely to be more pro-defense spending. This finding is quite intuitive and consistent with the expectation. On the other hand, Table 4 suggests that a district's urban-rural status, education level, and gender composition do not influence its legislator's preference on military spending. All three variables fail to show statistical significance. Finally, the age variable deserves some scrutiny. In the table, the age group from 15 to 24 is omitted as the comparison category. The findings suggest that when compared to the other age groups (i.e., 15-24, 35-44, 45-54, and 65 and above), the age group 25-34 is more pro-military spending while the age group 55-64 is more anti-defense spending. These interesting findings provide arguably the first empirical evidence for the question of how age affects preferences on defense spending in Taiwan.

## 5 Conclusion

In this study, we propose a solution to an important and long-standing empirical puzzle. While confronting a rising Mainland China, Taiwan has been constantly cutting military spending since the early 1990s. This observation contradicts the conventional wisdom in the literature on military spending. We put forth an original argument to explain this puzzle. The expanded trade with Mainland China makes the Taiwanese government more willing to cut defense spending to signal that Taiwan is not seeking independence. In addition, we empirically assess the proposed argument at both the aggregate level and the legislator level. The aggregate level of analysis allows a comparative analysis of the competing arguments in one unified framework, and the legislator level of analysis opens the black box of decision-making by analyzing the actors making decisions on the defense

budget. We find that at the aggregate level, trade shows a nearly perfect negative correlation with Taiwan's defense spending and remains both statistically and substantively significant after controlling for the competing explanations. At the legislator level, when a district has a higher degree of trade connection with Mainland China, it is more likely to elect an anti-defense spending legislator. Furthermore, the results at both levels of analysis suggest that the DPP adopts a policy less supportive of defense spending to signal that Taiwan is not likely to seek independence.

## Part IV

# A Rusty but Provocative Knife?

## The Rationale behind China's

## Sanction Usage

### Abstract

After South Korea Terminal High Altitude Area Defense (THAAD) deployment in 2016, China has launched a series of "economic sanctions" to South Korea, affecting personal visiting, department stores, and Korean industries in China. The Global Daily also have called consumers to boycott Korean goods and hotels. Surprisingly, the Chinese Foreign Ministry has never positively announced or affirmed these "economic sanctions" to South Korea on the issue of THAAD. Put differently; the sanctions usages did not reveal strong resolution from Beijing government and its leaders on the issues. In the end, South Korea did not cancel its THAAD implementation because of China's sanctions.

In the paper, I explain China's rationale to impost puzzling economic sanctions, which has a weak resolution, to South Korea and Taiwan. As signaling theory argues, economic sanction with insufficient resolution, which is doomed to fail, is more likely to become a more provocative foreign policy than expected. With the case study of South Korea and Taiwan on China's sanctions, the paper proposes a bureaucratic competition theory to explain the rationale of sanction usage in China: these sanctions are for pleasing the CCP by the domestic agencies. The paper examines position changes of leaders in organizations, including those initiated sanctions and those in charging the disputes, in both cases to support the argument. Two alternative explanations are discussed in addition to the proposed argument.

# 1 Observation: China's Use of Economic Sanctions on Neighbor

During the territorial conflicts with the Philippines on the Shoal in the South China Sea since late 2012, China initiated a series of “economic sanctions” to pressure Manila to withdraw from the disputed area.<sup>1</sup> Measures of sanctions included additional inspections on Philippine imported agriculture products and “travel bans,” which limited amounts of tour groups to the Philippines. At the time, China is one major trade partners with the Philippines on agriculture goods and top-three sources of tourists to visit the Philippines every year.

In other places of East Asia, China has pressured its political will via the use of economic sanction. It has compelled Japan on territorial issues regarding the Senkaku Islands by the export limitation on rare earth elements (REEs) to Japan since September 2010. China is currently and was the most significant producer and exporter of REEs at the time and provided 82% of rare earth elements to the market consumption in Japan<sup>2</sup>.

China did not launch economic sanctions only to neighbors involving sovereignty issues like the cases illustrated above. Similar implications of economic sanction usages can be found in Sino-Korean and Cross-Strait relations, such as issues on the Terminal High Altitude Area Defense (THAAD) and the 1992 Consensus. China has set investment regulation to Lotte, a Korean company offering lands for

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<sup>1</sup>See “China's Coercive Economic Diplomacy: A New and Worrying Trend,” at <https://www.csis.org/analysis/chinas-coercive-economic-diplomacy-new-and-worrying-trend> for detail discussions on disputes between China and Philippine. Glaser also posits discussions on other cases of China's use of economic sanctions, such as Norway during the nomination of Liu Xiaobo for the 2010 Nobel Peace Prize.

<sup>2</sup>See “Rare Earth Elements: The Global Supply Chain,” at <https://stuff.mit.edu/afs/athena/course/12/12.000/www/m2016/pdf/R41347.pdf>.



THAAD deployment, in major Chinese cities to pressure the South Korean government. Lotte-owned shopping malls and supermarkets located in those cities was shut down owing to abruptly fire inspections.<sup>3</sup> Korean pop stars' events in China had also been canceled during the same period.<sup>4</sup>

In the case of Taiwan, numbers of Chinese tourists group has dropped dramatically after the DDP parties won the election in 2016 "because Beijing has restricted the issuance of travel permits to Taiwan."<sup>5</sup> This drop of Chinese tourist has brought "depression" to tourism industries in Taiwan. Some tourism industries asked the new president to accept the "1992 Consensus" to maintain Cross-Strait economic relations and benefits similar to the period of former President Ma.<sup>6</sup> The new Taiwan president was blamed for the drop in Chinese tourists because Beijing did not consider that she has recognized the 1992 Consensus in her inauguration and other official speeches.<sup>7</sup>

In addition to consequences of those sanctions against the opponent government, China government did not positively affirm any of those actions as "economic sanctions" to pressure governments in the Philippine, Japan, South Korea, and Taiwan in all cases illustrated above. Different from the United States and

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<sup>3</sup>See Cynthia Kim and Adam Jourdan, "One year after China's THAAD warning, South Korean business suffer," Sep 14, 2017, at <https://www.japantimes.co.jp/news/2017/09/14/asia-pacific/one-year-chinas-thaad-warning-south-korean-business-suffer/#.WeNvY2iCzBU>.

<sup>4</sup>See Ankit Panda, "China Brings More Economic Retaliation for THAAD Against South Korea," Dec. 12, 2016, at <http://thediplomat.com/2016/12/china-brings-more-economic-retaliation-for-thaad-against-south-korea/>.

<sup>5</sup>See Shelley Shan, "Minister sees drop in Chinese tourism," at <http://www.taipeitimes.com/News/taiwan/archives/2016/04/08/2003643476>.

<sup>6</sup>See South China Morning Post, Sep. 12, 2016, "Travel industry asks Taiwan's government to tackle fall in mainland Chinese tourists since President Tsai Ing-wen took office," at <http://www.scmp.com/news/china/policies-politics/article/2018534/travel-industry-asks-taiwans-government-tackle-fall>.

<sup>7</sup>See Nicola Smith, "China Is Using Tourism to Hit Taiwan Where It Really Hurts," Nov. 16, 2016, at <http://time.com/4574290/china-taiwan-tourism-tourists/>.

other countries usually initiated sanctions, which has a clear list of targets and treatments for sanction actions, Beijing seldom provided official statements or only refers to ambiguous wording for economic sanctions. On the other hand, most sanctions are implemented without threatening to use by local governments, customs, and travel offices. In other words, there is an asymmetry between the national political strategy and implementations of economic sanctions, which is a puzzle to the literature expectation. This project is expected to explain bureaucrat competition to the puzzle of China's sanction usage.

## 2 Puzzling: Economic Sanction as a Dragging Knife

Based those special characteristics, China's actual sanction usage is puzzling: first, it is can push China to further conflicts to fulfill its policy goal with the top priority. Scholars (i.e., Helms, 1999; Selden, 1999; Askari, 2003) usually consider the economic sanction as an option in between diplomatic talks and the use of force. Selden (1999) argues that sanctions seem like a policy option falling between diplomatic words and wars. Economic sanctions have lower costs than the use of force but stronger effects than diplomatic words. Moreover, Helms (1999) posits that economic sanctions are a nonviolent political option, allowing states to address international crises without resorting to the use of costly military force. Economic sanctions are possible to be an effective but lower-cost alternative foreign policy option than war and diplomatic negotiation.<sup>8</sup>

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<sup>8</sup>In the literature, scholars (i.e., Doxey, 1980; Hufbauer, Schott and Elliott, 1990; Drury, 1998; Drezner, 2000; Marinov, 2005) emphasize on conditions to effectiveness of economic sanctions. Doxey (1980) refers to the pressure of the sender country as the necessary condition for successful sanctions. On the other hand, Marinov (2005) turns to examine the effectiveness of sanctions by levels destabilization to leaders in the target country.

However, economic sanctions can be a more dangerous than foreign policy-makers' expectation. Using economic sanctions can sink the sender country into the crisis of conflict escalation. Lektzian and Sprecher (2007) posit that there is a significantly increased probability of the use of military force after a sanction occurs. Scholars (i.e., Morgan and Miers, 1999; Drezner, 2000; Lacy and Niou, 2004; Lektzian and Sprecher, 2007) argue that actions can have different probability of successfulness in different stages of implementations. Morgan and Miers (1999) show that the probability of successful use of economic coercion is greater at the threat stage than at the implementation stage. In other words, those sanctions initiated by China to its neighbor can tie China government hand to further conflicts or compelled opponents. Therefore, it is a puzzle to observe implementation economic sanctions set China into the risk of conflict escalation, instead of threatening to use.

In addition to the first consequence of China's sanction, the target of China's sanctions has less incentive to compel to China's will. The stronger the signal an action provided in the sanction, the higher likelihood of successful sanction and lower probability of conflicts escalations (e.g., Morgan and Schwebach 1997; Hart Jr 2000; Lektzian and Sprecher 2007). Lektzian and Sprecher (2007) note that the stronger the signal an actor provided in the sanction, the lower likelihood of conflicts escalation. This is again puzzling with China's sanction usage: not Beijing but local government and other agencies imposed the sanction. Moreover, China's Minister of Foreign Affairs seldom admit these practices as "economic sanctions" to pressure the Philippines, Japan, South Korea, and Taiwan. Put differently, China's economic sanctions sent a signal with weak determinants to its opponents in disputes. With this signal, opponents have less incentive to compel

to China's sanction usage so that China has a higher probability to resort to other foreign policy options or giving up on disputes.

At the end of those disputes between China and its neighbors, China did not escalate any conflicts into further militarized conflicts as literature expected. Neither was China willing to compel opponents in disputes. As a result, it is puzzling for China's economic sanction usage, which is a rusty but provocative knife, to pursue its top foreign policy goal in the dispute.

### **3 Research Question: Domestic Bureaucratic Competition**

In the recent years, we have witnessed a heated debate on China's rise, peaceful or not, in both media and academia. Although without a general agreement in the debate, scholars (e.g., Mearsheimer, 2001; Johnston, 2003; Xiang, Primiano and Huang, 2015) have provided plenty of analyses on how China will rise as a great power in the security dimension after economic reform. Xiang, Primiano and Huang (2015) examine China's peaceful rise focusing on China's threat to use force, the display of force, and the actual use of force. In conclusion, they show no empirical evidence points to more conflicts between China and other states.

To extend studies on the peaceful rise of China, economic sanctions can be another dimension than the use of force. As mentioned earlier, the economic sanction is a foreign policy option in between the diplomatic wording and the use of force. In contrast to the conventional theory on the rising power, which emphasizes on the use of force, the analysis on China's use of economic sanction can be a new and compromising direction to study the rise of China, which is yet currently missing

in the literature.

What's more, China might use more economic sanctions than the actual use of force since 1979. According to Militarized Interstate Disputes<sup>9</sup> from 1979 to 2010, China only involves 89 disputes with all countries, including Taiwan, in the world. This is less than 1.5% of disputes over all country-year dyads.<sup>10</sup> Instead of using force or threatening to use force, it is possible that China has expressed its muscles in the world with other means, such as economic sanctions. This way, it is crucial to study China's use of economic sanctions, which is currently missing in the literature of rising China.

To study China's use of economic sanctions, the paper proposes analysis from the domestic perspective, especially focusing bureaucratic competition theory. As Putnam (1988) noted, the political consideration of domestic factors is an indispensable condition to explain foreign politics. Domestic political is an essential but missing dimension to study China's foreign policy and its peaceful rising. As a result, I proposed bureaucratic competition theory (i.e., Graham and Philip, 1971) as the hypothesis to explain China's economic sanction usage: These sanctions are for pleasing the party leaders by domestic agencies. In addition to the research question, I introduce two alternative explanations in the following sections to strengthen explanatory power of the bureaucratic argument further.

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<sup>9</sup>See Palmer et al., 2015, at <http://cow.dss.ucdavis.edu/data-sets/MIDs>.

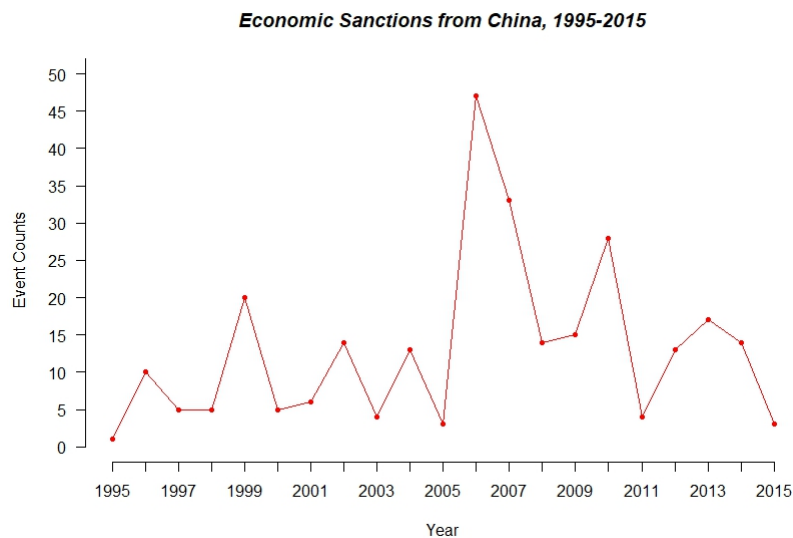
<sup>10</sup>89/6073=1.47.

## 4 Alternative Explanation

To strengthen explanatory power of the bureaucratic argument, I include the following alternative hypotheses from different levels of analysis into the discussion: (1) the rising China power and (2) the public choice approach. By adding both alternative hypotheses, the paper is expected to connect and contribute to the literature on rising China as well as those on economic sanctions, respectively.

### 4.1 China's Rising Power

The first one refers to international relations theory on the rise of China (i.e., Mearsheimer 2006, 2009; Kaplan 2011). Mearsheimer (2006) shows that China, as a rising power, will establish its hegemony in Asia and trigger tension between its neighboring countries (e.g., India, Japan, Russia). Moreover, a rising China is possible to pursue a foreign policy similar to that of "Imperial Germany, Imperial Japan, and Nazi Germany" (Mearsheimer, 2009, p. 252). Kaplan (2011) argues that China's behavior in the South China Sea as a rising regional power is similar to the United States in the Caribbean Sea in the late 19th centuries. Rising China's power is the main factor to explain its foreign policy behavior.



At first glance, stories of economic sanction illustrated in the beginning happened around the 2010s, especially after 2008.<sup>11</sup> The data on China's use of economic sanctions provide a result similar to this expectation. Figure 1 is the economic sanction initiated by China from 1995 to 2015.<sup>12</sup> There are more sanctions initiated by China in the latter years after 2005 than the early 1990s as China increases its national capability in the past decades. If rising China's power is a strong explanation, it is expected to observe a positive correlation with rising China's power (i.e., GDP, military expenditure, or CINC scores) with the use of economic sanctions.

## 4.2 Public Choice Theory

The second alternative hypothesis incorporates the public choice approach (e.g., Kaempfer and Lowenberg, 1989, 1992; Dorussen and Mo, 2001), which emphasizes

<sup>11</sup>In the existing research on China's rise, some scholars argue that the year 2008 is a turning point in the trajectory of China's rise (e.g., Buzan and Cox 2013; Shambaugh 2011; Zhao 2013).

<sup>12</sup>I set event based on CAMEO code 163, "Impose administrative sanctions", and 172, "Impose embargo, boycott, or sanctions, to generate these observations". Also, China is the initiated country for all cases.

on pressures from domestic interest groups to government decision makers on the use of economic sanctions. Kaempfer and Lowenberg (1989, 1992) introduce the public choice approach to study the domestic influence on economic sanctions, focusing on satisfying interest group in both sender and target countries. They (1989, p. 13) argue that “foreign policy trade restrictions are shaped largely by domestic interest group competition within the sanctioning country.” Put differently, different pressures from different domestic interest groups lead to different sanctions, such as import and export restrictions, and imposing agencies. Although this mechanism can be applied to both sender and target countries in the sanction, Dorussen and Mo (2001) differentiate strategies and preference between both sides in bargaining. They argue that the sender country prefer the strategy of audience cost that “governments can commit themselves to groups with a special interest in the policy of the target” (p. 420). Application of public choice approach emphasizing on domestic interest groups to China’s use of sanction can be a connect a signal-case study on China to more extensive literature on economic sanctions.<sup>13</sup>

To support this argument, it is expected to observe either evidents of direct lobbying from China’s domestic interest groups or the existed of close government-industry connection. Given that it is difficult to find these events, news on serious competition between South Korea and Taiwan on China’s domestic market those sanctions involved can be indirect evidence to support this alternative argument on the public choice theory.

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<sup>13</sup>Weiss (2013) show that nationalists protests during two US-China crises play the role of audience cost for China, an authoritarian regime, in negotiation.



## 5 Research Design

As illustrated earlier, China government seldom admit its practices of economic sanctions. To study China's usage of economic sanctions, the first challenge is data acquiring, especially the systematic one. The newspaper is probably the most accessible of resources for analysis. The Integrated Crisis Early Warning System (ICEWS) event data can create a brief picture of China's interaction with neighboring countries (See Figure in the previous section). However, considering the unit of analysis for the proposed argument in the project, the country-year data generated by the event data is not the best option. Instead, qualitative research method fits better with the data I expected to acquire. Since every sanction involved different government agencies, it is difficult to conduct cross sanctions a regression analysis. Therefore, I propose a case study design with multiple cases as a more appropriate option to answer the research question on domestic agency competition.

To support a proposed hypothesis, the paper examines position changes of leaders in organizations, including those initiated sanctions and those in charging the disputes, in both cases to support the argument of bureaucratic competition theory. For cases study, the paper first review activities related to economic sanction initiated from following major government institutions for each case study on South Korea and Taiwan. The former one includes State Administration of Press, Publication, Radio, Film, and Television of The People's Republic of China (SAPPRFT), Ministry of Commerce of the People's Republic of China; while the latter has the Taiwan Affairs Office and local Tourism Administration offices. After discussions on the role and actions of those institutes, I compare the change of leadership in those institutes for Taiwan and South Korea respectively. With

this comparison of the different character in sanctions for each government agency and its leadership changes, it is expected to identify the function of bureaucratic competition argument. In the following section, I first present discussions on two alternative explanations.

## 5.1 Test of Alternative Explanations

Before the primary analysis of the bureaucratic competition argument, I will first discuss two alternative hypothesis: China's rising power and the public choice argument. The former states that China as a newly rising power in the region will initiate more aggressive actions to its neighbors and the economic sanction is one of these actions. Thus, it is expected to China to impost more sanctions together with the rise of power. However, the paper finds positive coefficient but no statistical significance at 5% between China's uses of economic sanctions and different measures of China's national power by the binary negative binomial count model. The measures of China's national capability includes CINC scores, constant military spending, military expenditure by share of GDP, and constant GDP at Trillions USD.<sup>14</sup> Moreover, there is no statical significant of China's use of economic sanction after 2008.<sup>15</sup> This way, the rising power argument could not explain the distribution of China's economic sanctions: whether China resorted to more sanctions when its power grows; on the other hands, the country-year unit of analysis could not answer the asymmetric practice of China's sanctions between central and local government agencies.

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<sup>14</sup>The CINC scores are from the Correlates of War Projects; China's military spending in constant value and by the share of GDP is from the SIPRI Military Expenditure Database; China's constant GDP is from World Bank Data. The p-value for each measure of China's power with the negative binomial count model respectively are .089, .326, .175, and .351; the coefficients are 15.25, 3.38e-06, 196.016, and .082.

<sup>15</sup>The p-value is .878 for the count model with a dummy variable, which the year after 2008 is 1 and 0 for the previous years.

The second alternative hypothesis refers to the public choice argument, which focuses on the influence of domestic interest group on the government to use sanctions against their competitors. To support this argument, two possible pieces of information are required: first, direct influence or lobbying of local interest groups from the industry, which the sanction involved, to China's government; second, evidence of severe market competition between the target sector of the sanction and the local industry. Although the latter one is an indirect option to support these alternative explanations, it might be a possible proxy to test the argument in China, where the transparency of government lobbying is missing.

In the case of South Korea, the primary target of sanctions is the Lotte Group's supermarket, entertainment, and hotel investment. This way, the department store and retail industry should be the potential interest group and industry to benefit from the sanction. However, there is no direct evidence of China's interest groups lobbying or specific closer government-industry connection close to the time of economic sanctions. It is clear that there is no fact of lobbying from China's detail or department store industry to sanction South Korea and the Lotte Group. Furthermore, the incentive for domestic industry to sanction the Lotte Group is relatively low. According to the 2016 retail report, the Lotte Group was not on the list of the 2016 top hundred retail stores in China.<sup>16</sup> Little can other company gain interests from the sanction on Lotte's supermarket and mall. The cost of lobbying the government to sanction is relatively easy to outweigh the benefit of the additional market share.

In the case of Taiwan, the target of sanction is the industry of the group

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<sup>16</sup>See 2016 top hundred retail reports from China Chain Store & Franchise Association at <http://www.ccfa.org.cn/portal/cn/hangybzhuun.jsp?lt=31&pn=5&pg=1>.

tour to Taiwan, which is limited to individual travel agencies in each province. Compared to the sanction directly on the Lotte Group, the sanction to Taiwan damage the interest of those permitted travel agency in China and benefit other agencies without permissions. However, both direct or indirect evidence is missing to support the lobbying from the group with the potential to be benefited by the sanction. No evident of lobbying from the latter group or news on market competition between travel agencies right before the sanction. Second, there is no sign of national broad coalition and market competition between non-permitted travel agency to permitted one. Since the permission of group tour to Taiwan is initiated by the local government, only a national broad coalition against permitted travel agencies can explain the national broad sanction to Taiwan via the public choice argument. Hence, this alternative explanation cannot answer the use of sanction to Taiwan.

For insufficient evidence to support the public choice argument, the public choice argument based on the competition of domestic interest is hard to explain China's use of economic sanctions to either South Korea and Taiwan. To further explain the puzzle of China's economic, I propose two cases study on South Korea and Taiwan to review proposed bureaucratic competition theory in addition to both alternative hypothesis discussed above. With this case design, the paper is able to identify existence of bureaucratic competitions on the issue of sanctions within China.

## 6 Empirical Result: Case Study on South Korea

The sanction to South Korea started in early 2017, right after South Korea accepting the THAAD installation in July 2016. The measures of sanction covered Chinese group tour bans,<sup>17</sup> Lotte Group investment in China,<sup>18</sup> and voluntary boycotts of South Korean businesses and goods.<sup>19</sup> The People's Daily, the Global Times, and the Communist Youth League of China all severely condemned and urged to sanction South Korea. However, China's central government, especially the Ministry of Foreign Affairs, never official admit these actions as sanctions to South Korea, even if both news presses and the Youth League are with the CCP and have strong connections with China government. The sanction continued for the half year and ended in late October 2017 before South Korean President Moon Jae-in meet with Xi Jinping on the coming Asia-Pacific Economic Cooperation (APEC) Summit in Vietnam in early November.<sup>20</sup> In the end, South Korea did not withdraw the THAAD installation but promised that "deployment was not aimed at any third country and did not harm China's strategic security interests."

To apply to bureaucratic competition theory, I focus on leaders of three domestic agencies: Li Baoshan, the chief editor of People's Daily, Qin Yizhi and Gao Hucheng, the former minister of Ministry of Commerce. First, two domestic agencies have played a significant role during the sanction to South Korea. The People's Daily and the Global Times, a Chinese press under its auspices, both

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<sup>17</sup>See BBC, July 11, 2017, "South Korea tourism hit by China ban," at <http://www.bbc.com/news/business-40565119>.

<sup>18</sup>See Heekyong Yang and Hyunjoo Jin, June 6, 2017, "As missile row drags on, South Korea's Lotte still stymied in China" at <https://www.reuters.com/article/lotte-china/as-missile-row-drags-on-south-koreas-lotte-still-stymied-in-china-idUSL3N1JC3BA>.

<sup>19</sup>See Christopher Woody, Mar 20, 2017, "China is going after South Korea's wallet in their dispute over the THAAD missile system," at <http://www.businessinsider.com/china-south-korea-economic-boycott-protests-over-thaad-missile-system-2017-3>.

<sup>20</sup>See See Heekyong Yang and Hyunjoo Jin, October 31, 2017, "China, South Korea agree to mend ties after THAAD standoff," at <https://www.cnbc.com/2017/10/30/south-korea-china-agree-to-normalize-relations-after-thaad-fallout.html>.

condemned South Korea and Lotte Group for the THAAD installation, and they would pay the cost of this action. Moreover, the Global Times even asked Chinese people to voluntarily boycott Korean goods and companies as revenge for the THAAD.<sup>21</sup> In other words, they are one of the major forces in pushing domestic nationalism and economic sanctions during the dispute with South Korea. On the other hand, the Ministry of Commerce, which government agency should have been active during sanctions, presented little action to the sanction. Therefore, a comparison of the leaders shifted between these agencies could be a hint to the competition between domestic government agencies.

Li Baoshan, the chief editor of the People's Daily, was appointed to the current position in 2014. He was one of the alternate members of the Central Committee of the Communist Party of China during the 18th Party Congress with the order of 34th in the group. Alternative members of the Central Committee have been considered as candidates with prospective future in China. In the 19th Party Congress, Li's position has been changed to be in the Full Commission of the Central Commission for Discipline Inspection (CCDI).<sup>22</sup> This is the highest internal-control institute in the Communist Party of China (CPC). The Central Committee and the CCDI are instituted in different but crucial systems in the CPC. It is therefore difficult to compare the degree of personal promotion. Moreover, there is no considerable change in Li's position. For instance, he is not the member of the standing committee in the CCDI. Hence, it is fair to state that Li remains in the same position in the party and the government.

On the other hand, Gao Hucheng, the former Ministry of Commerce minister,

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<sup>21</sup>See news at <http://www.zaobao.com.sg/realtime/china/story20170228-730226>.

<sup>22</sup>See Xinhua, Oct. 22, 2017, at [http://news.xinhuanet.com/politics/19cpcnc/2017-10/24/c\\_1121848898.htm?baike](http://news.xinhuanet.com/politics/19cpcnc/2017-10/24/c_1121848898.htm?baike).

has a different story. He became the Ministry of Commerce minister in the 2013 but been removed from the ministry in early 2017. Zhong Shan, who worked under Xi in the Zhejiang from 2002 to 2007, takes over the position. This has been considered as a prelude for Xi to grip more power in the CPC during the 19th Party Congress.<sup>23</sup> After the 19th Party Congress, Gao is current one of the vice director of the Subcommittee of Hong Kong, Macao and Taiwan Compatriots and Overseas Chinese in the Chinese People's Political Consultative Conference (CPPCC). Concerning the personal promotion, it is clear that Gao has been demoted to the China government.

The People's Daily, a CPC newspaper, played a leading role in sanctioning South Korea on the THAAD. Its chief director maintains his position in the 19th Party Congress. On the other hand, the leader of the Ministry of Commerce, who should have taken actions to pressure South Korea, had little actions against the opponent in the dispute. Although there is no direct evidence connecting these personal promotions in China to sanctions on South Korea, this comparison of those China's government agencies still provides a hint to think about the effect of bureaucratic competition to the use of economic sanctions in China with the case of South Korea.

## 7 Empirical Result: a Case Study on Taiwan

The second case study to illustrate the effect of bureaucratic competition on China's uses of economic sanction via Taiwan's case since 2016. Right after the 2016 President Election in Taiwan, China began series of actions against the new

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<sup>23</sup>See Straitstimes, Feb. 25, 2017, at <http://www.straitstimes.com/asia/east-asia/china-appoints-new-economic-chiefs>.

government for not recognizing the “1992 Consensus,” which is the principle guideline for China and Taiwan government during the previous government from 2008 to 2016. Among different measures, the sanction of the group tour to Taiwan attract more public and media attentions.<sup>24</sup> For Taiwan, the China’s tourists was expected to bring 66 billion USD (200 billion TWD) revenue to Taiwan in 2015<sup>25</sup> The expected damage to Taiwan from the sanction is about 1.3 billion USD (40 billion TWD).<sup>26</sup> Moreover, three quarter of total tourists from China are group tourists, which required permitted travel agencies and government premonition to set up the tour.<sup>27</sup> Hence, the sanction on the tourist to Taiwan is significant to Taiwan and its government. In response, the protest in 2017 from those association of travel agents mentioned earlier regarding China’s tourists also supports the significant role of this sanction to Taiwan.

Similar to the sanction on the Lotte Group, China did not admit the drop of group tourists to Taiwan for the new government as a way of sanction. Although there is no official documentation on the travel ban to Taiwan, some travel agencies in Taiwan received the information and confirmed the sanction with anonymous route.<sup>28</sup> Officially, the president of Association for Relations Across the Taiwan Straits, the organization in China setting up for dealing with direct interaction with Taiwan, said that there is no such travel ban from China to Taiwan.<sup>29</sup> This

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<sup>24</sup>An example of other direct actions includes boycotting Taiwan’s participation in the International Civil Aviation Organization (ICAO) annual meeting in Montreal, which China did not take such action to the previous Ma government. See “Taiwan Snubbed by ICAO, Under Pressure from China,” at <https://www.voanews.com/a/taiwan-snubbed-icao-pressure-china/3522841.html>.

<sup>25</sup>See the news on effects of China’s sanction since 2016 at <https://news.tvbs.com.tw/local/653264>.

<sup>26</sup>See news on the effect of group tourists from China at <https://money.udn.com/money/story/5641/2898501>.

<sup>27</sup>See news on China’s travel ban to Taiwan, at [http://hk.on.cc/tw/bkn/cnt/news/20160617/bkntw-20160617113006486-0617\\_04011\\_001\\_cn.html](http://hk.on.cc/tw/bkn/cnt/news/20160617/bkntw-20160617113006486-0617_04011_001_cn.html).

<sup>28</sup>See news for the missing of the official statement on the travel ban at <https://tw.appledaily.com/headline/daily/20160123/37027875>.

<sup>29</sup>See news for the speech from the president of Association for Relations Across the



way, the resolution of China's sanction to Taiwan on tourists is unclear to Taiwan. Regarding the resolution of the sanction, Taiwan DDP government denied the existence of the sanction and of course did not compel to the China's demand on the 1992 Consensus.<sup>30</sup>

In the case of the sanction to Taiwan, the paper emphasizes on two sets of government agencies in China: China Tourism Administrations in each province as well as the Taiwan Affairs Office. The former set of government institutes include the central office in the central government and each province. As the sanction on the travel ban was directly imposed by offices in each province and the missing evidence of direct command from the office in the central government to the sanction, I, therefore, focus on leaders in each province instead of the one in the center. Given that there are 311 permitted travel agents across 31 provinces in China, I select top five offices in the provinces that have more permitted travel agents.<sup>31</sup> These offices includes Beijing Municipal Commission of Tourism Development, Tourism Administration of Guangdong Province, Tourism Administration of Zhejiang Province, Tourism Administration of Jiangsu Province, and Fujian Province Commission of Tourism Development. Each province has 29, 21, 18, 17, and 16 permitted travel agents respectively. Since the began of the sanction to Taiwan, I find that the leaders for those five offices in each province, including Song Yu, Zeng yingru, Xie Jijian, Qin Jingan, and Wu Xiande respectively, remain in their position. Qin Jingan for the Jiangsu office even got the promotion to be the member of the Jiangsu People's Congress. In sum, the leaders of the travel offices, which have engaged in the tourist's sanction to Taiwan, remain in their positions

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Taiwan Straits on the travel ban at <http://news.sina.com.cn/c/gat/2016-09-20/doc-ixvyqvyy6871065.shtml>.

<sup>30</sup>See news on how Taiwan government responded and its denial of the travel ban at <https://tw.appledaily.com/new/realtime/20160719/911101/>.

<sup>31</sup>The list of all permitted travel agents are available at Tourism Bureau, M.O.T.C Republic of China (Taiwan), <http://admin.taiwan.net.tw/public/public.aspx?no=163>

or being promoted.

In addition to those travel office in those provinces, the Taiwan Affairs Office is the comparison group to identify the bureaucratic competition argument. This office is the principal administrative agency in China responding to Taiwan issues, and the one should have acted aggressively to Taiwan new DDP government since 2016 but did not. Zhang Zhijun is the director of the office since 2013 and has a significant contribution to improving Cross-Strait relations with Taiwan Ma's government. Without other direct actions to pressure the new but prone independent Taiwan government, the Taiwan Affairs office only warned the dangerous of independent and stated China's position in Cross-Strait relationships.<sup>32</sup> Of course, these statements have little affects to change the Taiwan government position in Cross-Strait relations. In return, there are rumors on the further placement of Zhang in the party<sup>33</sup> for unable to deal with the Taiwan Tsai's government. The missing of his name in nomination of the 19th National Congress is another evident to observe.<sup>34</sup> One the one hand, the Taiwan Affairs Office should have pressured more on the Taiwan new government but had limited actions immediately; on the other hand, there are rumors on Zhang's future downgraded position in the government.<sup>35</sup>

By comparing changes on leaders between those five tourist offices in each province and the Taiwan Affairs Office, the leader of the latter government in-

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<sup>32</sup>See news for the statement from the Taiwan Affairs Office at <http://www.caixin.com/2016-05-20/100945996.html>.

<sup>33</sup>One example is that he would be forced to retire. See news on Xi and the party's comment to Zhang Zhijun at <http://www.ntdtv.com/xtr/gb/2016/12/28/a1304063.html>.

<sup>34</sup>See news on Zhang Zhijun during the 19th National Congress of the Communist Party of China at <http://www.epochtimes.com/gb/17/7/9/n9371745.htm>.

<sup>35</sup>Zhang is appointed to be the Vice Chairperson of the National People's Congress Foreign Affairs Committee in 2018 after the 13th National People's Congress. This is for sure an excellent promotion for Zhang, and he has been in the same position since 2013 in dealing with Cross-Strait relationships. However, the existence of those rumors should not be considered only as the conspiracy saying but at the minimum reflect the possible rules of personal promotion in China.

stitute is expected to be punished more than the formers. While lacking direct evidence, this indirect comparison yet give us a clue consider the possibility of bureaucratic competition to the use of economic sanctions in China in the case of Taiwan.

## 8 Conclusion

An economic sanction is an option in after diplomatic talks and before the use of force. A successful sanction is possible to save costs of militarized conflicts for the sender country. As a rising economic power, China has posted economic sanctions more than the 1980s, however, with a puzzling pattern. The central government of China seldom confirmed the use of sanctions. Furthermore, most sanctions were implemented by the local government or domestic agencies. This leads to an asymmetric practice of sanctions that is possible to decrease the probability for China to reach its policy goal at this stage. An asymmetric sanction can send a signal on China's weak resolution in disputes, which means its opponent has no incentive to compromise to China's sanctions. This way, China could only resort to the higher level of conflicts or compromise on the issue. Therefore, it is a puzzle why China has such asymmetric uses of economic sanction.

The paper proposes the bureaucratic competition as an explanation to China's use of economic sanction. Due to the principal-agency problem, domestic agencies are pleasing the party leaders by domestic agencies for their interests to stay in the office. Although the leaders' promotion in China is not the best observation of rewards from the CCP, it is fair to be the most convenient and observable factor to address the issue in addition to the size of budget or personnel for a certain

government agency. This way, China's use of economic sanctions is not the decision of China as a whole but results of domestic agencies within the government. What's more, I also include two alternative explanations, China's rising power, and public choice approach. This can not only strengthen my argument but also connect the paper to IR and economic sanctions literature.

While considering the problem of existing data on China's use of economic sanctions, I posit a case study design using sanctions to South Korea and Taiwan by comparing leaders' promotion in two Chinese domestic agencies. By the comparison of their role in the sanction and their latest promotion, I find out a hint to demonstrate the possibility of bureaucratic competition within China's sub-government agencies.

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