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M.Sc. Thesis in Development and International Relations

U.S.-China Relations, 2001-2015:

Economic Interdependence and the
Taiwan Issue

By Annika Tomzak

Development and International Relations, Chinese Area Studies

Submitted by: Annika Tomzak

Supervisor: Fuzuo Wu

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Abstract

Since the Chinese market opened up in the end of the 1970s and several economic reforms were started to be implemented, the state's economy and global influence grew significantly. As of today, China can be considered as one of the world's greatest emerging powers. The state's immense growth in power and influence leads to the prediction that China will be capable to challenge the hitherto prevailing status quo of U.S. predominance in the international world order. As China has the option to either undermine U.S. power or to complement it, the analysis of U.S-China relations is of great interest. Therefore the thesis investigates in the Sino-American relationship during the first 15 years of the 21st century with special focus on the economic interdependence of the two countries and how the Taiwan issue influences this relation.

The matter of economic interdependence between China and the U.S. is analysed by taking a closer look at U.S.-China trade from 2001 to 2015 as well as the respective foreign investment in each country of question. The Sino-American trade grew significantly during the last 15 years: The total trade of goods increased from \$80.48 billion in 2001 to \$520.75 billion in 2013, according to the National Bureau of Statistics of China (2012). Economic statistics between the U.S. and China differ greatly, which can be accounted to different methodologies to calculate data applied by each country. Therefore, U.S. official statistics by the United States Census Bureau (2015) compile different numbers, stating that the total trade of goods between China and the U.S. increased from \$121.46 billion in 2001 to \$562.16 billion in 2013. Next to the bilateral trade, bilateral investment of China and the U.S. grew as well. The U.S. is the 6th biggest investor in China, with a total investment of \$2.59 billion in 2015. The Chinese economy constitutes a profitable market for U.S. manufactures, because of lower labour costs compared to other Asian countries. With the relocation of U.S. companies from Japan or Taiwan to China, the U.S. contributes significantly to China's FDI.

In order to investigate the influence the Taiwan issue has on U.S.-China relations, the reactions of the U.S. and China towards Taiwan's endeavours to reach independence, as well as the position of the U.S. and China towards the continued arms deals between the U.S. and Taiwan, are subject of the analysis. Since the Second World War, U.S.-Taiwan relations had been close. Both U.S. presidential administrations of the 21st century stressed that the three Joint Communiqués, thus also the one-China principle, as well as the Taiwan Relations Act form the basis of U.S.-Taiwan relations. However, the relationship between the U.S. and

Taiwan were put to the test when Taiwan's then-president Chen Shui-bian pursued determined steps to lead Taiwan into independence from China. The Bush administration emphasised that it will not accept any unilateral endeavours to alter the status quo across the Strait. Nevertheless, arms sales between the U.S. and Taiwan continued steadily until today. After the inauguration of Taiwan's new president Ma Ying-jeou, relations across the strait started to improve, not least because of the implementation of several economic policies and agreements between Taiwan and China.

The continuation of arms sales between the U.S. and Taiwan throughout the years was justified by both U.S. governments by referring to the Taiwan Relations Act, which states U.S. commitment to support Taiwan to defend itself from outside threats. China, however, argues that the U.S. officially acknowledges the one-China principle and the PRC as China's sole legal government. Therefore, according to China, Taiwan is an internal Chinese affair, in which the U.S. is interfering in. Furthermore, China stresses that arms sales to Taiwan are not solely of defensive nature, although the Taiwan Relations Act states that the U.S. should only supply defensive weaponry to maximise the island's security.

Overall, Sino-American economic relations improved significantly in the course of the past 15 years, which also positively influenced political relations between the two countries. Additionally, improved economic relations across the strait proved to be beneficial for U.S.-China relations. Both countries were able to continue strengthening their bilateral ties without being increasingly apprehensive about how the respective relations with Taiwan might influence these. Nevertheless, controversial subjects between the U.S. and China remain.

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List of Abbreviation

APEC	Asian-Pacific Economy Cooperation
ARATS	Association for Relations Across the Strait
ASEAN	Association of Southeast Asian Nations
BEA	Bureau of Economic Analysis
BIT	Bilateral Investment Treaty
CIC	China Investment Corporation
C.I.F.	Cost, Insurance, and Freight
CRS	Congressional Research Service
C.V.	Customs Value
ECFA	Economic Cooperation Framework Agreement
F.A.S.	Freight Along Side
FDI	Foreign Direct Investment
F.O.B.	Free On Board
JCCT	Joint Commission on Commerce and Trade
M&A	Merger and Acquisition
MFA	Ministry of Foreign Affairs
MFN	Most Favoured Nation
MOFCOM	Ministry of Commerce
ODI	Overseas Direct Investment
OECD	Organisation of Economic Cooperation and Development
PPP	Purchasing Power Parity
PRC	People's Republic of China
RMB	Renminbi [¥]
ROC	The Republic of China
S&ED	Strategic and Economic Dialogue
SEF	Strait Exchange Foundation

TMD	Theatre Missile Defense
TRA	Taiwan Relations Act
U.S.	The United States of America
UN	United Nations
USD	U.S. Dollar [\$]
WTO	World Trade Organisation

1.0 Introduction

Since the early 20th century, the United States of America (U.S.) had been one of the world's greatest powers, with political, economic and military predominance over other states. However, after the death of Mao Zedong in 1976 and Deng Xiaoping's decision to open up the Chinese market, China's economy became stronger and the state can by now be considered the world's greatest emerging power (Hynes, 1998). The relationship between the U.S. and China will be of weighty interest in the course of the 21st century based on the prediction that China will be able to either undermine U.S. power in the nearer future, or to complement it.

After the formation of the People's Republic of China (PRC) in 1949, the relationship between the U.S. and China had been one of fluctuating nature. The incidents on the Tiananmen Square in 1989 as well as the end of the Cold War, led bilateral relations between China and the U.S. to tension up. As response to the Tiananmen crackdown in 1989, the George H. W. Bush administration imposed several sanctions on China. These sanctions, together with the collapse of the Soviet Union in 1991, ended the period of closer friendship between China and the U.S. of the 1980s.

Being aware of the growing importance of China, not only regionally in Asia but also internationally, the Clinton administration focused on strengthen bilateral relations with the PRC. Consequently, President Clinton and his Chinese counterpart Jiang Zemin signed a joint U.S.-China statement during a bilateral summit in 1997. This statement formed the basis for the declared efforts of setting up a 'constructive strategic partnership' between China and the U.S.

Major differences in ideologies, values and state systems proved to be great irritants in building up Sino-American relations throughout the years. Additionally, numerous major controversial subjects affect bilateral relations between the U.S. and China, such as the issue of Taiwan, the proliferation of weapons, China's relations with North Korea and general human rights standards in China. Especially the traditional bilateral ties between the U.S. and Taiwan, which were established in the 1940s, continue to negatively affect Sino-American relations nowadays.

However, bilateral relations not only revolve around political relations and discrepancies. After economic reforms in China, initiated by Deng Xiaoping in 1978, the Chinese market

opened up to international economic cooperation. Following this trend, bilateral relations in the areas of economy, trade and commerce between the U.S. and China turned out to become more and more interdependent. As of 2014, China is, after Canada, the largest trading partner of the U.S. According to the U.S. Bureau of Economic Analysis (BEA), exports of goods and services to China in 2014 (latest statistics available) were \$166.6 billion¹, whereas imports from China were \$482.7 billion (BEA, 2015, p. 1). The difference between exports and imports are mirrored in the increasing trade deficit of the U.S. with China. There are disagreements among economic analysts whether the trade deficit reflects an unbalanced or unfair Sino-American relationship, which is harming the U.S. economy, or whether the trade deficit is simply the result of global supply chains. China is often the last stage of production and (mostly) assembles the products before they are being exported (Morrison, 2015b, p. 3). Further, China holds an immense amount of U.S. Treasury securities - \$1.24 trillion in July 2015 (Morrison, 2015b, p. 13). U.S. economists fear that China's holdings of U.S. Treasury securities could be used as leverage over the U.S. foreign policy when it comes to discrepancies between the two states (Morrison, 2015b, p. 14).

The issue of Taiwan is of great importance when dealing with U.S.-China relations. The Republic of China (ROC), which was defeated by the communist forces in the Chinese civil war and fled to Taiwan in 1949, had been a long-term ally of the U.S. In times of the Cold War, but especially during the Korean War, protecting ROC was of great importance for the U.S., mainly in order to stop the spread of communism in Asia and to protect U.S. forces and interests in the Pacific. Furthermore, the location of the island in the Taiwan Strait displayed major logistic benefits in terms of trade and other economic interests for the U.S. The close relationship to Taiwan triggered complications for the U.S.-China relationship, even after the U.S. government withdrawn official recognition of the ROC as the sole legal government of China in 1979. Especially the continued arms sales from the U.S. to the island provoked criticism by the PRC, stressing the U.S. would interfere in internal affairs. Throughout the years, even though Taiwan lost its statehood, the island continued to be a close ally of the U.S. and its security was always of great significance. This position is mirrored, among others, by President Bush's statement that "the U.S. would do its utmost to help Taiwan defend itself" (Rabin, 2012, p. 4).

¹¹ These numbers only display the official U.S. statistics. It is noted that numbers change significantly between U.S. and Chinese official statistics. In the analysis both set of statistics are taken into consideration.

The main purpose of this thesis is to analyse U.S.-China relations, hence the basic characteristics of the current bilateral relationship under the influence of economic interdependence and the Taiwan issue. Therefore, the thesis concentrates on the U.S.-China relationship of the first 15 years of the 21st century, thus, during the Bush and Obama administrations. This decision was not solely made upon the fact that these are the two last presidential administrations of the U.S., but also due to the changed position of the U.S. in the Asian region after the terror attacks of 9/11. The U.S. foreign policy concentrated more on its anti-terror politics, which caused a loss of influence in Asia. This power vacuum was gladly filled by China, which made its peaceful rise in this region possible. Nevertheless, 9/11 also led to a positive shift in the U.S.-China relationship. China's support in the Afghanistan war strengthened the relationship between the two countries.

Compared to Bush's general unilateralist approach in foreign policies, the Obama administration emphasised its multilateralism and relied more on 'soft power' and cooperation, instead of 'hard power' and military engagement. The major shift in the U.S. foreign policy approach, together with the increased importance of establishing bilateral cooperation with China as a rising power, makes the analysis of Sino-American relations under the Bush and Obama administration highly interesting.

1.1 Research Questions

For the purpose of contributing to the already existing research on U.S.-China relations, this thesis aims at analysing the bilateral relationship from 2001 to 2015, under influence of the U.S.-Taiwan bond and the Sino-American economic interdependence. Therefore, the following three interlinked research questions will be central to the analysis:

What are the characteristics of U.S.-China relations in the first 15 years of the 21st century?

How have relations been influenced by economic interdependence and the Taiwan issue?

Why has economic interdependence between the U.S. and China been deepened in spite of the geopolitical competition over the Taiwan issue?

2.0 Methodology

The following section presents the techniques applied in the analysis, thus the procedures used to select and analyse information and sources in order to examine the research questions. By demonstrating how used data was generated and analysed, the reader is in the position to critically evaluate the validity and reliability of the thesis.

2.1 Choices of Theories

Even though social science provides numerous theoretical approaches, which are able to be applied on international relations, the relevant theories in this realm are the most dominant theories in international relations: Liberalism and Realism. It may sound contradicting combining two very different theories in one thesis. Liberalism, also called idealism, believes in the 'good', in changing relations and peace (Jackson & Sørensen, 2013, p. 101). Realism sees human nature as selfish, a constant struggle for power and security, often paired with the expectation of war (Dunne & Schmidt, 2014, p. 104). However, this thesis concentrates on two angles when aiming to analyse the relationship between the U.S. and China. On the one hand, there is the foremost geopolitical aspect, which is the relationship under influence of U.S.-Taiwan bonds. The most influential aspect here is the proliferation of weapons, hence, the U.S. arms sale to Taiwan in order to assure its security. It is a definite realist situation: Two great powers, in this case the U.S. and China, and their struggle for more security and power. Continuing this line of thought, it becomes evident that neorealism as well as Waltz's (1979; 1990) and Mearsheimer's (2001) assumptions of power distribution and accumulation is greatly applicable on the U.S.-China relationship. Both states, the world's greatest power and the world's greatest emerging power, struggle for the predominant role in the Asian region.

On the other hand, there is the aspect of economic interdependence in the analysis. Since the opening of the Chinese market in the late 1970s, trade and commercial relations between the U.S. and China flourished. By now, China is one of the major trading partners of the U.S. In turn, China is dependent on the U.S., as it is, for example, a key partner for China to acquire technology (Weidenbaum, 2000, p. 437). This economic interdependence is being best theorised with the neoliberal approach, thus, in an optimistic world in which international relations are subordinate to a network of interdependent relationships, in which norms as well as rules influence and, if needed, restrain the behaviour of states (Garrison, 2005, p. 2). The strands inside neoliberalism accounting best for interdependence between states are neoliberal institutionalism and complex interdependence. Both sub-groups of neoliberalism

emphasise the importance cooperation and trade relations have on the state's behaviour. Complex interdependence outlines the focus a state has on 'low politics', once interdependence is installed. It is linked with liberal institutionalism. This strand stresses that international organisations, such as the United Nations (UN) or the World Trade Organisation (WTO), but also international rules and norms, encourage cooperation between states and by that foster greater interdependence (Keohane, 1989, p. 2; Keohane & Nye, 1989, p. 3).

The greatest contradiction in combining those two schools of thoughts is their respective regard on the impact of international organisations. Liberalists see non-state actors as majorly important when it comes to international relations, whereas realists at most acknowledge the existence of international institutions in the international world order. However, due to their assumption that the nation state is the only actor in international relations that matters, they largely dismiss the importance non-state actors constitute in international politics and nation states' relations.

2.2 Types of Empirical Data

The research of this thesis falls within the scope of international political economy. The focus on the Taiwan issue and economic interdependence between the U.S. and China accounts for a geopolitical and economic aspect of the analysis.

The geopolitical aspect, thus the analysis of U.S.-China relations under the aspect of U.S. bonds with Taiwan, demands for merely qualitative data. This set of empirical data consists exclusively out of secondary sources, which includes predominantly academic articles, research papers, as well as news reports and publications from the two governments in question. Those sources will draw the mainly descriptive picture of the development of U.S.-China relations during the last 15 years. It is acknowledged that research conducted by individuals and governmental reports can contain subjective perceptions of facts reported. Nevertheless, in the realm of this thesis, possible subjectivity in sources is not deemed to be of a greater issue. This assertion can be justified by stressing that the obtained data is purely used as a source of fact-information. In this regard, subjectivity plays a minor role because the qualitative data 'only' delivers facts, as for example which agreements have been signed or which arms sales deal are intended. As long as the truth of those facts can be proofed, possible subjectivity of utilised sources does not matter.

The merely economic angle of the analysis, hence, the economic interdependence and trade and commercial relationship between the U.S. and China will be investigated with the help of

quantitative secondary data, in form of multiple statistical and numerical databases. Here, statistical comparisons of trade and economic cooperation constitute a helpful tool to point out the economic interdependence of the U.S. and China. In order to ensure the reliability of the data, official governmental data-banks, such as the U.S. International Trade Commission DataWeb, the United States Census Bureau, the National Bureau of Statistics of China or China's Ministry of Commerce are being utilised². Those extensive databases provide frequent updates and form the statistical basis for many political decisions and academic publications. Besides official statistics, certain qualitative sources, like annual reports or academic journal articles, are being included in the analysis of the economic interdependence. These are deemed to be useful to form the line of argumentation as well as weigh and prioritise the aspects that constitute a major role in the analysis.

2.3 Limitations

Even though the first research question lets suggest that the general characteristics of U.S.-China relations in the first 15 years of the 21st century are subject to the analysis, solely the bilateral economic relations and the Taiwan issue are central to the analysis of the Sino-American relationship. Therefore, other main issues such as the matter of cyber security or the South China Sea disputes are not subject of this analysis.

The decision to concentrate exclusively on the Bush and Obama administration stems from several considerations. On the one hand, the foreign policy towards China changed greatly from the Clinton to the Bush administration. Clinton sought to establish a constructive partnership with the PRC and improve bilateral relations in every aspect. The Bush administration strongly opposed Clinton's general policies and approached its presidential term with the 'ABC policy' – Anything But Clinton (Yu, 2009, p. 84). However, the U.S. foreign policy made a significant shift after the terror attack of 9/11, and bilateral relations between China and the Bush administration started to improve. The reason the Obama administration is of interest in this thesis, is the difference it shows in its overall political approach compared to the Bush administration. The U.S. foreign policy shifted from unilateralism to multilateralism, and from relying on 'hard power' to a merely concentration on 'soft power'. Moreover, during the two mentioned U.S. presidential administrations, China-Taiwan relations showed major fluctuations. The revisionist Taiwanese president Chen Shui-bian challenged cross-strait relations and risked military conflict in the region. His

² Please note that also a non-governmental database is consulted for the analysis of U.S.-China economic relations: the Rhodium Group, China Investment Monitor.

predecessor Ma Ying-jeou however, worked towards stronger interdependent cross-strait relations and eased the tensed situation between China and Taiwan.

2.4 Literature Review

The Sino-American relationship had been a vibrant topic since the establishment of the PRC in 1949. In recent years, many social scientists studied the bilateral relations and paid special emphasis on the U.S.-China relations under the influence of the Taiwan issue. In 2000, a bipartisan panel of national U.S. security experts stated in a report that the cross-strait relationship between Taiwan and China is “the most intractable and dangerous East-Asian flashpoint – and the one with the greatest potential for bringing the United States and China into confrontation in the near future” (RAND, 2000, p. 22).

Most researchers agree that improved economic relations between China and the U.S. as well as China and Taiwan have a positive effect on political and military relations across the strait, and that there is clear evidence that relations became more and more interdependent lately. Hickey and Zhou (2010) argue that “[t]he economic interdependence between the PRC and the U.S. as well as Taiwan has helped promote a reconciliation of longstanding political and military problems” (p.155). Furthermore, the two authors claim that the Taiwan issue is a core national interest for all three states involved and that a prediction of future proceedings is impossible. However, they state that “[a] peaceful solution of this issue will have a win-win-win consequence to this trio that is bound by shared economic and security interests” (p.156).

Furthermore, Kan and Morrison (2014) stress in a Congressional Research Service (CRS) report that cross-strait disputes and tensions have been reduced by increased interdependence between Taiwan and China, and promoted economic relations: “The resumption of the cross-strait dialogue resulted in even closer economic engagement between Taiwan and the PRC as well as a reduction of tension” (p.2).

Harvard professor Johnston (2013) emphasises that economic considerations should effect China’s political decision-making process: “China should avoid major conflict with the United States to concentrate on economic development; and building ‘new type major power relations’ based on the recognition that U.S.-China interdependence creates major costs for China resulting from any U.S. economic decline” (p. 36). Johnston clearly argues that China’s economic well-being is dependent on U.S. policies towards China which therefore also affects China’s policies towards Taiwan.

The analysis of U.S.-China relations with regards to Taiwan had been a popular topic among social scientists in the past decades. In fact, numerous academic research articles and books have been published, conducting either U.S.-China relations, China-Taiwan relations, U.S.-Taiwan relations, or even the triangular relationship of the states in question.³

However, while researching on the topic, it turned out to be difficult to find many contemporary contributions on this topic. Especially the impact of the Obama administration on U.S.-China relations under the influence of the Taiwan issue were barely examined in academic articles so far. Furthermore, interlinking economic relations with the political dispute on Taiwan was rarely considered in academic publications. Therefore, the contemporary aspect of this analysis, thus especially the examination of the Obama administration in Sino-American relations under the influence of the Taiwan issue, contributes to the already conducted research on this topic by covering the mentioned literature gap.

3.0 Theoretical Framework

In order to approach the research questions of this thesis, different international relation theories and the respective subgroups can be applied. As already elaborated upon in the Methodology, the two main theories of choice are neorealism and neoliberal institutionalism. This theoretical chapter introduces the chosen theories and their core assumptions. Furthermore, it presents specific strands in each theory relevant for the analysis of this thesis. By highlighting their respective core concepts the earlier argumentation of the choice of theories is underlined. During the analysis theoretical assumptions are picked up again to construct the line of argumentation.

3.1 Neorealism

The dominant school of thought in international relations and politics is the theory of realism (Dunne & Schmidt, 2014; Wohlforth, 2012). Scholars of political science, like Dunne and Schmidt (2014), claim that realism can be divided into different subgroups, with the most common division into classical realism and neorealism (also referred to as structural realism).

Opposed to classical realism, which puts the individual, statesmen and human nature, in the centre of international relations, neorealists concentrate on the structure of the system in

³ Examples of those publications are among others Guo & Guo (2010): *Thirty Years of China-U.S. Relations*, Lampton (2001) *Same Bed, Different Dreams: Managing U.S.-China Relations, 1989-2000*, and Cliff & Shlapak (2007): *U.S.-China Relations after Resolution of Taiwan's Status*

which international relations take place. According to Waltz (1990), the international structure develops due to states' interactions and at the same time, the structure restrains or impels the state from/to certain actions (Waltz, 1990, p. 29). One of the core concepts in realism that every realist strand agrees on is the assumption that the international world order is a system defined by anarchy in which the rational actor, here the nation state, acts independently. Waltz identifies the anarchical structure, being the ordering principle of the international system, as a general condition (Waltz, 1990, p. 36). Furthermore, Waltz stresses that, what he calls 'distribution of units' is another determinant defining the international system (Waltz, 1990, p. 29). The relative distribution of power, "the combined capability of a state" (Waltz, 1990, p. 36), is what determines international relations and should, therefore, be in the centre of political analyses. The way power is distributed among nation states, hence the number of existing great powers, shapes the international system. Therefore, "international structures vary with significant changes in the number of great powers" (Waltz, 1990, p. 29). Additionally, the distribution of power determines the place a nation state takes up in the hierarchical order in the international system. Assuming that, due to the amount of accumulated power, states are placed differently in the system, and that this placement determines the states' behaviour, Waltz attributes more importance to the concept of power than the idea of ideology or governmental form (Waltz, 1990, p. 29). Compared to this assumption, classical realists ascribe certain characteristics to states and statesmen, and focus on the behaviour and the outcomes which are linked to those characteristics (Waltz, 1990, p. 36). In Waltz's words: "[N]eorealists offer a theory that explains how structures affect behavior and outcomes" (Waltz, 1990, p. 37).

3.1.1 Waltz's 'defensive realism'

Within neorealism, there is a crucial differentiation between 'defensive' and 'offensive' realists. The discrepancies of the two strands revolve around the issue whether nation states are power or security 'maximizers'. Waltz, not only a predominant neorealist, but also the major representative for defensive realism, argues that states' main interest lies with security instead of power when situations become critical (Waltz, 1990, p. 36). Therefore, in defensive realism, states are seen as security 'maximizers'. Without security, the survival of the state cannot be assured, and without the guaranteed survival, states cannot "safely seek such other goals as tranquillity, profit, and power" (Waltz, 1979, p. 126). Waltz argues, that, if states solely seek to maximise their power, there would be no balancing in international world politics. In fact, if weaker state have the choice, they are most likely choosing to join

coalitions with other weaker states, because they feel threatened by stronger powers (Waltz, 1979, p. 127). If a state accumulates too much power, other states will increasingly fear for their survival. Thus, Waltz argues that states should be moderate in seeking power – he suggests an amount big enough to ensure their own security, but not too great, in order to avoid other states counterbalancing against them.

3.1.2 Mearsheimer's 'offensive realism'

In his work *The Tragedy of Great Power Politics*, Mearsheimer (2001) introduces a new realist strand. Mearsheimer's 'offensive realism' combines classical realist concepts with neorealist assumptions. As every realist theory agrees upon, the nation state is the only actor that matters in an international world dominated by anarchy. Offensive realism agrees with the classical realist assumption that states seek to maximise power. However, Mearsheimer does not attribute the accumulation of power to the human lust for power, but, corresponding to Waltz's neorealism, to the structure of the international system. Since states are constantly in doubt of other states' intentions, combined with the omnipresent threat of war, caused by the anarchical world order, maximising power is seen as the best way of ensuring national security. Mearsheimer points out that the concepts of blackmail and war are the main strategies in order to gain power (Mearsheimer, 2001, p. 13). Furthermore, Mearsheimer argues that states are prone to act aggressively towards each other, for the means of increasing the probability of their survival (Mearsheimer, 2001, pp. 3, 21). In a nutshell, he stresses that "the international system forces great powers to maximise their relative power because that is the optimal way to maximize their security. In other words, survival mandates aggressive behaviour" (Mearsheimer, 2001, p. 21). Following the thought of maximising power, the "ultimate aim [of states] is to be the hegemon" (Mearsheimer, 2001, p. 2). Mearsheimer identifies two strategies states pursue in order to maintain the balance of power when another state seeks hegemony: balancing and buck-passing. Balancing implies that a state itself accepts the task of deterring the alleged hegemon, whereas buck-passing suggests that the state, which is in fear for its survival, conveys the mission of deterring the hegemon to another state (Mearsheimer, 2001, p. 13).

3.2 Neoliberal Institutionalism

During the 1970s and 1980s, the increased significance of other actors besides the nation state challenged hitherto prevailing school of thoughts. Those actors, consisting of for example of transnational corporations or interest groups, outlined the need of certain amendments in the traditional liberal theory (Keohane & Nye, 1972). The renewed theory –

neoliberalism or neoliberal institutionalism – agreed in fact with essential core presumptions of neorealism: anarchy being the overall principle of the international system, in which states (Waltz also refers to those as ‘units’) interact with each other (Keohane, 1986, p. 166). However, where realists emphasise the importance of (military) power in order to maximise national interest (survival), neoliberals perceive that states, as rational actors, redefine their national interest due to interstate interactions and international regimes and norms (Nye, 1988, pp. 238-9).

Where (neo-)realism ‘only’ perceives the nation state as a determining factor in international relations, neoliberal institutionalism includes non-state actors, such as multinational corporations, transnational social movements, and international organisations (Keohane & Nye, 1989, p. 3), in their theory, stressing that those actors have their fair share in affecting international politics (Keohane & Nye, 1971, p. 330). Besides non-state actors, international institutions also encompass international regimes, a set of rules or procedures governing international relations (Keohane & Nye, 1989, p. 5). With the help of international institutions, which are promoting the flow of information among nation states, cooperation in the international system between sovereign states is possible even with anarchy as the organising principle. This cooperation usually encompasses ‘low politics’ such as economic relations and social affairs. Furthermore, international institutions help reducing distrust among nation states, because they foster the ability of states monitoring each other (Keohane, 1989, p. 2). Thereby, nation states can assure another state’s adherence to norms or the solidity of agreements and cooperation (Keohane, 1989, p. 2). This statement reflects the earlier assumption by Keohane (1984) that cooperation is not only dependent on mutual interest, thus having a potential gain from the cooperation, but also on the existence of international institutions (p.13). Nevertheless, even though an established cooperation among nation states might emphasise ‘low politics’ of economy and social affairs, liberal institutionalists do not extinguish the possibility of the use of military power or war, or as Keohane and Nye (1989) stress: “military power is still important in world politics”. The theory of greater cooperation among nation states, and thereby the emphasis of ‘low politics’ compared to ‘high politics’, as argued for in the next part, is interlinked with Keohane’s and Nye’s concept of (complex) interdependence in world politics.

Complex Interdependence

Paying emphasis on the interdependence of nation states, the involvement of non-state actors in international relations and the importance of cooperation, (complex) interdependence is a concept inside neoliberal institutionalism, which underlines the value to interdependency of nation states in international relations. Introduced by Keohane and Nye (1989) in their work *Power and Interdependence*⁴, complex interdependence attempts to challenge realist hypotheses by stressing that not only the nation state but also other non-state actors participate in international politics, and that hard politics, e.g. military force, remains rather ineffective. The ineffectiveness of military force is not an ultimate status. Rather, Keohane and Nye point out that the use of military force and its effects can be costlier than other means, e.g. economic sanctions, and cannot guarantee a success (Keohane & Nye, 1989, pp. 16, 28). Therefore, the two theorists argue that “military force [...] could be irrelevant to resolving disagreements on economic issues among members of an alliance” (Keohane & Nye, 1989, pp. 16, 28). Instead, interdependence accentuates the importance of relations between states in areas such as economic relations and foreign trade. Nevertheless, compared to economic power, military power remains more effective when it comes to actual conflicts among rivals (Keohane & Nye, 1989, p. 17). Consequently, Keohane and Nye emphasise the importance of military power for political or military relations of a nation state or an alliance with opponent coalitions (Keohane & Nye, 1989, p. 25). Beside the minor role of military force, two more characteristics of complex interdependence are introduced. Multiple channels indicate the possibilities societies have to cooperate and connect, in both formal and informal manners. In total, multiple channels refer to interstate, transgovernmental, and transnational relations (Keohane & Nye, 1989, p. 25). It is not only the interaction between governmental elites connecting societies, but also informal relations between non-governmental elites and transnational organisations (Keohane & Nye, 1989, p. 24). Besides pursuing their own needs and interests, those actors also “act as transmission belts, making government policies in various countries more sensitive to one another” (Keohane & Nye, 1989, p. 26). The third characteristic of complex interdependence is the absence of hierarchy among issues. As opposed to realism, where security and survival is pivotal in national interests, the international agenda in complex interdependence consists of numerous issues where no issue-area is consistently dominant over the others, such as military security (Keohane & Nye, 1989, p. 25). Furthermore, “many issues arise from what used to be considered domestic

⁴ First edition of *Power and Interdependence* was published in 1977

policy, and the distinction between domestic and foreign issues becomes blurred” (Keohane & Nye, 1989, p. 25).

In general, Nye (1993) finds that once complex interdependence between states has been established, ‘low politics’, such as economic and social affairs, are of greater importance and in the focus of state interest, whereas ‘high politics’ of national security are of lesser concern. Interdependence is most apparent in industrialised and pluralist countries, and is hence linked to the modernisation process of a state (Jackson & Sørensen, 2013, p. 109).

4.0 Historical Overview

The following chapter provides an overview of U.S.-China and U.S.-Taiwan relations of the last 50 years, starting with the Nixon administration. Even though communist China was established in 1949 and the U.S.-Taiwan relation already began after the Second World War, Nixon’s presidency was chosen as point of departure. Nixon was the first U.S. president who acknowledged that an established relationship with China would contain certain benefits and opportunities for the U.S. national interest. For the sake of a better overview of the historical events, the different U.S. presidential administrations of the past 50 years constitute the outline of the chapter’s division in subcategories. The historical overview points out how Taiwan and other issues, such as security matters and national interests, influenced the bilateral relationship between the U.S. and China as well as how the Sino-American economic relations developed.

The Nixon/Ford Administration, 1969-1974/1974-1977

Since the establishment of the PRC in 1949, relations between the U.S. and China were tense. Fearing the spread of communism in Asia, the U.S. officially supported the National Government of China and continued to recognise it as the sole representative of China, even after the ROC fled to Taiwan, following its defeat by the PRC movement. The island of Taiwan possessed a strategically favourable position in the Taiwan Strait in terms of trade and security, especially after the outbreak of the Korean War in 1950. In 1954, the U.S. and ROC signed the ‘Sino-American Mutual Defense Treaty’, which stabilised their military relations. In the following years, the U.S. facilitated Taiwan to establish a strong and prosperous economy, among others by means of U.S. economic aid, and bilateral commercial relations were consolidated (U.S. Department of State, 2015; TECRO, 2015).

In 1969, Nixon was the first U.S. president initiating a changing U.S. position towards China. The Nixon administration and its foreign policy considered China as an important part for balancing out international disparities (Garrison, 2005, p. 30). While the Taiwan issue remained widely unresolved, the established Shanghai Communiqué between the U.S. and China in 1972 agreed on “settling international disputes without the threat of force and reducing tension through normalization of U.S.-China relations, and [the Communiqué] established the concept that neither power should seek hegemony in Asia” (Garrison, 2005, p. 31). Additionally, the U.S. officially acknowledged the one-China principle and the PRC as China’s sole legal government. However, the continuation of arms sales to Taiwan constituted major obstacles in the process towards normalisation (Garrison, 2005, p. 39).

The Carter Administration, 1977-1981

Even though the Carter administration expressed its support of the Shanghai Communiqué from 1972 as well as the one-China principle, proceeding with the normalisation process with China did not have a major priority in Carter’s foreign policy. Nevertheless, the U.S. government showed its willingness to continue the normalisation dialogue, which remained to be difficult on account of discrepancies concerning Taiwan. Nevertheless, on 04 December 1978, the U.S. agreed on the content of the final draft of the ‘Joint Communiqué of the Establishment of Diplomatic Relations’, including the acknowledgement of Taiwan as a integrated part of China. On 01 January 1979, the U.S. officially recognised the PRC (Huang, 2010, p. 171). Due to the continuing strong support of Taiwan by the U.S. public, the Congress passed the Taiwan Relations Act (TRA) in March 1979, signalling America’s population the uninterrupted maintenance of relations with Taiwan. The TRA acts as legal basis to govern the unofficial U.S.-Taiwan relationship (U.S. Department of State, 2015). Among others, it ensures the supply of equipment for purposes of self-defence from the U.S. to Taiwan, and facilitates the establishment of national offices in the U.S. or Taiwan respectively (TECRO, 2015). Passing the TRA would, according to the Chinese, not interfere with the established normalisation.

With the reached normalisation and the opening up of the Chinese market, bilateral interactions between China and the U.S. also started to improve, especially trade relations benefitted greatly. As a result, the U.S. and China granted each other the Most Favoured Nation (MFN) status, which in turn fostered further trade agreements (Kao, 2010, p. 102).

The Reagan Administration, 1981-1989

In 1981, the presidential administration changed from Carter to Reagan. The strong anti-Communist and long supporter of Taiwan already announced during his presidential campaign that the TRA and not the Joint Communiqué should form the basis of the U.S. China policy. Consequently, his pro-Taiwan attitude led to more tense relations with China in the beginning of his administration (Garrison, 2005, p. 79). A major obstacle for several years in U.S.-China relations constituted the arms sales policy on Taiwan. China announced great consequences for the bilateral relation if the U.S. arms sale to Taiwan would continue. They proclaimed that, if the U.S. is not decreasing its arms sales to Taiwan every year, Chinese ambassadors in the U.S. would be recalled and thereby the U.S.-China relationship downgraded (Garrison, 2005, p. 85). As a result, the dispute about the arms sales to Taiwan cut further establishments in numerous areas of the bilateral cooperation. In the ‘August 17 Communiqué’ from 1982, the U.S. declared to decline its arms sales to Taiwan. This final Communiqué served the purpose of further strengthen bilateral ties in the area of economy, culture, education, science and technology. However, in order to continue the close U.S.-Taiwan ties, Reagan signed the ‘Six Assurances’, which are stating that the U.S.

1. has not agreed to set a date for ending arms sales to Taiwan;
2. has not agreed to hold prior consultations with the PRC on arms sales to Taiwan;
3. will not play any mediation role between Taipei and Beijing;
4. has not agreed to revise the Taiwan Relations Act;
5. has not altered its position regarding sovereignty over Taiwan;
6. will not exert pressure on Taiwan to negotiate with the PRC (TECRO, 2015, n.p.)

Nevertheless, China and the U.S. increased their bilateral relations in the economic and commercial area. The normalisation process as well as China’s economic reforms allowed Sino-American trade of goods and services to increase and by 1984 the U.S. became China’s third largest trading partner, after Japan and Hong Kong (Dong, 2013, p. 3).

Supporting China’s modernisation process had certain benefits for the U.S. Besides being able to protect its national interests, economic ties and cooperation also dragged away the focus from the Taiwan question and therefore further confrontations were avoided (Garrison, 2005, p. 96).

The George H.W. Bush Administration, 1989-1993

The declared policy goal of Bush was to further strengthen and stabilise U.S.-China relations, in order to increase the pressure on the Soviet Union. This political approach explained his reactions to the Tiananmen crackdown in 1989: Bush ignored the voices inside his administration to speak out harsh sanctions against China and its leaders. Instead, Bush sought to not threaten U.S.-China relations by disconnecting the PRC from the international community (Garrison, 2005, p. 112). However, the U.S. did respond to the Tiananmen Square crackdown with numerous sanctions, to communicate its objection regarding PRC's actions. The mostly liberal reaction by the U.S. towards the crackdown can be explained by the developing China-Soviet relations, as well as the assumption that greater bilateral economic relations stabilises U.S.-China cooperation and therefore could result in certain political reforms in China (Garrison, 2005, p. 115). In fact, already in May 1989, Bush's administration pronounced a development of U.S-China trade relations in order to support a further development of economic liberalisation (Garrison, 2005, p. 116). Therefore, the U.S. government also continued to grant China the MFN tariff status. Without the renewal of MFN, the U.S. economy would suffer immensely and the PRC would lose its motivation to make allowances for U.S. national core interests, such as fair trade practices, human rights, or missile and arms sales (Garrison, 2005, p. 122).

The Clinton Administration, 1993-2001

After the end of the Cold War, the new presidential administration wanted to engage China on greater human rights standards and linked bilateral trade relations to the progress in human rights. Clinton's administration expected the PRC to improve its human rights standards, if its progress was interlinked with trade and commercial cooperation and therefore with its own prosperity. Continuing this line of thought, Clinton's administration linked the MFN tariff status with human rights, which in turn jeopardised the renewal of China's MFN status in 1994 (Garrison, 2005, p. 138). In early 1994, then-Secretary of State Christopher announced the possible withdrawal of the MFN status and by that provoked the PRC to disregard the U.S. human rights policy and deplore U.S. intervention in China's internal affairs (Garrison, 2005, p. 139). Caused by China's unwillingness of complaisance in terms of human rights, Clinton's administration saw the need to adjust its foreign policy toward China and de-link human rights from the MFN (Kao, 2010, p. 323). In order to maintain U.S.-China relations, the renewal of MFN tariff status was indispensable. Even though concerns in several areas remained (e.g. China's record of human rights abuses or the continued proliferation of

weapons of mass destruction), the renewal of the MFN status was agreed on in June 1997 (U.S. Department of State, 1997). At the end of Clinton's presidential term in 2000, the U.S. total trade of goods with China accounted for \$116.20 billion according to the U.S. Census Bureau (U.S. Census Bureau, 2015).

Furthermore, political bilateral relations continued to improve: During the U.S. visit of China's president in October/November 1997, President Jiang and President Clinton agreed on pursuing important steps to continue the work towards a 'constructive strategic partnership', despite significant differences in human rights issues (Frost, 1997).

5.0 Analysis

In the analytical chapter of this thesis the bilateral relations between the U.S. and China under the influence of economic interdependence and the Taiwan issue are examined. Chapter 5.1, 'Economic Interdependence', is divided into two more sub-sections, namely into 'U.S.-China Trade Relations' and 'U.S.-China Bilateral Investment Relations'. The Taiwan issue, chapter 5.2, is segmented into the two presidential administrations of the past 15 years, the Bush and Obama administration. The analysis ends with the discussion section where analysed relations are linked to the chosen international relations theories.

5.1 Economic Interdependence

During the last decades, starting with economic reforms in China at the end of the 1970s, China evolved into a major world economy. In fact, China's economy ranks second as the largest world economy after the U.S., on the basis of the nominal dollar and the Purchasing Power Parity (PPP) (Lawrence, 2013, p. 32). Interlinked with China's general economic development, the economic relation between China and the U.S. also developed and increased since 1978. The U.S.-China two-way trade, for example, increased sharply from \$2 billion in 1979 to \$591 billion in 2014 (Morrison, 2015b). The trade agreement granting both states MFN status, signed after normalisation between the U.S. and China was reached in 1979, opened possibilities for developed

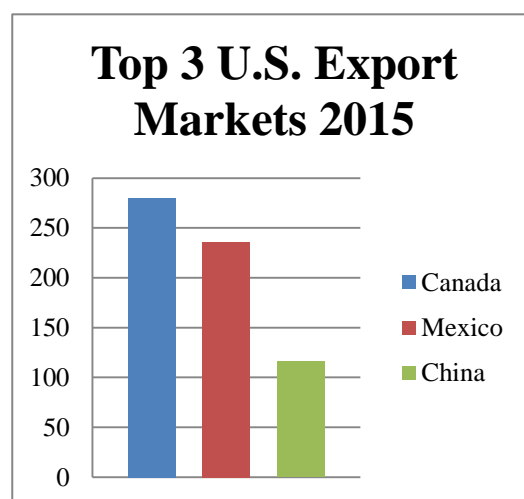


Diagram 1: Official U.S. statistics – Top 3 U.S. Export Markets 2015
Source: U.S. International Trade Commission DataWeb, 2015

trade and economic relations. According to official U.S. statistical data, China is the greatest

source of imports for the U.S., its second largest trading partner and, after Canada and Mexico, the third largest export market for the U.S. (Lawrence, 2013, pp. 32-33; Morrison, 2015b, p. 2). Additionally, economic reforms in China resulted, among others, in a decrease of import tariffs. The average import tariffs in China were lowered from over 50% in 1982 to less than 10% in 2005 (Dong, 2010, p. 200). By lowering import tariffs, thus reducing trade barriers, the Chinese government aims at making the market more attractive to foreign investments due to greater accessibility.

Even though Sino-American economic relations developed greatly, numerous issues and controversial subjects emerge during cooperation, as for example China's WTO commitments. In order to feature room for bilateral debates, China and the U.S. established two forums for discussions of economic issues and concerns of the two states - the U.S.-China Joint Commission on Commerce and Trade (JCCT) from 1983 and the U.S.-China Strategic and Economic Dialogue (S&ED), established in 2009 by U.S. President Obama and his Chinese counterpart Hu Jintao.

In 2001, China joined the WTO. The WTO membership caused further implementations of economic reforms inside China, with the intent to expand prosperity of the population, further liberalise trade and to reach greater integration in the world community (Dong, 2010, p. 193). Every WTO member state issues a list of commitments and exemptions when joining the organisation. In China's case, commitments include lower tariffs of imported goods and broader trading rights for foreign and domestic companies (Dong, 2010, p. 193). In its '2015 Report to Congress On China's WTO Compliance' the U.S. Trade Representative points out the complexity of China's WTO membership as well as certain problems and its influences of U.S.-China trade and investment relationship. Those "can be traced to the Chinese government's interventionist policies and practices and the large role of state-owned enterprises and other national champions in China's economy, which continue to generate significant trade distortions that inevitably give rise to trade frictions" (United States Trade Representative, 2015, p. 2). However, the U.S. Trade Representative also recognised intentions from the Chinese government to implement further economic reforms with the potential of addressing existing problems and promote the realisation of "the tremendous potential of the U.S.-China trade and investment relationship" (United States Trade Representative, 2015, p. 2). Nevertheless, when disputes over trade issues fail to be resolved by dialogue, WTO member states can bring cases to the WTO. Since 2001, the U.S. brought

17⁵ cases against China to the WTO, whereas China brought nine⁶ cases against the U.S. to the WTO (WTO, 2016).

After having introduced basic facts displaying the economic relationship between the U.S. and China, more details are given on the U.S.-China trade relations of the last 15 years as well as the reciprocal investment of China and the U.S. Regarding trade relations, data and statistics of the respective imports and exports are provided for the purpose of presenting development and coherence of the bilateral trade relations. Those statistics will also display the trade balance deficit of the U.S., and what it might indicate for future relations. However, differences between official U.S. trade statistics and official Chinese trade statistics repeatedly cause debates. As for example, both states agree that the U.S. trade deficit with China is immense and continues to grow. Discrepancies emerge concerning the amount of the deficit and with which pace it is increasing. Martin (2016) compares the respective figures and states that according to official U.S. statistic, the bilateral trade deficit rose from \$83 billion in 2001 to \$367 billion 2015. Chinese statistics however, show its bilateral trade surplus from \$28 billion in 2001 increasing to more than \$237 billion in 2015 (Martin, 2016, p. 1). The cause for different trade data are divergent statistics of U.S. imports from China (see Table 1).

Comparison: U.S.-China official data On China's Exports, imported in the U.S. [\$ in billion]					
Year	2009	2010	2011	2012	2013
U.S. Imports (C.I.F.)⁷	309.56	382.99	417.39	444.45	459.19
CN Exports (F.O.B.)	220.80	283.29	324.45	351.78	368.41

Table 1: Comparison of U.S. and Chinese official trade statistics, 2009-2013

Source: U.S. International Trade Commission DataWeb, 2015; National Bureau of Statistics of China, 2012

⁵ 7 cases = Implementation notified by respondent; 4 cases = In consultation; 3 cases = Settled or terminated (withdrawn, mutually agreed solution); 1 case = Report(s) adopted, no further action required; 1 case = Report(s) adopted with recommendation to bring measure(s) into conformity; 1 case = Panel established, but not yet composed (WTO, 2016)

⁶ 3 cases = Report(s) adopted, no further action required; 2 cases = Implementation notified by respondent; 2 cases = Report(s) adopted with recommendation to bring measure(s) into conformity; 1 case = In consultation; 1 case = Panel composed (WTO, 2016)

⁷ The U.S. and China have different measures in valuing their exports and imports. The U.S. is normally using the 'freight along side' (F.A.S.) method to value its exports and the 'customs value' (C.V.) to measure its imports. As opposed to that, China uses the 'free on board' (F.O.B.) method to value its exports and the 'cost, insurance, and freight' (C.I.F.) method to value its imports (Martin, 2016, p. 1). In order to be able to accurately compare official U.S. and Chinese data, statistical data for U.S. imports has been in this case calculated in C.I.F.

As Table 1 indicates, China's trade statistics are "routinely much lower in value than the official U.S. trade statistics" (Martin, 2016, p. 3). In 2004, the JCCT decided on conducting research on the causes of the different trade statistics. The two conducted studies, released in October 2009 and December 2012, conclude that the "eastbound data"⁸ showed the greatest discrepancies, which are responsible for 80-90% of the total dissimilarities in the bilateral trade balance (Martin, 2016, p. 6; JCCT, 2009, p. 2). The discrepancies in eastbound trade can stem from intermediary countries or regions, due to, for example, adding new values when goods are re-exported, or the last known destination is not declared as U.S. by Chinese exporters but as the intermediary country (JCCT, 2009, p. 3).

In order to present an as complete picture as possible, both official statistical data, from the U.S. and China, are being displayed in the following sections.

5.1.1 U.S.-China Trade Relations

Since normalisation between the U.S. and China has been reached, trade relations between the two countries continued to increase on an annual basis. Looking at American-Sino relations, economic and especially trade relations proved to be of major importance and is a significant component on the path of increasing cooperation and strengthening bilateral relations. According to official Chinese trade statistics, the bilateral trade of goods between the U.S. and China increased from \$80.48 billion in 2001 to \$520.75 billion in 2013 (see Table 3), thus in only 13 years it grew 6.5 times. Compared to this data, official U.S. statistics display different numbers. The total trade of goods with China rose, according to the U.S. government, from \$121.46 billion in 2001 to \$562.16 billion in 2013 (see Table 2), thus it increased by 'only' 4.6 times. Even though the difference between the two official data sets concerning the growth of total trade from 2001 to 2013 is substantial, it does not fail demonstrating the consistent increase in trade relations.

⁸ 'Eastbound data' = U.S. imports from China and Chinese exports to the U.S. (Martin, 2016, p. 5).

U.S. Trade in Goods with China - Official U.S. statistics

[\$ in billion]

Year	Exports (F.A.S.)	Imports (C.V.)	Total	Trade Balance
2001	19.18	102.28	121.46	-83.10
2002	22.13	125.19	147.32	-103.07
2003	28.37	152.44	180.80	-124.07
2004	34.43	196.68	231.11	-162.25
2005	41.19	243.47	284.66	-202.28
2006	53.67	287.78	341.45	-234.10
2007	62.94	321.44	384.38	-258.51
2008	69.73	337.77	407.51	-268.04
2009	69.50	296.37	365.87	-226.88
2010	91.91	364.95	456.86	-273.04
2011	104.12	399.37	503.49	-295.25
2012	110.52	425.62	536.14	-315.10
2013	121.72	440.43	562.16	-318.71
2014	123.68	466.75	590.43	-343.08
2015	116.19	481.88	598.07	-365.70

Table 2: Official U.S. statistics – U.S. Trade in Goods with China, Official U.S. statistics, 2001-2015
Source: United States Census Bureau, 2015)

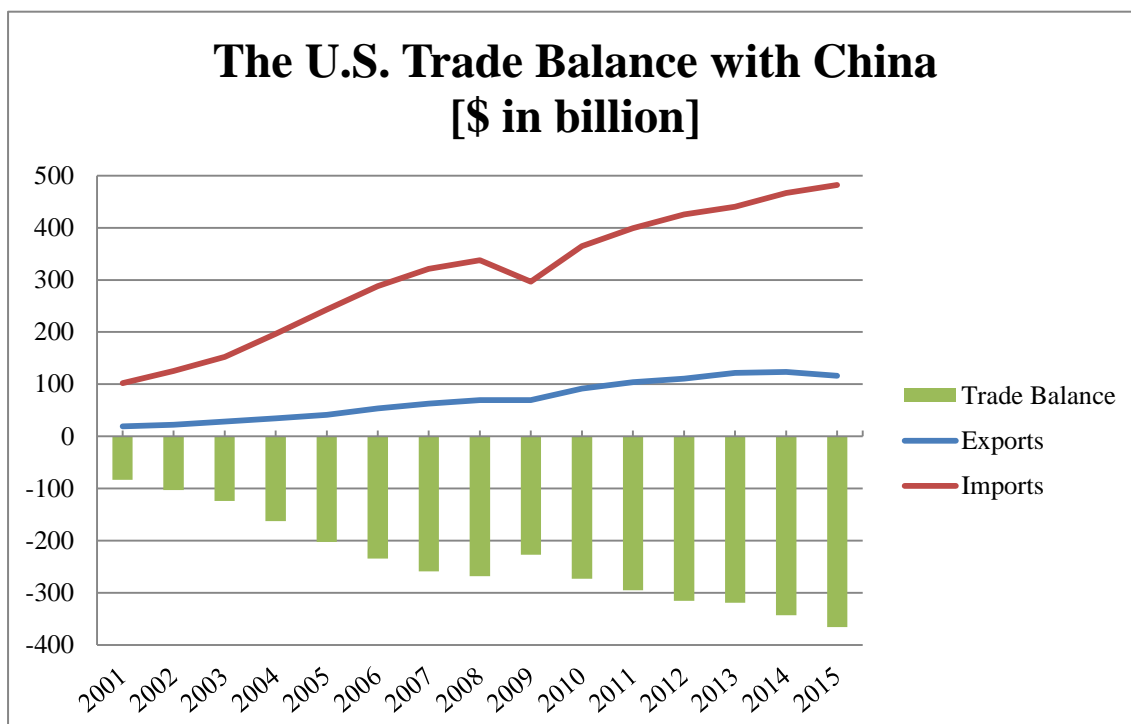


Diagram 2: Official U.S. statistics – U.S. Trade Balance with China, 2001-2015
Source: United States Census Bureau, 2015

Table 2 and 3 show the discrepancies in the value between official U.S. and Chinese statistical trade data in more details. As mentioned earlier, both countries use different methods in measuring the value of imports and exports. It might be more coherent to evaluate trade statistics, calculated with the same method – internationally, F.O.B. and C.I.F. are the common, though not universal, methods in evaluating trade data (Martin, 2016, p. 4). However, in order to fulfil the purpose of the thesis, which includes displaying accurate statistics in order to present a, even if complex, complete and truthful picture of real-life situations, including the issue of different measurements in trade values, sticking to the normally used methods of each country is crucial.

China Trade in Goods with the U.S.
– Official Chinese statistics
[\$ in billion]

Year	Exports (F.O.B.)	Imports (C.I.F.)	Total	Trade Balance
2001	54.28	26.20	80.48	28.08
2002	69.95	27.24	97.18	42.71
2003	92.47	33.87	126.33	58.60
2004	124.94	44.66	169.60	80.29
2005	162.89	48.62	211.51	114.27
2006	203.45	59.21	262.66	144.24
2007	232.68	69.39	302.07	163.29
2008	252.38	81.36	333.74	171.02
2009	220.80	77.46	298.26	143.34
2010	283.29	102.10	385.39	181.19
2011	324.45	122.13	446.58	202.32
2012	351.78	132.90	484.67	218.88
2013	368.41	152.34	520.75	216.06

Table 3: Official Chinese statistics – China's Trade in Goods with the U.S., Official Chinese statistics, 2001-2013
Source: National Bureau of Statistics, 2012

Despite major differences in the total value of trade in official U.S. and Chinese statistics, the overall trend of Sino-American trade relations are similar in both countries' data sets, as displayed by Diagram 2 and 3. It shows a constant increase in both exports and imports. However, imports in Diagram 2, as well as exports in Diagram 3 demonstrate a decrease in values from 2008 to 2009. This trend can be ascribed to the global economic crisis, which impacted the trade in most countries.

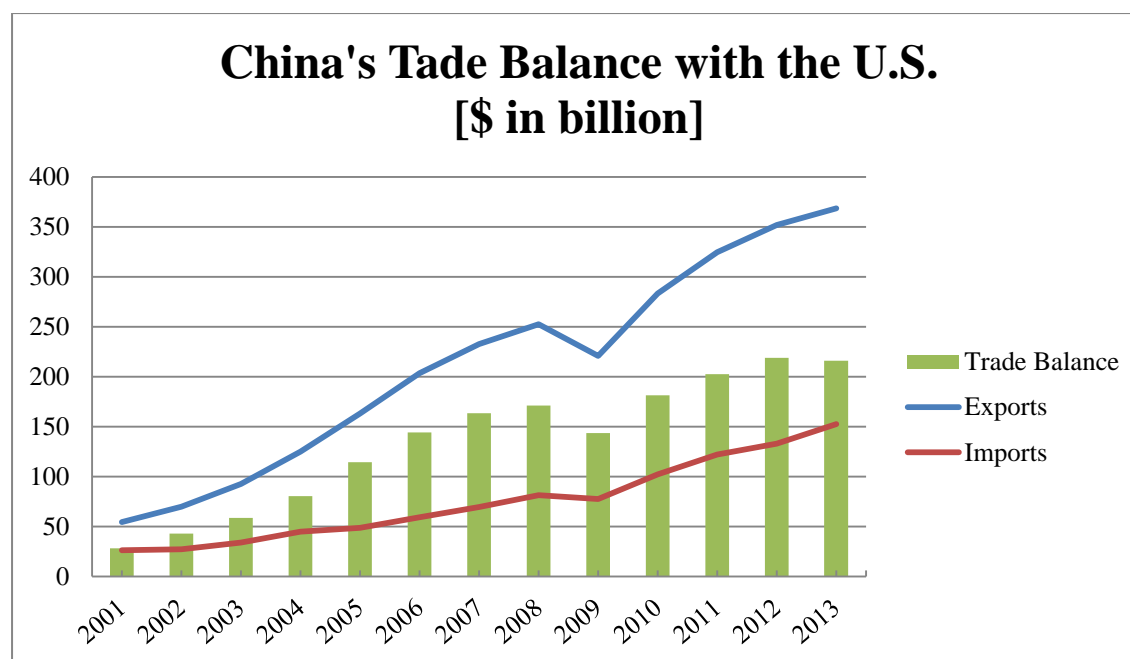


Diagram 3: Official Chinese statistics – China’s Trade Balance with the U.S., 2001-2013
Source: National Bureau of Statistics of China, 2012

Even though China is ‘only’ the third biggest export market for the U.S., financial and trade analysts see the possibility of China emerging to an extended trade market, in case further comprehensive economic reforms are being implemented (Morrison, 2015b, p. 6). This claim is justified by an increased PPP of Chinese population due to China’s economic growth. Therefore, implementing further reforms, which leads to further growth of the economy will consequently also result in an increased demand of foreign goods and services. “China’s growing economy, large foreign exchange reserves (at nearly \$3.6 trillion as of August 2015), and its 1.37 billion population, make it a potentially enormous market” (Morrison, 2015b, p. 7). As of today, ‘aerospace products & parts’, ‘oilseeds and grains’, ‘motor vehicles’, ‘semiconductors and other electronic components’ and ‘waste and scrap’ constitute the major U.S. exports to China (see Table 4).

Top 5 U.S. Exports to China [\$ in million]			
NAIC 4-Digit Commodity	2014	2015	Percent Change 2014-2015
Aerospace products & parts	13.93	1.44	10.90%
Oilseeds & Grains	16.29	13.00	-20.10%
Motor vehicles	11.25	9.25	-17.80%
Semiconductors & other electronic components	6.45	6.93	7.30%
Waste & scrap	7.09	5.94	-16.20%

Table 4: Official U.S. statistics –Top 5 U.S. Exports to China, 2014 + 2015
Source: U.S. International Trade Commission DataWeb, 2015

The amount of the value of the top 5 exports commodities changed significantly from 2014 to 2015, which caused alterations in the ranking. The normally first ranked commodity ‘oilseeds and grains’ had to endure a loss of 20.10%, causing a downgrading from the first to the second rank. In fact, three out of five commodities (‘aerospace products and parts’ and ‘semiconductors and other electronic components’ excluded) experienced losses in their export values from 2014 to 2015 (see Table 4). The decrease in imported oilseeds and grains in U.S. exports to China can be explained by record harvest of oilseed products, e.g. soybean, in both countries, combined with lower prices, as well as a lower grain volume (Sandler, Travis & Rosenberg Trade Report, 2014).

As already pointed out, the U.S. trade of goods deficit with China is immense and is expected to continue growing. Especially since China joined the WTO in 2001, Sino-American trade expanded, including a growing U.S. trade deficit. In the year of China’s accession to the WTO, the U.S. trade balance already accounted for \$-83.10 billion (see Table 2). Until 2015, the trade balance with China increased to \$ -365.6945 billion (see Diagram 2), which is a negative change of nearly 340%.

The steady increase in the trade deficit is one of the major concerns for U.S. political leaders. Trade analysts are not only concerned about the deficit – in fact, they take it as an indicator that bilateral trade relations are unfair for the U.S. and harming its economy (Lawrence, 2013, p. 36; Morrison, 2015b, p. 2). In turn, Chinese officials are not taking the blame for the trade deficit of the U.S. and point out to seek the reason in “U.S. controls on exports of advanced technology” (Lawrence, 2013, p. 36). Another explanation for the trade deficit, offered by analysts, is the global supply chain. By that, they are referring to the practice that for the production of one item, components from several countries are being used. Most of the time, China is the final destination, where the product is being assembled. Therefore, the statistics declare these products and the entire value as being from China (Lawrence, 2013, p. 36). The WTO estimated in a joint study with the Organisation of Economic Cooperation and Development (OECD) that “the U.S. trade deficit in China would be reduced by 25% (in 2009) if bilateral trade flows were measured according to the value-added that occurred in each country before it was exported” (Morrison, 2015b, p. 3).

The immense trade deficit only occurs in bilateral trade of goods. According to the Office of the U.S. Trade Representative (2014) the service surplus of the U.S. with China was \$17.0 billion in 2012 – an increase of 9.9% compared to 2011 (United States Trade Representative,

2014). This data let suggest that the U.S. service surplus is still existent and might have even grown.

5.1.2 U.S.-China Bilateral Investment Relations

Investment is an important feature in bilateral trade relations and has occupied a position of growing significance in Sino-American ties. Just as trade, investment can boost another country's economy by e.g. the creation of jobs. In order to support bilateral investments, China and the U.S. are negotiating on reaching a bilateral investment treaty (BIT). With an established BIT both countries hope for a more liberalised environment for foreign investment. Additionally, it could assist in limiting Sino-American issues on aspects such as market access and protections for intellectual property (Lawrence, 2013, p. 39), Economic analysts suggest that the BIT could not only enhance bilateral trade relations between the U.S. and China, but also have a significant, positive impact on the Chinese economy. It could lead to further implementations of economic reforms and economic circumstances, such as greater market competition in China or a more adapted use of resources, which could boost commercial growth in China (Morrison, 2015b, p. 39).

Gao Hucheng, China's Commerce Minister, stated at a S&ED summit: "With such an extensive investment relationship, it is necessary for the two sides to have an institutional environment for the protection of these investments" (Eckert & Yukhananov, 2013). The details of what Gao calls an 'extensive investment relationship' is given in the following chapters.

Treasury Securities

China holds an immense amount of U.S. debt and has in fact been the largest holder of U.S. Treasury securities. As of September 2015, China accumulated \$1.26 trillion, followed by Japan with \$1.12 trillion (Morrison, 2015b, p. 13; Statista, 2016). Being an export-driven economy, China receives U.S. dollars (USD) for exported goods, which are being exchanged (sold) into renminbi (RMB) in order to cover exporters' expenses, e.g. paying workers. This exchange from USD to RMB is necessary because China's financial system prohibits payment exchanges inside China with a foreign currency (Lawrence, 2013, p. 38). Buying USD from Chinese exporters ensures USD rates to remain high, meaning hindering the RMB to appreciate compared to the USD and therefore staying competitive in the global trade of goods. Thus, China pegs the RMB to the USD. Simply holding the accumulated amount of USD in forex reserves does not bring any benefits, in terms of interests, for China. Instead,

forex reserves are invested in U.S. Treasury securities, which count as a relatively ‘safe’ investment (Morrison, 2015b, p. 13). By investing in U.S. Treasury securities, China is loaning money to the U.S., ensuring the continued consumption of Chinese products in its biggest export market. In fact, China’s investment in U.S. Treasury securities is a win-win situation. Not only guarantees China the purchasing power in the U.S., but by keeping the RMB lower than the USD, Chinese goods can be sold to economical prices in the U.S. market (Seth, n.d.). China’s holdings of U.S. Treasury securities increased sharply during the first decade of the 21st century. In 2002, China held \$118.0 billion which increased to \$1258.0 billion by September 2015 (see Table 5), thus a rise of 966.10%.

China’s Holdings of U.S. Treasury Securities: 2002 – September 2015

[in \$ billions]

Years	2002	2004	2006	2008	2010	2012	2014	Sept.‘15
China’s Holdings	118.0	222.9	396.9	727.4	1160.1	1202.8	1244..3	1258.0
(%) of Total Foreign Holdings	9.6%	12.1%	18.9%	23.6%	26.1%	23.0%	21.7%	20.6%

Table 5: Official U.S. statistics – China’s Holdings of U.S. Treasury Securities, 2002-September 2015

Source: U.S. Department of the Treasury, retrieved from Morrison (2015b), p.15

From 2010 to 2015 the accumulation of U.S. Treasury securities slowed down and China’s holdings in percentage compared to the total foreign holdings decreased from 26.1% in 2010 to 20.6% by September 2015.

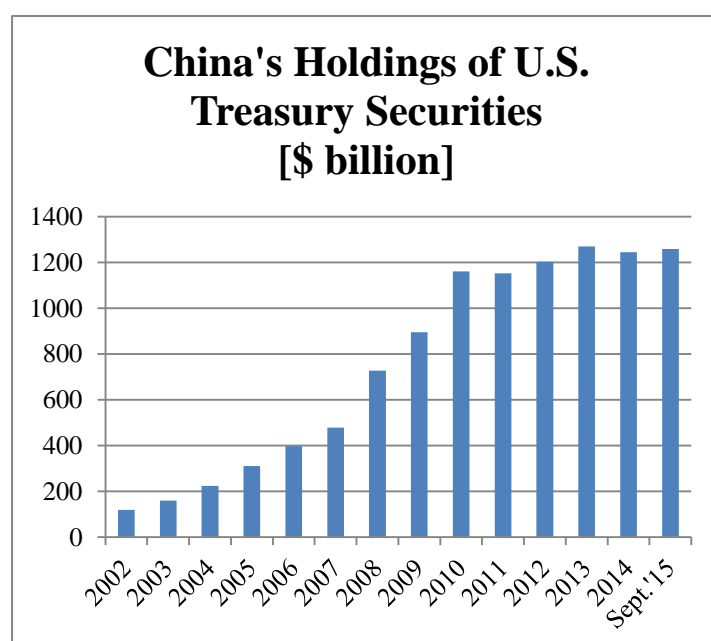


Diagram 4: Official U.S. statistics – China’s Holdings of U.S. Treasury Securities, 2002-September 2015

Source: U.S. Department of the Treasury, retrieved from Morrison (2015b), p.15

The immense amount of U.S. Treasury securities, held by China, triggers concerns among U.S. policymakers and economic analysts. These Concerns evolve around possible leverage given to China due to its large holdings of U.S. debt securities. In case of discrepancies over foreign policies and the bilateral trade relations, it is feared that China can threaten the U.S. to sell an immense share of its securities, in order to achieve a

more beneficial outcome (Morrison, 2015b, p. 14). However, as Morrison (2015b) argues, the holdings of U.S. Treasury securities display a meagre quantity of ‘practical leverage’. As pointed out earlier, China is an export-driven economy, with the U.S. market being its biggest export destination. Therefore, the well-being of China’s economy depends on the U.S. economy being stable, healthy and growing. Consequently, selling a major share of its U.S. debt securities would harm both, the U.S.’ and China’s economy, and might even result in a depreciation of the USD against global currencies, which also implies that China’s remaining holdings of U.S. Treasury securities would decrease in their value (Morrison, 2015b, p. 14). In the end, pegging the RMB to the USD decreases a possible leverage China might have had due to its holdings of U.S. debt securities.

Foreign Direct Investment

After China implemented its ‘Open Door Policy’ in 1978, thus China’s opening to the global economy, Foreign Direct Investment (FDI) in China began to grow rapidly and is, since then, steadily growing each year. Especially during the 1980s, China received a great amount of

Annual U.S. FDI in China [\$ in million]	
2001	4433.22
2002	5423.92
2003	4198.51
2004	3940.95
2005	3061.23
2006	2865.09
2007	2616.23
2008	2944.34
2009	2554.99
2010	3017.34
2011	2369.32
2012	2598.09
2013	2819.87
2014	2670
2015	2590

Table 6: Official Chinese statistics – Annual U.S. FDI in China, 2001-2015
Source: National Bureau of Statistics of China, 2012; China’s Ministry of Commerce (MOFCOM), 2016 for data on 2014+2015

foreign investment (Kao, 2010, p. 103). Hong Kong, being the biggest foreign investor in China, invested \$92.67 billion in 2015 (MOFCOM, 2016). According to official Chinese statistics, the U.S. ‘only’ ranked 6th among foreign countries investing in China, with a total investment of \$2.59 billion in 2015 (see Table 6). However, the U.S. contributes significantly to China’s FDI – due to lower labour costs, compared to other Asian countries, such as Taiwan or Japan, U.S. manufacturers relocated companies and industries to China (Hickey & Zhou, 2010, p. 142).

After economic reforms, the establishment of foreign companies and manufactures in China were legalised and by that foreign investors were authorised to produce and sell their goods in China (Kao, 2010, p. 103). As of today, a major part of ‘made in China’-products are being manufactured by foreign-owned, or –invested companies.

Thus, FDI in China possesses a weighty part in the success and importance of China’s export-driven economy. In the first two decades after China’s opening to the global economy,

Annual Chinese FDI in the U.S. (ODI) [\$ in million]	
2004	119.93
2005	231.82
2006	198.34
2007	195.73
2008	462.03
2009	908.74
2010	1308.29
2011	1811.42
2012	4047.85
2013	3873.43

Table 7: Official Chinese statistics –
Annual Chinese FDI in the U.S., 2004-
2013
Source: National Bureau of Statistics
of China, 2012

Chinese companies and firms were forbidden to invest in businesses outside China – the focus was on boosting the establishment and development of domestic companies (Morrison, 2015a, p. 17). This attitude by the Chinese government changed in 2000 when they started encouraging Chinese companies to invest abroad. The motive of this change of heart lied, among others, in the massive accumulation of foreign exchange reserves. Even though, China invested a weighty part of those in U.S. Treasury securities, they, though being said to pose a safe investment, promised, compared to foreign investments, a relatively low profit (Morrison, 2015a, p. 17). The immense boost of foreign investment in the U.S. in 2008 (see Table

7) could be ascribed to the establishment of the China Investment Corporation (CIC) in 2007 in order “to seek more profitable returns on [China’s] foreign exchange reserves and diversify away from its U.S. dollar holdings” (Morrison, 2015a, p. 17).

Comparing U.S. FDI in China with Chinese FDI in the U.S., the demonstrated data sets display that Chinese FDI in the U.S. used to be significantly smaller throughout the years. However, according to official Chinese statistics, this trend changed in 2011, where China’s investment in the U.S. increased profoundly and even exceeded U.S. FDI in China (see Diagram 5).

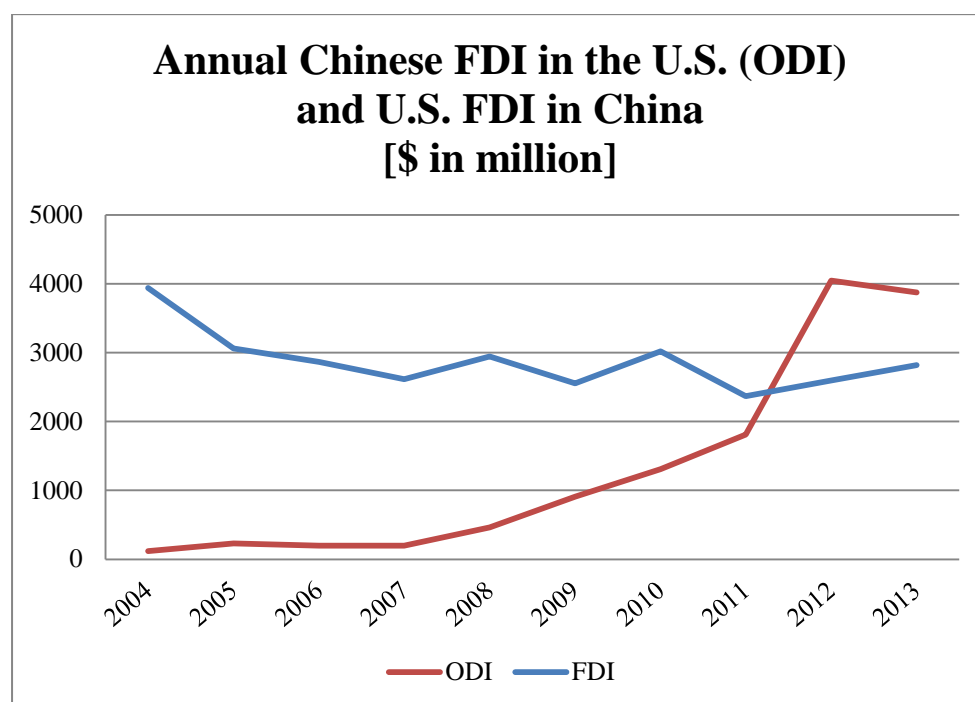


Diagram 5: Official Chinese statistics – Annual Chinese FDI in the U.S. and U.S. FDI in China

Source: National Bureau of Statistics of China, 2012

Note: China's FDI is referred to as Overseas Direct Investment (ODI) in order to be able to make a distinction between the two foreign investments. Only the years 2004-2013 are displayed because those are the years where data on China's investment in the U.S. was available. In order to compare FDI and ODI it was decided to concentrate on this time span.

Official U.S. statistics on FDI with China show the same trend of a steadily growing FDI by China in the U.S. Where in the beginning of the 21st century (2002-2003), China's FDI was practically not existent – U.S. data shows negative FDI flows, which indicates the outflow of investments (see Table 8) (Morrison, 2015b, p. 16) – Chinese FDI in the U.S. began to increase and surpassed U.S. investments in China in 2011. Morrison (2015b) suggests that rising foreign investments in the U.S. points to fewer foreign investment barriers in the U.S. and more liberalised regulations for Chinese investors, compared to regulations in China, U.S. investors are encountering (p. 16)⁹.

⁹ Official Chinese and U.S. statistics on FDI differ because both countries use different methods to calculate foreign investments. "The components of FDI are equity capital, reinvested earnings and other capital (mainly intra-company loans). As countries do not always collect data for each of those components, reported data on FDI are not fully comparable across countries. In particular, data on reinvested earnings, the collection of which depends on company surveys, are often unreported by many countries." (UNCTAD, 2013).

Annual Chinese Investment in the U.S. and U.S. Investment in China (ODI)

[\$ in million]

Year	FDI	ODI
2002	-120	No data available
2003	-62	1273
2004	150	4499
2005	146	1955
2006	315	422.6
2007	8	5243
2008	500	15971
2009	500	-7512
2010	1037	5420
2011	520	-1087
2012	1370	-3482

Table 8: Official U.S. data – Annual Chinese FDI in the U.S. and U.S. FDI in China

Source: Organisation of Economic Cooperation and Development, n.d.

Morrison (2015b) provides some positive but also critical voices regarding growing Chinese investment in the U.S.: He stresses that China's foreign investment in the U.S. does not only improve the general bilateral Sino-American relations, it also creates new job opportunities in the U.S. and by that could undermine critical voices that U.S.-China trade relations is harmful for the U.S. economy and employment due to the outsourcing of labour (p.19).

Nevertheless, critics argue that Chinese FDI is mainly focused on Mergers and Acquisitions (M&A) instead of Greenfield investments, in order to create a more developed dominant and competitive position of Chinese companies. When concentrating on M&A, Chinese firms still benefit by obtaining technology and know-how, but it does not boost the U.S. economy, because no new factories are being built which would create more job opportunities (p.20).

The private consulting firm 'Rhodium Group' presents annual and cumulative estimations of Greenfield and M&A transactions by China in the U.S. Their 'China Investment Monitor' shows that the value of annual M&A investments in the U.S. are in fact significantly higher than Greenfield investments, and grew enormously from 2007 onwards (see Diagram 6). In September 2007, the 'China Investment Corporation' was founded. The purpose of the establishment of the 'wholly state-owned company' was to create "a vehicle to diversify China's foreign exchange holdings and seek maximum returns for its shareholder within acceptable risk tolerance" (CIC, n.d.). The immense holdings of foreign reserves by China are normally used for buying up U.S. Treasury securities which are known to be the safest investment. However, it also does not promise any gain for the Chinese state in form of interest rates or alike. In order to make a profit out of its foreign reserves, the PRC established CIC in order to invest governmental money abroad. Therefore, CIC goes for big

investments with a high return – like big investment funds do. They are known for investing in proven concepts where a profit is as much guaranteed as possible. Also CIC’s statement to invest “within acceptable risk tolerance” is another explanation for the augmented investment in M&A instead of Greenfields.

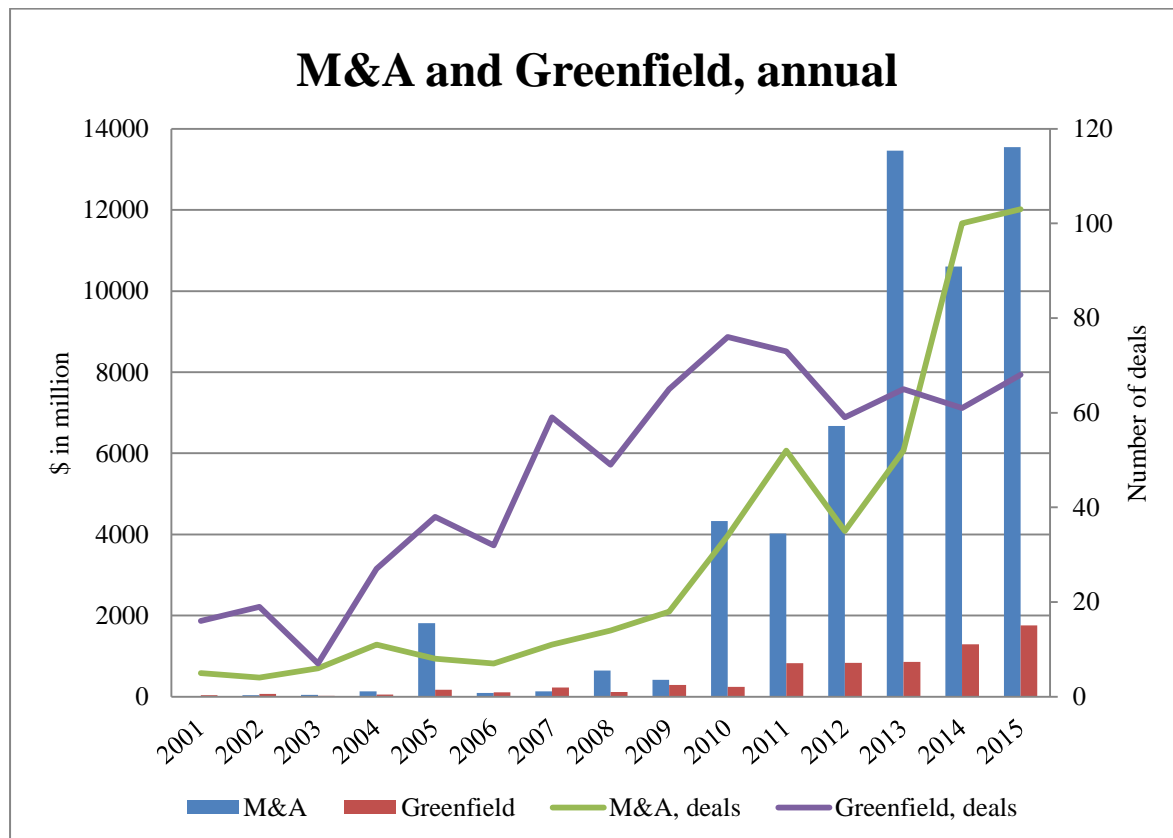


Diagram 6: Rhodium Group’s estimation on the annual amount of value and projects of Chinese M&A and Greenfield investments in the U.S., 2001-2015
Source: Rhodium Group, China Investment Monitor, 2016

5.2. The Taiwan Issue in the U.S.-China Relationship, 2001-2015

In the following sections, the relations between the U.S. and China are examined. For that purpose the chapter is divided up into two parts, which respectively are dealing with the Taiwan issue under the Bush administration and under the Obama administration. Each subchapter starts with a general overview of the U.S. foreign policy approach towards China and major events that occurred. Providing this information does not only benefit the general overview, but also outlines main differences between the two U.S. administrations in their approach towards China. After the foreign policy towards China is outlined, the respective responses of each administration as well as China in regards to the major controversial subjects in the Taiwan issue, namely Taiwan’s quest for independence and the U.S. arms sales to the island, are analysed.

5.2.1. The Taiwan Issue under the Bush Administration

As outlined in the historical overview, Clinton's administration pursued a cooperative policy towards China and President Clinton together with his counterpart Jiang promised to make efforts working towards a 'constructive strategic partnership'. Opposing Clinton's approach towards China, George W. Bush, as he already announced during the 2000 presidential election, and his administration practiced a more 'hard-line policy' towards China, one of 'strategic competition' (Garrison, 2005, p. 165). In the beginning of his first term, Bush relied strongly on the Congress Advisory Board, which is said to have had great influence on Bush's foreign policy (Yu, 2009, p. 84). Consequentially, the Board's stance that President Clinton and his administration made one too many concessions to the PRC during their presidential terms, was mirrored in President Bush's foreign policy, often referred to as 'ABC' – Anything But Clinton (Yu, 2009, p. 84). According to the new administration, China, being a major power, seeks to tilt the balance of power in Asia in its own favour, which, as Condoleezza Rice stated, "makes it a strategic competitor, not the 'strategic partner' the Clinton administration once called it" (Rice, 1999, p. 56), and should be treated as such. Instead of building up a closely interlinked relationship with the PRC, Bush's administration wanted to focus on further stabilising already established ties with allies in East Asia, such as Japan and Taiwan (Garrison, 2005, p. 165). President Bush supported the 'Taiwan Security Enhancement Act'¹⁰ and approved the initiative to involve Taiwan in the 'Theatre Missile Defence System' (TMD)¹¹. All those steps were included in the initial East Asian policy by the Bush administration (Garrison, 2005, p. 165).

The terrorist attacks on the U.S. on 9/11 constitute a turning point in the until then tense U.S.-China relationship: the Bush administration changed the rather confrontational policy towards China to a more "cooperative, constructive, and candid" (Hickey & Zhou, 2010, p. 139) relationship. The changed stance towards China can be explained by, inter alia, President Jiang Zemin's quick expression of condemnation of terrorism in general as well as China's fast declaration to support the U.S. in its fight against terror (Bo, 2010, p. 254; Rabin, 2012). China supported the U.S. in the war in Afghanistan by contributing \$150 million for assisting the reconstruction of Afghanistan, as well as permitting Japanese vessels to be placed in the

¹⁰ The 'Taiwan Security Enhancement Act' was a U.S. Congressional bill, which was never approved by the Senate or signed into law by the President. It foresaw enhanced military support for Taiwan as well as direct U.S.-Taiwan military communication lines (106th Congress, 2000).

¹¹ TMD = "deployment of nuclear and conventional missiles for the purpose of maintaining security in a specific region, or theatre. The purpose [...] is to protect allies from local threats in their region or to address specific security issues and enable credibility in addressing particular threats" Encyclopædia Britannica (2015).

Indian Ocean and by that overlooking the traditional tense military relation between China and Japan (Rabin, 2012). Instead of regarding China as a threat to the U.S., the U.S. government had a new enemy and found in China a strategic 'friend' in its 'War on Terror'. The focus of bilateral relations shifted away from disputes and discrepancies towards mutual interests and cooperation (Garrison, 2005, p. 175).

The shift in U.S. policy priorities towards the fight of terrorism contains other benefits for Sino-American relations. Incorporating terrorism in the centre of U.S. foreign policy priorities simultaneously embedded security as well as economic concerns on top of the U.S. priority list. Consequently, per se traditional and value-based issues were moved to the background and for example China's human rights record did only play a minor role in U.S.-China relations during Bush's presidential term (Wang, 2009, p. xvi). This transition differs to a great extent from Bush's predecessor Clinton, who, unsuccessfully, tried to link human rights standards in China to the MFN status and by that the access to the U.S. economy (Roberts, 2015, p. 115). In fact, Bush saw greater opportunity in positively influencing China's human rights records by granting market access and integrate China economically, than by a conventional, often combative human rights dialogue (Roberts, 2015, p. 115).

Especially in the beginning of his presidential term, Bush placed great importance in bilateral U.S.-Taiwan relations and sought to foster the already close ties between the two countries. Those policy implementations can be explained by the Bush administration's intention to strengthen security cooperation with other democratic states and partners in the East Asian region, such as Japan and Taiwan, instead of increasing cooperation with China (Garrison, 2005, p. 167). Not only, according to the U.S. government, does Taiwan's peaceful transition into a multi-party democracy demonstrate the importance and successfulness of U.S.' overall foreign policy to spread democratic values globally, but also the importance to continue arms sales to the island and by that ensuring Taiwan's ability to defend itself from non-democratic enemies (Hickey & Zhou, 2010, pp. 151-152).

The Issue of Taiwan's Independence

Especially during Bush's second presidential term, bilateral relations between Taiwan and the U.S. tensed up. Rising U.S.-Taiwan controversies can be ascribed to the policies of Taiwan's contentious president Chen Shui-bian, in office from 2000 until 2008. The Bush administration acknowledged its need for establishing a functional relationship with China in order to fulfil the complex task of "maintaining the stable balance in Asia" (Department of

Defense, 2001, p. 4). However, this China centric strategy was feared to be unsuccessful due to Chen's endeavours to reach Taiwan's independence. Even though Chen promised in his first presidential term to accept and respect the heretofore status quo of Taiwan and China, and follow the 'five no's'¹², Chen changed his manifesto in his second term and tried to reach de jure independence from China with the help of a nationwide referendum in 2004 (Hickey & Zhou, 2010, p. 146). He ignored any warnings by the U.S. government to not continue his move towards independence and by that hazard the possibilities of provoking the PRC and causing a destabilisation of the region (Hickey & Zhou, 2010, p. 146). Colin Powell, then-Secretary of State, stressed that "[t]here is only one China. Taiwan is not independent. It does not enjoy sovereignty as a nation, and that remains our firm policy" (U.S. Department of State, 2004a, n.p.). Already in 2003, the Bush administration publicly disagreed with any unilateral attempts to make changes to the status quo by either China or Taiwan and instead reaffirmed the one-China principle (Garrison, 2005, p. 175; Hickey & Zhou, 2010, p. 143) and the PRC as being China's sole legal representative, as stated in the Joint Communiqués. "On Taiwan, the [U.S.] President repeated our policy of a one-China policy, based on the three communiques, the Taiwan Relations Act, no support for Taiwan independence" (Kan, 2014a, p. 74). Further, Bush repeated the U.S. condemnation of expected moves by Chen towards independence during a meeting with then-PRC Premier Wen Jiabao in December 2013:

We oppose any unilateral decision by either China or Taiwan to change the status quo. And the comments and actions made by the leader of Taiwan indicate that he may be willing to make decisions unilaterally to change the status quo, which we oppose (The White House, 2003, n.p.)

The strong stance against Chen's political approaches was highly valued by the Chinese side. During the same meeting in December 2013, Wen stated:

In particular, we very much appreciate the position adopted by President Bush toward the latest moves and developments in Taiwan – that is, the attempt to resort to referendum of various kinds as an excuse to pursue Taiwan independence. We appreciate the position of the U.S. government (The White House, 2003, n.p.)

¹² 'Five no's': a pledge made by Chen Shui-bian in his inauguration speech in 2000. Those encompass, if ensured that the PRC will not use any military force against Taiwan: "[1] no declaration of independence, [2] no referendum on independence, [3] no change in the ROC title, [4] no reference to the 'state to state' formula in the constitution, [5] and no change in the Guidelines for National Unification" (Hickey & Zhou, 2010, p. 146).

The PRC clearly articulated its stance of considering Taiwan as an indisputable part of China and that they will never permit Taiwan to become independent:

Taiwan is an inalienable part of Chinese territory, and we maintain consistently that under the basis of the one China principle, we are committed to safeguard peace and stability in the Taiwan Strait, and to the promotion of the improvement and development of cross-strait relations [...] We will by no means allow Taiwan independence (The White House, 2006, n.p.)

In fact, Chen's relentless moves towards independence from China led the PRC to passing the so-called 'Anti-Secession Law' in 2005. This bill officially formalises the long-standing policy by the PRC to apply 'non-peaceful means' in order to prevent Taiwan to reach de jure independence. However, the law also stresses that non-peaceful means are the PRC's last resort. Instead, China hopes to reunify with the island by peaceful means:

In the event that the 'Taiwan independence' secessionist forces should act under any name or by any means to cause the fact of Taiwan's secession from China, or that major incidents entailing Taiwan's secession from China should occur, or that possibilities for a peaceful reunification should be completely exhausted, the state shall employ non-peaceful means and other necessary measures to protect China's sovereignty and territorial integrity (Anti-Secession Law, 2005, Article 8)

Besides the referendum in 2004, Chen pursued different steps which enraged PRC authorities, such as "changing the name of Taiwan's state corporations, shelving the National Unification Guidelines and National Unification Council, holding a series of controversial referendums, and making repeated calls for a new Taiwan constitution" (Hickey & Zhou, 2010, p. 146). Furthermore, the Chen administration held on to its efforts of re-joining the UN. In 2007, the 15th consecutive proposal of joining the UN, from which Taiwan was expelled in 1971, was rejected (Reuters, 2007). Not only China, but also the U.S. welcomed this outcome. The U.S. opposes Taiwan's membership in international organisations, in which statehood is a precondition for accession, following the statement of acknowledging the one-China principle.

The Issue of Arms Sales to Taiwan

One of the major controversial points in U.S.-China relations in regards to Taiwan is undoubtedly the continuation of U.S. arms deals with the island. In April 2001, Bush agreed

on an immense arms sales deal to Taiwan, including 4 Kidd class destroyers, 12 P-3C Orion anti-submarine aircraft, and 8 diesel submarines (Kan, 2014b, p. 8). “Of course, the United States is also committed to make available defensive arms and defensive services to Taiwan in order to help Taiwan meet its self-defense needs” (U.S. Department of State, 2004b, n.p.). Arms deals are expected to enhance Taiwan’s security and stabilise cross-Straits relations. “We believe a secure and self-confident Taiwan is a Taiwan that is more capable of engaging in political interaction and dialogue with the PRC [...]” (U.S. Department of State, 2004b, n.p.). Already in the beginning of his first presidential term, Bush clearly demonstrated his and his administration’s position towards Taiwan by stating: “I have said that I will do what it takes to help Taiwan defend herself, and the Chinese must understand that” (Kan, 2014a, p. 71).

As a response to U.S. arms sales to Taiwan, the PRC repeatedly referred to the signed three Joint Communiqués between the U.S. and China as the base of Sino-American relations. In these Communiqués, the U.S. officially acknowledges the one-China principle and the PRC as being China’s sole legal government. Therefore, selling arms to Taiwan is considered by the PRC as interfering in China’s internal affairs (Hickey & Zhou, 2010, p. 141). Moreover, China considers the sale of fighters to Taiwan, such as the type F-16, as especially critical. By arguing that fighters are by nature rather of an offensive type, than of a defensive one (Lawrence, 2013, p. 31), China is referring to the TRA, section 2(b)(5): “It is the policy of the United States to provide Taiwan with arms of a defensive character” (96th Congress, 1979, n.p.). Even though the TRA provides a helpful argument against the case of selling fighters to Taiwan, China generally objects the bilateral agreement between the U.S. and the island. Its opposition of the TRA refers to three major arguments: (1) the normalisation between China and the U.S. is based on the three signed Communiqués. The TRA is not part of the international agreements which are forming the base of bilateral relations; (2) The TRA is interfering in China’s domestic affairs; (3) According to the three Communiqués, there is only one China and the PRC is its sole representative (Lin & Chou, 2011, pp. 3-4). Therefore, Taiwan belongs to China and any issue with Taiwan should be accounted as China’s internal affair.

Even though relations between the U.S. and Taiwan tensed up during Chen’s second presidential term, due to his controversial political approaches, the Bush administration signalled its willingness to continue arms sales to the island. Condoleezza Rice’s statement from 2002 provides an explanation for this decision: “[T]he United States has certain

obligations under the Taiwan Relations Act to help Taiwan defend itself. Those are the cornerstones of American policy toward Taiwan” (Garrison, 2005, p. 154). Nevertheless, the Communiqué from 1982 also points out that the amount of arms sales to Taiwan should be proportionate to the threat constituted by China (Garrison, 2005, p. 181). The total value of U.S. sales of defence articles and services to Taiwan from 2004 to 2007 amounts to \$4.3 billion (Kan, 2014b, p. 1) and in 2008 alone, Bush agreed on an arms sales deal worth more than \$6.4 billion of arms equipment, resulting in the suspension of scheduled military exchanges (Hickey & Zhou, 2010, pp. 145, 154). However, bilateral consultations were already re-established after four months, in February the following year.

The U.S. intentions to continue arms sales to Taiwan are not solely based on the U.S. commitment to help Taiwan defend itself. Next to the economic benefits that accrue from large arms sales to the island, the U.S. government still continues to regard Taiwan as a strategic partner or ‘hedging strategy’ against China in case of unfortunate future occurrences (Hickey & Zhou, 2010, p. 153).¹³

5.2.2. The Taiwan Issue under the Obama Administration

Bush’s general policy approach during his two presidential terms was characterised by confrontation and unilateralism. Compared to this, the approach of the Obama administration proved to be more cooperation-based, yet also less action-prone. Especially in regards to his foreign policy, Obama emphasised his multilateral stance, with certain dominant guidelines: the need of consulting traditional allies as well as seeking a dialogue with enemies before a decision is made or confrontational actions are taken (Yan, 2010, p. 279). Nevertheless, even though Obama differs in his overall presidential performance, the U.S. foreign policy of the Obama administration towards China followed mostly the same path as the Bush administration did. China and the U.S. proceeded to have numerous bilateral meetings – Obama and his then-counterpart Hu Jintao met 12 times during Obama’s first presidential term – and continued to work on significant bilateral and global issues, such as Taiwan and the global economic crisis (Bo, 2010, p. 258; Lawrence, 2013, p. 10). Other issues, such as China’s human rights record, continued to play a minor role in bilateral dialogues. Hillary Clinton, then Secretary of State, stressed: “[O]ur pressing on those issues [Tibet, Taiwan, human rights] can’t interfere with the global economic crisis, the global climate change crisis, and the security crisis” (Dougherty, 2009). In July 2009, Obama implied his hope and

¹³ For a more detailed overview on U.S. arms sales to Taiwan during the Bush administration, please see Appendix A.

willingness to work on establishing “a positive, constructive, and comprehensive relationship” (The White House, 2009a) with China. This statement not only suggests that Obama relies on shared mutual interests as the skeleton for future bilateral relations, but also that he acknowledges the importance of China, as an emerging power. Thus, China already plays and will continue to play a crucial role in international relations in the near future, not only in Asia, but also globally. Recognising China’s importance in world politics signalled a shift in the U.S. perception of China. After the global financial crisis of 2008 the U.S. government stopped regarding China as a developing country. Instead, China was seen from now on as a developed nation, with the obligation to take international responsibility for global issues of economic and international security matters (Yan, 2010, p. 278).

With the foreign policy focus on the fight against terrorism, the U.S. government lost its supremacy in the Asian region. The gap that emerged due to this political shift was gladly filled by China, which expanded its power status in the region during the years of the Iraq and Afghanistan war. However, during his presidential terms Obama enforced the withdrawal of a vast amount of troops from Iraq and Afghanistan and turned the administration’s attention back to the Asian Pacific region. Obama’s administration calls this approach the ‘policy of strategic rebalancing to the Asia-Pacific’. One of the major factors motivating the U.S. to ‘rebalance’ the Asian Pacific regions is of course of economic nature. As then-Secretary of State Clinton stressed in November 2011: “Open markets in Asia provide the United States with unprecedented opportunities for investment, trade, and access to cutting edge technology” (Clinton, 2011). Nevertheless, the U.S. government saw other possibilities of gaining from a rebalance Asian Pacific region: “the desire to shape the development of norms and rules in the Asia-Pacific and [...] to shape China’s choices as a rising power, while offering reassurance to China’s neighbors through intensive U.S. engagement in the region” (Lawrence, 2013, p. 6). The ‘rebalancing strategy’ of the Obama administration caused a tensing up of bilateral U.S.-China relations. Together with Iran, China was categorised as countries which are being likely to “pursue asymmetric means” (Lawrence, 2013, p. 6) in order to work against U.S. endeavours in the region. Moreover, critics comment on two central concept as being problematic in the ‘rebalancing strategy’ of the U.S.: (1) they are apprehensive of antagonising China and anticipate that thereby expectations of U.S. allies will surpass U.S.’ actual intentions of providing military or political support in controversies U.S. allies are having with China; (2) critics of the ‘rebalancing strategy’ consider the strong military presence in the new approach as unnecessarily high and expecting that the high focus

on military power is leading to regional instability instead of balancing the region (Lawrence, 2013, p. 7).

Even though Sino-American relations experienced some tense periods during Obama's two presidential terms, both sides acknowledged the need of bilateral cooperation in times of crises and economic interdependence. In the beginning of his presidential term, China's president Xi has sought to form a 'new model' of bilateral relations between the U.S. and China. After a bilateral meeting with Obama in June 2013, Xi stated:

China and the United States must find a new path – one that is different from the inevitable confrontation and conflict between the major countries of the past. And that is to say the two sides must work together to build a new model of major country relationship based on mutual respect and win-win cooperation (The White House, 2013, n.p.)

Securing the stability of international relations reflects the pressure Xi experiences due to domestic issues, such as uprisings in Hong Kong, domestic corruptions and the slowing down of China's economic growth (Buckley, 2014). Part of the new relationship model is the acceptance of the respective national interests. However, this proves to be challenging for the U.S. government. The PRC has defined its core interests as the following: the maintenance of the Communist Party rule, the protection of China, including its sovereignty and territories such as Taiwan and maritime territories in the South and East China Sea, as well as holding up the economic and social development inside China (Lawrence, 2013, p. 9). In order to respect China's national interests, the U.S. would have to breach bilateral agreements it established with third countries such as Japan or the Philippines, and annul its engagement with Taiwan as stated in the TRA (Lawrence, 2013, p. 9). Building the new model of cooperation with the U.S. had been a major priority of China's foreign policy towards the U.S. ever since. However, as of today a new relations model between the U.S. and China has not been realised.

The Issue of Taiwan's Independence

After Taiwan's controversial president Chen was replaced by Ma Ying-jeou, tensions across the strait diminished. Chen's hostile policy towards China did not only harm the balance of cross-strait relations, but also the U.S.-Taiwan relations. Further, his policy endangered the security environment in East Asia. Opposing his predecessor's approach, Ma started his first

presidential term with reassurances towards China to not pursue Chen's move for independence. In his inauguration speech, Ma pledged a continuation of the 'three-no's' principle – no unification, no independence and no use of force:

I sincerely hope that the two sides of the Taiwan Strait can seize this historic opportunity to achieve peace and co-prosperity. Under the principle of 'no unification, no independence, and no use of force,' as Taiwan's mainstream public opinion holds it, and under the framework of the ROC Constitution, we will maintain the status quo in the Taiwan Strait (Kan, 2014a, p. 83)

Further, Ma emphasised his willingness to expand cross-strait contacts – economically, socially and people-to-people (Sutter, 2012, p. 161). When Ma was inaugurated as Taiwan's president in 2008, Bush still held the presidential position in the U.S. Bush congratulated Ma on his presidential election and pointed out in his congratulation statement: "I believe the election provides a fresh opportunity for both sides of the Taiwan Strait to reach out and engage one another in peacefully resolving their differences" (AIT, 2008, n.p.). In fact, greater economic cross-strait cooperation and integration is said to have had a positive influence on bilateral China-Taiwan relations (Hickey & Zhou, 2010, pp. 147, 150). Since 1992, bilateral cooperation between China and Taiwan takes place through quasi-official entities – the Strait Exchange Foundation (SEF), located in Taipei, and the Association for Relations Across the Taiwan Strait (ARATS), located in Beijing (Kan & Morrison, 2014, p. 6). Starting with Ma's presidential term in 2008 until 2014, the SEF met 10 times and signed 21 cross-strait economic or functional agreements (Kan & Morrison, 2014, p. 7). One of the signed bilateral agreements, established in June 2010, was a free-trade agreement between Taiwan and China, the Economic Cooperation Framework Agreement (ECFA), which "provided privileged access to Chinese markets and other economic benefits for various important constituencies in Taiwan" (Sutter, 2012, p. 161). According to official Taiwanese trade statistics, China ranked first as a trading partner with \$115.39 billion in total trade in 2015, out of which \$71.21 billion accounts for total exports to China and \$44.18 for total imports from China (Bureau of Foreign Trade, 2016). For China, Taiwan ranks as 7th greatest trading partner in 2014 (latest data available), with a total trade value of \$198.31 billion, which accounts for an increase of 6% compared to the previous year (chinadaily, 2015).

In November 2009, Obama repeated Bush's statement that the U.S. policy is based on the three Communiqués as well as the TRA. Additionally, a joint statement of the U.S. and PRC was published the same day, stressing that the U.S. follows the one-China policy: "The

United States stated that it follow its One China policy and abides by the principle of the three U.S.-China Joint Communiqués” (The White House, 2009b, n.p.).

After Ma’s victory in the presidential election in 2008, the issue of Taiwan’s move towards independence had not stirred up cross-strait relations any longer. Ma held up his promise he made in his inauguration speech in 2008 to not pursue Taiwan’s independence, which enabled Taiwan and China to establish a closer cross-strait relationship. As its predecessor, the Obama administration regards the improvement of relations across the strait positively and considers it as important and beneficial for the balance of the region and for all actors involved (Sutter, 2012, pp. 162-163). In a Joint Statement of the U.S. and PRC in 2011, Obama said:

The United States applauded the Economic Cooperation Framework Agreement between the two sides of the Taiwan Strait and welcomes the new lines of communication developing between them. The United States supports the peaceful development of relations across the Taiwan Strait (The White House, 2011, n.p.)

The Issue of Arms Sales to Taiwan

As stated before, the Obama administration, like its predecessor, acknowledges the three signed Communiqués between the U.S. and China as well as the one-China principle with the PRC as China’s sole legal government. Nevertheless, Obama emphasises the importance of the U.S.-Taiwan relationship and the significance of the TRA to form the basis of this relation (Bo, 2010, pp. 263-264; Department of Defense, 2001, p. 61). Even though the Obama administration fails to emphasise Taiwan’s democracy and its democratic values, it has been distinct and determined in its foreign policy towards Taiwan. Obama stated before his presidential inauguration in a letter to Ma on 22 May 2008 that “[...] I will do all I can to support Taiwan’s democracy in the years ahead” (USC US-China Institute, 2008, n.p.).

In its annual report to Congress, the U.S. Department of Defense stated: “Consistent with the TRA, the United States has helped to maintain peace, security, and stability in the Taiwan Strait by providing defense articles and services to enable Taiwan to maintain a sufficient self-defense capability” (Department of Defense, 2015, p. 61). As already stated, the TRA provides the justification to the U.S. to continue arms sales and military support in general to the island. During her Asian trip in 2009, then-Secretary of State Clinton stated that “under the Taiwan Relations Act, there is a clear provision that the United States will provide support for Taiwan’s defense. And that is why there have been, over the many years, the sale

of defensive materials to Taiwan” and that the “[U.S.] policy remains as it has been” (U.S. Department of State, 2009, n.p.).

Besides the obligation to provide defence articles to Taiwan, as stated in the TRA, the U.S. argues that arms sales and military support are vital for Taiwan’s leadership to engage with China, without being intimidated by or helpless against the superior power. As mentioned earlier, the State Department emphasised in its testimony in 2004 that a more secured Taiwan is better capable of interacting politically with China. This argument for continuing arms sales to Taiwan was repeated by Kurt M. Campbell, then-Assistant Secretary in the U.S. Bureau of East Asian and Pacific Affairs, in 2011, stating that

Taiwan must be confident that it has the capacity to resist intimidation and coercion as it continues to engage with the mainland [...] We will continue to strongly stand by our commitment to provide Taiwan with those defense articles and defense services necessary to enable Taiwan to maintain a sufficient self-defense capability (U.S. Department of State, 2011)

As opposed to this security argument by the U.S., the PRC stresses that continuing arms sales to the island is supporting Taiwan’s endeavours for seeking independence from China, which will cause destabilisation in the East Asian region. The Ministry of Foreign Affairs of the People’s Republic of China (MFA) issued the following statement:

[T]he US side still uses the so-called Taiwan Relations Act as an excuse to announce new arms sales to Taiwan [...] This will send a seriously wrong signal to the Taiwan side and the separatist forces aimed at ‘Taiwan independence’ and will gravely impair peace and stability in the Taiwan Strait (MFA, 2010, n.p.)

Moreover, as stated before, selling military equipment to the island contradicts not only with the U.S. acknowledgement of the one-China principle, but it also breaches the U.S. commitments in the Joint Communiqué from 1982, in which the U.S. states to gradually reduce the arms sales to Taiwan until they come to a stop after a period of time (Lawrence, 2013, p. 31).

Nevertheless, the Obama administration approved several arms deals during the eight years in office (see Appendix B and C). In January 2010, the Obama administration authorised an arms sales deal to Taiwan, worth \$6.4 billion. China’s officials reacted strongly to this deal.

Then-Vice Foreign Minister He Yafei stressed that this arms deal seriously breaches the three Joint Communiqués and is again interfering in internal Chinese affairs:

[W]hat the US side is doing constitutes a serious violation of the principles enshrined in the three Sino-US Joint Communiqués [...] and a gross interference in China's internal affairs. It will seriously jeopardize China's national security and undermine China's peaceful reunification. The Chinese side hereby expresses its strong indignation and lodges a stern protest (MFA, 2010, n.p.)

Furthermore, He announced certain sanctions on the U.S. due to its arms sales deal. Those sanctions included postponement of military-to-military contacts, like the Multilateral Arms Control and Non-proliferation, as well as the imposition of sanctions on U.S. companies, which were being involved in the deal (MFA, 2010). However, as of 2013, there were no indications of applied sanctions to U.S. firms by China (Johnston, 2013, p. 16).

The last arms deal between Taiwan and the U.S. was notified to Congress in December 2015, with an estimated value of \$1.83 billion. The deal was resolutely opposed by the PRC again (Reuters, 2015). Vice Foreign Minister Zheng Zeguang emphasised breached regulations by the U.S.:

The arms sale from the US to Taiwan severely violates the international law, the basic norms governing international relations and the principle of the three joint communiqués between China and the US, and severely damages China's sovereignty and security interests (MFA, 2015, p. n.p.)

Additionally, Zheng followed the example from China's 2010 response on U.S. arms sales to Taiwan, stating that sanctions are going to be imposed on U.S. companies selling arms to the island (MFA, 2015). Since no imposition was applied on U.S. enterprises after 2010, this could potentially be the first instance where U.S. firms are sanctioned due to their participation in arms sales to Taiwan.

5.3 Discussion: Economic Interdependence despite Taiwan Issue

The shift of Bush's foreign policy towards China after the terrorist attacks on 9/11 demonstrates the realisation of the U.S. government that it is in need of China's support – not only to fight terrorism, but also to face other international crises, such as the global financial crisis. However, this political reconsideration by the Bush administration also symbolised U.S. national interest in security matters. The need for allies in its war on terror was of

greater interest, than holding up old controversies or adhering to bilateral ties with traditional allies such as Taiwan. Instead, the U.S. government proclaims to establish a “cooperative, constructive, and candid” (Hickey & Zhou, 2010, p. 139) relationship with China.

Nevertheless, the improved bilateral relationship between the U.S. and China was not only developed as a response to 9/11. The Sino-American relationship turned out to be increasingly interdependent, not least because of intensified economic relations. For U.S. exporters, China composes a highly interesting sales market. China’s growing economy, but especially its huge population, which because of globalisation demands more and more international products, form alluring possibilities for U.S. firms. As a result, U.S. exports to China increased from \$19.18 billion in 2001 to \$116.19 billion in 2015, a 506% increase, making China the third largest export market for the U.S. (according to official U.S. statistics¹⁴). Furthermore, China relies on U.S. FDI in the country. Beneficial factors such as comparable low labour costs lead U.S. plants to relocate from their original position, such as Japan or Taiwan, to China (Hickey & Zhou, 2010, p. 142). According to official Chinese statistics, annual U.S. FDI in China accounted to \$2590 million in 2015. Among all countries investing in China, the U.S. ‘only’ ranks 6th, with a share of 2% of total FDI in China (MOFCOM, 2015). Nevertheless, having major U.S. companies relocate to China contributes significantly to Chinese FDI as to its general economy.

China is the largest source of imports for the U.S. As stated by U.S. trade statistics, U.S. imports from China accounted for \$481.88 billion in 2015. The size of the U.S. population together with the great purchasing power makes the U.S. market highly interesting for Chinese exporters. Furthermore, low labour and production costs ensure competitive pricing of Chinese products sold in the U.S. compared to other products available.

Especially in times of the financial crisis, the U.S. became heavily dependent on China in financial matters. China is the number one holder of foreign reserves in the world and also possesses the biggest amount of U.S. Treasury securities. According to U.S. data, China held \$1258 billion in U.S. Treasury securities as of September 2015, which accounts for 20.6% of the total foreign holdings of U.S. Treasury securities.

The investment and trade realities presented in this section demonstrate the immense influence the two economies have on each other. Sino-American relations have become increasingly interdependent in the past 15 years and their economic relationship today is more interwoven as it has ever been.

¹⁴ Source: United States Census Bureau, 2015

The close economic interaction between the U.S. and China also influences mutual interests in other areas as well as global challenges that need the attention of both countries. Sino-American cooperation is inter alia needed on energy security and climate change, collaboration to tackle the financial and economic crisis, contain the spread of nuclear weapons, and confront transnational menaces (Bo, 2010, p. 258). On this account, bilateral dialogue between the two actors increased steadily. In Obama's first presidential term alone, he met with his Chinese counterpart Hu Jintao 12 times. Moreover, a great example of bilateral communication mechanisms between the U.S. and China is the in 2006 initiated S&ED. During this dialogue, which is held two times a year, both countries have the opportunity to bring topics of agitation concerning economic relations and trade on the agenda, which then can be discussed with the aim of finding a common solution. It had been confirmed by both parties, that "the mechanism had become an effective framework to resolve disputes and react to challenges in the rapidly growing bilateral trade and investment" (Hickey & Zhou, 2010, p. 143). Not only bilateral communication increased, also multinational and international communication and cooperation intensified on platforms such as the Asian-Pacific Economy Cooperation (APEC), G20, G8 + Summit and the Association of Southeast Asian Nations (ASEAN) +3 Summit (Hickey & Zhou, 2010, p. 143). Those established communication channels, caused by greater economic interdependence, represent the concept of multiple channels in complex interdependence among states, introduced by Keohane and Nye (1989).

Even though China-U.S. relations show certain aspects of neoliberal institutionalism and complex interdependence, as elucidated upon before, the two states still act in ways described by defensive as well as offensive realism. First of all, there is the matter of balancing power in the East Asian region. After the two wars in the Middle East mitigated in 2009, the Obama administration decided to place more focus on its 'rebalancing strategy' in East Asia. Dominant or superior powers, as in this case the U.S.¹⁵, try to prevent other great powers from reaching regional hegemony and surpassing the actual hegemon. In this case, China was able to rise in power and influence in East Asia, because the U.S. was too occupied with fighting terrorism than being able to hold its old power position. However, when the war in the Middle East winded down, the U.S. saw the possibility to regain its superior position in

¹⁵ Robert O. Keohane (1984) describes the U.S. in his work *After Hegemony* as a dominant power in world politics.

the East Asian region. According to offensive realism, states will seek to accumulate as much power as possible and by that challenge the existing status quo.

The continuation of arms deals with Taiwan is not solely caused by U.S. obligations stated in the TRA, but is also hold up in order to ensure the balance of power in the East Asian region, where Taiwan is an important partner for the U.S. Moreover, as the TRA states, the arms sales to Taiwan shall not exceed the level of threat posed by China and other surrounding states. Maximising power only to the point where a state has the power to defend itself, but not seeking to further accumulate power, is one concept introduced by defensive realism. In defensive realism, the “avoidance of change can be defined as maintenance of the status quo or the balance of power” (Blazevic, 2010, p. 147).

China’s efforts of reaching reunification with Taiwan can be accounted to maximise its power in the region and internationally. However, the continuation of U.S. arms sales to the island is seen as a threat to those endeavours by Chinese officials. The TRA, which is forming the basis of U.S.-Taiwan relations, states the U.S. commitment of helping Taiwan to defend itself. Here, the defending principle of the TRA is especially emphasised – delivered weaponry should only be of defensive nature and be in accordance to threats by surrounding states – a typical defensive realism example. Though, the PRC argues that arms deals from the U.S. to Taiwan is destabilising the region and endangering cross-strait relations as well as China’s national interest to reunify with Taiwan. Thus, arms sold to Taiwan are not only of defensive character. Especially sold fighters, as those of the F-16 type, are offensive in nature. China fears that the sale of weaponry is empowering Taiwan to a point where the ROC is confident enough to seek independence from China again, as former President Chen did. To this end, China continues maximising its own power in order to maintain the superior power relation between China and Taiwan. This is where Waltz (1979) saw the problem with maximising power above the amount needed for securing the state (p.126). Due to China’s ongoing power maximisation, Taiwan feels increasingly threatened and attempts to further boost its own power. Moreover, Taiwan’s fear for survival is mirrored in its endeavours to form a coalition with the U.S. As Waltz (1979) elucidated, if a state is threatened by a greater power and its own power maximisation is not sufficient enough to secure the state’s survival, the weaker state will seek to join a coalition with either a union of weaker states or a greater power (p.127).

The issue of Taiwan continued to constitute a major irritant in Sino-American relations of the past 15 years. Even though the relationship between the U.S. and the island were problematic during the presidential administration of Chen from 2000 to 2008, Bush held on to the traditional ties between the two countries, demonstrated by, inter alia, the continuation of arms sales to Taiwan. Chen's foreign policy did not only rock bilateral relations between the U.S. and Taiwan, but made cross-strait relations even more critical and dangerous than they already had been. With Taiwan's new president Ma, relations with the U.S. as well as with China started to improve. The implementation of a number of economic policies by the Ma administration (Hickey & Zhou, 2010, p. 148) leads to stronger cross-strait cooperation in trade and investment matters and the two traditional opponents became more interdependent. This improvement also holds benefits for U.S.-China relations. With closer China-Taiwan relations, the possibility of provoking the PRC when cooperating with the Taiwanese government, decreased substantially for the Obama administration. Consequentially, China and the U.S. were in a position to improve their bilateral relations, especially in the economic sector, without having to be largely apprehensive about how relations with Taiwan might influence these. Nevertheless, the continued arms sales to the island remain to be a red rag for China.

6.0 Conclusion

This thesis aimed at analysing the Sino-American relationship in the first 15 years of the 21st century in order to answer the following research questions:

What are the characteristics of U.S.-China relations in the first 15 years of the 21st century?

How have relations been influenced by economic interdependence and the Taiwan issue?

Why has economic interdependence between the U.S. and China been deepened in spite of the geopolitical competition over the Taiwan issue?

In order to answer the three interlinked research questions, major theories of international relations are applied. The neoliberal institutionalism as well as complex interdependence is utilised in order to analyse the economic interdependence between the U.S. and China. In order to evaluate the influence that the Taiwan issue and the relationship between the U.S.

and Taiwan has on Sino-American relations, neorealism and its subgroups defensive realism, introduced by Waltz, and offensive realism, introduced by Mearsheimer, are applied.

During the last 15 years, the bilateral relationship between the U.S. and China had not been one of stable nature. Influenced by significant differences in fundamental norms and values, cooperation proved to be difficult before the Bush administration took term in 2001. The U.S. shift of foreign policy towards China was caused by the terrorist attacks of 9/11. Focusing on the fight against terrorism, but also facing several global crises, such as the financial crisis and climate change, the U.S. found itself in need of greater cooperation with China, a rising power with the world's second largest economy. Furthermore, mutual interests in international affairs boosted bilateral cooperation between the U.S. and China. As a result, relations between the two great powers became more and more intertwined, especially in the economic area.

Bilateral trade between China and the U.S. increased significantly since 2001: As of today, China is the largest source of imports for the U.S. and the third largest market for U.S. exports. According to official Chinese statistics, the total trade of goods increased from \$80.48 billion in 2001 to \$520.75 billion in 2013, thus a growth by 6.5 times. Official U.S. data sets however published a different set of numbers, which is calculating that total trade of goods between China and the U.S. grew from \$121.46 billion in 2001 to \$562.16 billion in 2013. Following official U.S. trade data, imports from China in 2015 accounted for 80.6% of the total trade (\$481.88 billion), thus exports to China only account for 19.4% of the total trade (\$116.19 billion). This immense difference in exports and imports creates a trade balance deficit for the U.S. Since 2001, the U.S. trade balance deficit increased from \$-83.10 billion to \$-365.70 billion. The rising trade deficit negatively affects the U.S. household debt. The vast amount of U.S. debt is being held by China. Ranking number one in foreign debt holding countries, China holds \$1244.3 billion of U.S. Treasury securities in 2014. The accumulated amount of U.S. Treasury securities by China worries policymakers and economic analysts. They fear that it constitutes a leverage for China and enables the country to influence e.g. foreign policy making to its benefit by threatening to sell a great share of its holdings otherwise. This argument, criticising the immense holdings of U.S. Treasury securities, can however also discount the criticism: Besides harming its own export-driven economy, by damaging its biggest export market, selling a vast amount of debt security could result in a depreciation of the USD, leading to a decreased value of the remaining debt securities held by China. Therefore, selling U.S. Treasury securities would hurt China's

economy just as much as it would hurt the U.S. economy. This example alone greatly demonstrates the interconnectedness of the two economies and how dependent the one economy is on the well-being of the other economy.

As Sino-American trade relations improve, bilateral communication of the two countries increases. For economic matters, two forums for discussion had been established – the JCCT and the S&ED. Those forums give room to discuss controversial matters and settle debates. If, however, the respective representatives find themselves unable to resolve discrepancies, both countries have the option to bring it as a case in front of the WTO, of which China is a member since 2001. The multiple channels of communication as well as the WTO as an international institution, governing international relations by providing a set of rules, represent core aspects and concepts of neoliberalism as well as complex interdependence.

The terrorist attacks of 9/11 constitute a turning point of the foreign policy towards China by the Bush administration. During his first ten months in office, Bush followed a ‘hard-line policy’ against China, moving away from Clinton’s and Jiang’s efforts of establishing a ‘constructive strategic partnership’. According to the Bush administration, China is seeking to shift the balance of power in its own favour, which would make it a ‘strategic competitor’, not a potential partner. This attempt to change the status quo in the East Asian region represents the idea of power maximisation in offensive realism. However, due to the enhanced focus of the U.S. to fight terrorism, China was able to rise peacefully in East Asia and fill the power gap, which emerged due to the shift in U.S. foreign policy. Only after President Obama withdrew a vast amount of U.S. troops from Afghanistan and Iraq, the focus of U.S. foreign policy turned back to the Asian Pacific region. The stimulus of adopting the ‘policy of strategic rebalancing to the Asia-Pacific’ was not solely of economic nature. Instead, the Obama administration saw the possibility of shaping China’s political choices and conveys a feeling of reassurance to China’s neighbours by deploying U.S. military forces in the region. The aim of gaining back its old power status in the East Asian region, demonstrates the offensive realism concept that states will seek to accumulate as much power as possible and by that challenge the existing status quo.

The Bush and Obama administration were both distinct and determined in their policy towards Taiwan. Both presidential administrations stated their recognition of the one-China principle, as stated in the three Joint Communiqués, but also acknowledge the TRA as the guiding principle in their relations with the island. The TRA clearly states the U.S. commitment to help Taiwan defend itself, to which end the U.S. is selling weaponry to the

island. Nevertheless, the emphasis is on the defensive character of bilateral U.S.-Taiwan relations. First of all, the arms being sold to Taiwan should be of defensive nature. Second, the arms sales should be in conformity with the potential threat, exerted by Taiwan's surrounding states. The defensive character of U.S.-Taiwan military cooperation demonstrates the core concept of defensive realism. According to Waltz (1979), states seek to accumulate security. Maximising security is obtained by the maximisation of power. However, once the state can ensure its survival, it will stop accumulating power.

China's typical reaction towards U.S. repeated arms sales to Taiwan are of adverse nature. One of China's core national interests is the reunification with Taiwan, which the PRC perceived as of being in danger due to the arms deals. Furthermore, China's officials imply the continuation of arms sales to Taiwan will lead to a destabilisation of the East Asian region and endanger cross-strait relations. In order to pursue its national interest to be reunified with Taiwan, China continues maximising its own power and by that also maintaining the bilateral power relations with Taiwan. Additionally, China is criticising the types of weaponry which are being sold to Taiwan. Especially F-type fighters are causing disputes because, according to the PRC, those fighters are of offensive rather than defensive nature.

The Taiwan issue and particularly the U.S. arms sales to Taiwan are a major irritant in Sino-American relations. However, with the inauguration of Taiwan's president Ma in 2008, China-Taiwan relations started to improve. Greater cross-strait cooperation, especially in the area trade and investment, led to an increased interdependency between China and Taiwan. These improved ties also hold benefits for U.S.-China relations. Especially economic relations between the U.S. and China were strengthened with a more balanced relationship across the strait. Additionally Sino-American relations are less likely to face major setbacks due to U.S. interferences in China-Taiwan disputes.

In a nutshell, increased economic interdependence between China and Taiwan as well as China and the U.S. was able to promote appeasement between the three parties. Nevertheless, each state has its core national interest, which will not be subject of alterations. The PRC sees Taiwan as an inalienable part of China. The U.S. will defend its allies, like Taiwan, and will not accept threats against those by external forces, especially from China. Taiwan will not agree to any reunification efforts by China.

Appendix

Appendix A: U.S. Arms Sales to Taiwan – Bush Administration

Source: Kan, S. A., 2014b. *Taiwan: Major U.S. Arms Sales Since 1990*, Washington: Congressional Research Service.

Year	Date of Notification	Major Item or Service as Proposed (Usually Part of a Program with Related Support)	Value of Program (\$ million)
2001	18 July	(50) Joint Tactical Information Distribution Systems (JTIDS) terminals (a version of Link 16) for data links between aircraft, ships, and ground stations	\$725
	05 September	(40) AGM-65G Maverick air-to-ground missiles for F-16s	\$18
	26 October	(40) Javelin anti-tank missile systems and (360) Javelin missiles	\$51
	30 October	Logistical support/spare parts for F-5E/F, C-130H, F-16A/B, and IDF aircraft	\$288
2002	04 June	(3) AN/MPN-14 air traffic control radars	\$108
	04 September	(54) AAV7A1 amphibious assault vehicles	\$250
	04 September	Maintenance and spare parts for aircraft, radars, AMRAAMS, other systems	\$174
	04 September	(182) AIM-9M-1/2 Sidewinder air-to-air missiles	\$36
	04 September	(449) AGM-114M3 Hellfire II anti-armour missiles to equip AH-1W and OH- 58D helicopters	\$60
	11 October	(290) TOW-2B anti-tank missiles	\$18
	21 November	(4) Kidd-class destroyers	\$875
2003	24 September	Multi-functional Information Distribution Systems (MIDS) (for Po Sheng)	\$775
2004	30 March	(2) Ultra High Frequency Long Range Early Warning Radars	\$1,776
2005	25 October	(10) AIM-9M Sidewinder and (5) AIM-7M Sparrow air-to-air missiles; continued pilot training and logistical support for F-16 fighters at Luke AFB	\$280
2007	28 February	(218) AMRAAMs and (235) Maverick air-to-ground missiles for F-16 fighters	\$421
	08 August	(60) AGM-84L Harpoon Block II anti-ship missiles	\$125
	12 September	(144) SM-2 Block IIIA Standard air-defence missiles for Kidd-class destroyers	\$272
	12 September	(12) P-3C maritime patrol/ASW aircraft	\$1,960
	09 November	Patriot configuration 2 ground systems upgrade	\$939
2008	03 October	(330) Patriot Advanced Capability (PAC)-3	\$3,100

		missile defence missiles	
	03 October	(32) UGM-84L sub-launched Harpoon anti-ship missiles	\$200
	03 October	spare parts for F-5E/F, C-130H, F-16A/B, IDF aircraft	\$334
	03 October	(182) Javelin anti-armour missiles	\$47
	03 October	upgrade of (4) E-2T aircraft (Hawkeye 2000 configuration)	\$250
	03 October	(30) AH-64D Apache Longbow attack helicopters, (173) Stinger air-to-air missiles, (1,000) AGM-114L Longbow Hellfire missiles	\$2,532

Appendix B: U.S. Arms Sales to Taiwan – Obama Administration

Source: Kan, S. A., 2014b. *Taiwan: Major U.S. Arms Sales Since 1990*, Washington: Congressional Research Service.

Year	Date of Notification	Major Item or Service as Proposed (Usually Part of a Program with Related Support)	Value of Program (\$ million)
2010	29 January	(114) PAC-3 missile defence missiles	\$2,810
	29 January	(60) UH-60M Black Hawk utility helicopters	\$3,100
	29 January	(12) Harpoon Block II anti-ship telemetry (training) missiles	\$37
	29 January	(60) MIDS (follow-on technical support for Po Sheng C4 systems)	\$340
	29 January	(2) Osprey-class mine hunting ships (refurbished and upgraded)	\$105
2011	21 September	Retrofit of 145 F-16A/B fighters, with 176 AESA radars, JDAMs, etc.	\$5,300
	21 September	Continuation of training of F-16 pilots at Luke Air Force Base	\$500
	21 September	Spare parts for F-16A/B, F-5E/F, C-130H, and IDF aircraft	\$52

Appendix C: Latest U.S. Arms Sale to Taiwan

Source: U.S. Federal register, *Arms Sales Notification*, 36(b)(1), 2016

Year	Date of Notification	Major Item or Service as Proposed (Usually Part of a Program with Related Support)	Value of Program (\$ million)
2015	16 December	208 Javelin Guided Missiles, etc.	\$57
	16 December	4 Multifunctional Information Distribution Systems (MIDS) On Ship Low Volume Terminals (LVTs); 4 Command and Control Processor (C2P) units, etc.	\$75
	16 December	769 TOW 2B Aero, Radio Frequency (RF) Missiles (BGM-71F-Series) ; 14 TOW 2B Aero, Radio Frequency (RF) (BGM-71F-Series) Fly-to-Buy Missiles ; 46 Improved Target Acquisition System (ITAS) ; 4 ITAS spares, etc.	\$268
	16 December	13 MK 15 Phalanx Block 1B Baseline 2 Close-in Weapons System (CIWS) Guns; 8 CIWS Block 1 Baseline 0 to Block 1B Baseline 2 upgrade kits; 260,000 Rounds of 20mm MK 244 MOD 0 Armour-Piercing Discarding Sabots (APDS)	\$416
	16 December	The sale, refurbishment, and upgrade of 2 Oliver Hazard Perry-class frigates (FFG-7) being provided as Excess Defence Articles (EDA).	\$190
	16 December	250 Block I -92F MANPAD Stinger Missiles; 4 Block I -92F MANPAD Stinger Fly-to-Buy Missiles, etc.	\$217
	16 December	36 Assault Amphibious Vehicles(AAVs); 30 .50 Calibre M2 machine guns; 6 7.62mm M240 machine guns	\$375
	16 December	Follow-on life cycle support to maintain the Multifunctional Information Distribution Systems Low Volume Terminals (MIDS/LVT-1) & Joint Tactical Information Distribution Systems (JTIDS)	\$120
	16 December	unspecified minesweepers in a direct commercial sale	\$108 ¹⁶

¹⁶ This data information was retrieved from the U.S. Naval Institute, 2015

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