

# A NEOLIBERAL INSTITUTIONALIST APPROACH TO THE MODERN VIETNAM-CHINA MARITIME DISPUTE

---

*Hoang-Anh Nguyen*

Vietnam National University, Hanoi

*Hong-Van Tran*

National Economics University

*The recent escalation of the territorial dispute in the South China Sea between Vietnam and China has received increasing international attention. Being economically, politically and militarily inferior to China, Vietnam has met challenges while raising its voice against China's actions. In this paper, the authors will use the neoliberal institutionalism approach in international relations to analyze Vietnam's current situation, address the causes of the problems, and seek possible solutions for the Vietnamese government.*

Recently, considerable attention has been paid to the disputes over maritime territories in the South China Sea, especially the dispute between China and Vietnam over two island groups known in English as the Paracel Islands and the Spratly Islands, in Vietnamese as the Hoang Sa and the Truong Sa, and in Chinese as the Xisha and the Nansha. The fact is that a historical review reveals that this territorial quarrel took root many years ago.<sup>1</sup> However, rela-

---

1 The origin of this dispute between these two countries can be traced back to 1956, when sovereignty of the Paracel Islands and the Spratly Islands fell to South Vietnam replacing the French according to the Geneva Agreements. China has politically and diplomatically condemned the decision and reaffirmed their control over the islands. China then gained control over the entire Paracel Islands after a battle with Republic of Vietnam Navy on January 19, 1974, and gained control over a proportion of the Spratly Islands after confrontation with Vietnam People's Navy in 1988. For more information on the history of this dispute, see Min Gyo Koo, "The Island and Maritime Disputes in the South China Sea," in *Island Disputes and Maritime Regime Building in East Asia: Between a Rock and a Hard Place* (New York: Springer New York, 2010), 137-66; and Leszek Buszynski, "The development of the South China Sea maritime dispute," *National Security College Occasional Paper*, no. 5 (September, 2013): 3-7.

tions have in recent times turned remarkably chillier after the state-owned China National Offshore Oil Corporation (CNOOC) placed its deep sea-drilling rig Haiyang Shiyou 981 (HD-981) in disputed waters south of the Paracel Islands on May 2, 2014. Although Vietnam bitterly denounced this move and claimed that the drilling rig was located within its 200-nautical-mile exclusive economic zone (EEZ) according to United Nations Convention on Law of the Sea (UNCLOS), China responded by sending a large flotilla of ships to protect the rig as well as declaring that it “has irrefutable sovereignty over the Paracel Islands and maritime territories in its Exclusive Economic Zone.”<sup>2</sup> Tensions severely flared up after Chinese boats repeatedly rammed and attacked Vietnamese ones with water cannons, which consequently led to several anti-Chinese protests and two violent riots against foreign-owned factories in Vietnam. The Haiyang Shiyou 981 stand-off ended with China announcing that the oil platform had completed its commercial exploration operations and would be withdrawing it on July 15, 2014; nevertheless, Vietnam and other claimants did not expect that China would scale back their increasing ambitions in South China Sea expansion as it had published a new map reinforcing territorial claim over the region.<sup>3</sup> For them now, seeking a peaceful solution to the dispute is crucially important.

The South China Sea is a semi-enclosed area of approximately 3.5 million square kilometers extending from the Singapore and Malacca Straits to the Strait of Taiwan. It was not by chance that many countries have overlapping territorial claims to these waters, as well as to some of the islands and rocky outcrops in them such as the Paracels and the Spratly Islands. The main driver is the search by all nations for natural resources to fuel economic growth, in this case oil, natural gas, minerals, and fish.<sup>4</sup> Fossil fuel obviously plays an important role in the economic development of China – the emerging superpower of Asia – as well as other developing countries such as Vietnam and the Philippines. Recent political instability in the Middle East has in particular raised concerns about the availability of oil for economic development and, as a result, prompted East Asian and South-

---

2 Mark C. Eades, “Why China Is Angry About a Game of Beach Volleyball,” *U.S. News*, June 10, 2014, <http://www.usnews.com/opinion/blogs/world-report/2014/0610/china-is-angry-at-vietnam-and-the-philippines-volleyball-dilomacy>, (accessed November 10, 2014).

3 Michelle FlorCruz, “China’s New Vertical Map Gives Extra Play To Disputed South China Sea Territories,” *International Business Times*, June 25, 2014, <http://www.ibtimes.com/chinas-new-vertical-map-gives-extra-play-disputed-south-china-sea-territories-1611550> (accessed November 10, 2014).

4 Fraser Cameron, “South China Sea Background Note,” *EU-ASIAN Centre (2013): 1*, [http://www.eu-asiacentre.eu/pub\\_details.php?pub\\_id=112](http://www.eu-asiacentre.eu/pub_details.php?pub_id=112) (accessed November 10, 2014).

east Asian states to turn to the sea for their energy needs. In addition, according to studies conducted by the Department of Environment and Natural Resources of Philippines, the South China Sea holds one third of the entire world's marine biodiversity thereby making it a very important area not only for the ecosystem but also for fishermen and the fishing industry of surrounding nations. Quite apart from that, worry about the infringement of maritime security and free transit of maritime commerce through those waters has contributed to the focus of international attention on this chronic dispute.<sup>5, 6, 7, 8</sup>

Having already acknowledged the historical, economic, and security significance of the two island groups in dispute, the Vietnamese government immediately implemented some measures, but their efforts have met challenges. On the sea, Vietnamese ships sent to call for the withdrawal of the drilling rig HD-981 from the disputed waters was attacked and China continuously warned Vietnam off "harassing Chinese ships".<sup>9</sup> On the other hand, a group of Vietnamese citizens, mostly young people and nationalists, are criticizing the government for perceived soft policies and urging more drastic action. The Vietnamese government therefore finds itself in a delicate situation where harsh moves can exacerbate the conflict but where limited action will lead to inaction on the part of China and criticism from its citizens.

However, to the authors' best knowledge, scholarly literature encompassing this particular issue is very limited. The Haiyang Shiyou 981 stand-off is the worst maritime conflict between these two countries in the last twenty-five years, since 1988 when China fiercely took control of some rocks and sandbanks of the Spratly Islands by military force.<sup>10</sup> The sudden aggravation of the dispute is unexpected not only to governments and international organizations but also researchers. Moreover, as of November 2014,

---

5 Mark Landler, "Offering to Aid Talks, U.S. Challenges China on Disputed Islands," *The New York Times*, July 23, 2010, <http://www.nytimes.com/2010/07/24/world/asia/24dipl.html> (accessed November 10, 2014).

6 Zachary Keck, "India Wades Into South China Sea Dispute," *The Diplomat*, March 12, 2014, <http://thediplomat.com/2014/03/india-wades-into-south-china-sea-dispute> (accessed November 10, 2014).

7 Ian Storey, "Japan's maritime security interests in Southeast Asia and the South China Sea dispute," *Political Science* 65, no. 2 (2013): 135–56, doi:10.1177/0032318713508482 (accessed November 10, 2014).

8 General Secretariat of EU, "Guidelines on the EU's Foreign and Security Policy in East Asia" (paper presented at the meeting for the Council Of The European Union, Brussels, June 15, 2012).

9 "China warns Vietnam over stand-off in South China Sea," *BBC*, May 8, 2014, <http://www.bbc.com/news/world-asia-27332723> (accessed November 10, 2014).

10 Min Gyo Koo, *Island Disputes and Maritime Regime Building in East Asia: Between a Rock and a Hard Place* (New York: Springer New York, 2010), 153-54.

with the most recent standoff just recently concluded, it is understandable that few relevant scholarly studies have yet been published. Therefore, the objective of this paper is to discuss new problems with which Vietnamese government have to deal in present time and suggest some possible solutions. The authors will tackle these tasks using neoliberal institutionalism approach developed by Robert Keohane, Joseph Nye, and other scholars.

### **Dependent and Interdependent Relationship in a Territorial Dispute**

The policy of Vietnamese government on settling territorial dispute over the Paracel Islands is quite controversial among the Vietnamese citizenry. Prime Minister Nguyen Tan Dung stated in his speech at the National Assembly meeting on June 11, 2014: “Vietnam keep consistent stance is that the disputed islands belongs to its sovereignty. We have sufficient evidence and legal history to confirm this. But Vietnam advocates negotiation and peaceful means to settle claims over the Paracel Islands.”<sup>11</sup> In harmony with his speech, Vietnam has only sent non-military ships to the disputed waters in order to call for Chinese adherence to international law. The Vietnamese government has also continuously publicly condemned China for its actions in the South China Sea as a way to put China under international pressure. However, this approach did not in fact have a big impact on Chinese behavior. Some Vietnamese as well as foreign scholars believe that Vietnam should sue China at the International Court of Justice if it really wants the dispute settled.<sup>12</sup> The fact that the Philippines has already filed a lawsuit in January 2014 in regards to the South China Sea dispute to challenge China before a UN court at The Hague<sup>13</sup> makes this a plausible move, but the attitude of the Vietnamese government seemed unchangeable. The way governments deal with the dispute will clearly become a topic for consideration by statesmen and researchers in the future. Nonetheless, to the extent of the analysis on this paper, the authors will not try to answer the question “Which dispute settlement policies are better for the Vietnamese government to carry out?” but to the discuss new problems they have to face in the present which could potentially limit their policy choice.

---

11 Le Phux, “The best way to solve the sovereignty dispute,” *VietNamNet Bridge*, June 21, 2014, <http://english.vietnamnet.vn/fms/government/105309/the-best-way-to-solve-the-sovereignty-dispute.html> (accessed December 11 2014).

12 “Vietnam should sue China, say scholars,” *VietNamNet Bridge*, June 22, 2014, <http://english.vietnamnet.vn/fms/government/105421/vietnam-should-sue-china-say-scholars.html>.

13 “Philippines files case to UN in South China Sea dispute,” *BBC*, March 31, 2014, <http://www.bbc.com/news/world-asia-26781682> (accessed November 10, 2014).

International relations theory analyses relative influence. This influence can be considered as a countries' power. In the traditional view of power, military strength has widely been deemed to be the primary means by which one state gains relative power over another. This view has been criticized by neoliberal institutionalists for its lack of ability to explain the relations between countries in the modern world.<sup>14</sup> They argued that power can be military coercion or it can be the ability to control outcomes. According to Robert O. Keohane, interstate power arises not out of the possession of coercive power resources, but from the asymmetric interdependence in specific issues.<sup>15</sup>

Keohane has developed a new concept of interstate power source – asymmetries interdependence whereby less dependent actors in an interdependent relationship can use their position to influence others. This concept is extremely useful in analyzing the maritime dispute between Vietnam and China. Dependence can be defined as a situation in which a system is contingent on external forces. In contrast, interdependence describes a situation of mutual dependence between social actors which involve state actors and non-state actors.<sup>16</sup> The battle of the Paracel Islands in 1974 between the naval forces of the People's Republic of China and Republic of Vietnam (South Vietnam) is an appropriate example in analyzing the effect of interdependence on state behavior. In 1974, the Democratic Republic of Vietnam (North Vietnam) was still engaged in war with the South. It therefore needed support, mainly from the Soviet Union and China, particularly after decades of heavy bombings by the United States that led to severe damage to the North Vietnamese economy. Exploiting the situation, China completely took control over the Paracel Islands following naval combat with the Republic of Vietnam Navy on January 19, 1974. North Vietnam's government, however, of course did not want to worsen their relationship with ally the Chinese and simply did nothing to publicly oppose Chinese action. This example therefore exhibits how a country's behavior can be affected by its dependency on the other.

---

14 Keohane and Nye have given some examples of countries in the modern world and argued that military power did not provide good explanations for the nature of international regimes. For more information, see Robert O. Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, 3<sup>rd</sup> ed. (New York: Longman, 2001), 115.

15 Helen V. Milner and Andrew Moravcsik, eds., *Power, Interdependence, and Nonstate Actors in World Politics* (Princeton: Princeton University Press, 2009), 249.

16 Walter Carlsnaes, Thomas Risse and Beth A Simmons, eds., *Handbook of International Relations* (London: SAGE publications Ltd, 2013), 402.

Keohane argued that interdependence “might be symmetrical, as in the case of Germany and France; it might be asymmetrical, as in the case of the United States and Guatemala.”<sup>17</sup> And only in the asymmetrical case, could a country take advantage of its resources or the needs of the other to influence the latter’s behavior. In other words, the country having relatively more resources or relatively less need will have the ability to exert greater power. Ariel Rubinstein has modeled this situation in a study on game theory. As he proved, when two people are trying to reach an agreement on how to divide a pie, the one with a lower fixed bargaining cost in each period will gain the whole pie.<sup>18</sup> In the North Vietnam case, its immediate needs for China’s economic and political support during the Vietnam War led to its relatively weaker position preventing it from making any response which could have an adverse impact on the bilateral relationship.

Similarly, Vietnam’s economic dependence on China may be the primary reason deterring Vietnamese government action in the present. It is no longer just about using military force to repel Chinese incursions into disputed areas as some Vietnamese nationalists call for as even the denunciation of Chinese claims to the area and appeals for help from the international community can be difficult to politically justify under threat of economic retaliation from China. Until now, no quantitative study has been conducted to determine the extent to which Chinese retaliation might harm the Vietnamese economy given the level of economic dependence. Nevertheless, a simple assumption may be made realizing that the reliance is far enough developed to case the Vietnamese economy to suffer from Chinese retaliation.

In the period of 2000-2013, Vietnam’s exports to China accounted for approximately 10 percent of Vietnam’s total exports, while import had increased from 10 to 28 percent in the same period.<sup>19</sup> According to the General Statistics Office of Vietnam, Vietnam’s exports to China in 2013 was \$13 billion while imports reached \$37 billion. China’s imports from Vietnam are mainly agricultural, forestry, and fishery products whereas Vietnam’s imports from China are primarily mechanical, chemical, and input materials for the local garment and textile sector. Deputy Chairman of the Vietnamese Na-

---

17 Robert Keohane *Interview: Conversations with History, Institute of International Studies, UC Berkeley, 2004, 5.*

18 Ariel Rubinstein, “Perfect equilibrium in a bargaining model,” *Econometrica* 50, no. 1 (January, 1982).

19 General Department of Vietnam Customs, *Statistical Data on Exports and Imports of Vietnam (2000-2013)*; and *International Monetary Fund, Statistics Dept, Direction of Trade Statistics Yearbook (2000-2013).*

tional Assembly's Committee on Economic Affairs Mai Xuan Hung has made it clear that "about 80 percent of Vietnam's input materials are imported from China and 60 percent of agricultural exports are sold to China."<sup>20</sup> This would obviously pose a problem to Vietnam's economic development if trade from China was interrupted. This situation would not be reflected in China considering the fact that exports to and imports from Vietnam accounted for a very small proportion of its economy. In 2012, China's export and import ratio with Vietnam was only 1.49 and 1.13 percent respectively.<sup>21</sup>

China is currently the largest Engineering, Procurement, and Construction (EPC) contractor in Vietnam. According to the Vietnamese National Assembly's Committee on Financial and Budgetary Affairs 90 percent of EPC contracts, among them thirty of Vietnam's national key projects, were implemented by Chinese enterprises through 2010.<sup>22</sup> In a report of Vietnam National Research Institute of Mechanical Engineering published in April 2014, Chinese contractors were found to have been assigned to deliver EPC contracts for five out of the country's six chemical projects, both of its mineral processing projects, forty-nine of its sixty-two cement projects, and sixteen of twenty-seven thermal power projects. The impact of dependence on China in this field is clearly visible at a construction site in southwestern Hanoi, where a construction of a train line involving Chinese companies has been suspended since May 2014.

However, more concerning is that Chinese contractors prefer to use Chinese equipment and workers,<sup>23</sup> which not only contributes little to local human resource development but also causes technology dependence on China. In some projects funded by Chinese aid, using Chinese technology, equipment and services is a condition attached to concessional loans. But in other projects, Chinese contractors simply enjoy the cheap price of their country's technology.<sup>24</sup> What follows is that most of technology implemented in national projects in Vietnam is Chinese. The problem is that the cheap

---

20 Le Chau, "Our economy and the South China Sea: Effort to overcome challenges," *VnEconomy*, May 26, 2014, <http://vneconomy.vn/thoi-su/kinh-te-va-bien-dong-du-noi-vuot-qua-thach-thuc-20140526025656131.htm> (accessed December 10, 2014).

21 The Observatory of Economic Complexity, *Exchange Statistics about China (2012)*.

22 "From the incident of EVN to the lesson awakening the dependence on Chinese contractors," *Finance*, June 16, 2014, <http://tapchitaichinh.vn/Kinh-te-dau-tu/Tu-su-co-cua-EVN-va-bai-hoc-canhtinh-viec-le-thuoc-nha-thau-Trung-Quoc/50315.tctc> (accessed December 10, 2014).

23 Le Hong Hiep, "The rise of Chinese contractors in Vietnam," *East Asia Forum*, March 14, 2013, <http://www.eastasiaforum.org/2013/03/14/chinese-contractors-rise-in-vietnam-causes-problems-and-implications> (accessed November 10, 2014).

24 *Ibid.*

technology they use is usually out-of-date and costly to operate, which raises serious concerns for statesmen.<sup>25</sup> In fact, there were already some incidents involving Chinese equipment in national projects,<sup>26</sup> the most well-known instance involved two 900 MVA transformers installed at the Hiep Hoa transformer station in Bac Giang Province breaking down within one week of service, leading outages in eight northern provinces.<sup>27</sup> The replacement of such devices with complementary units in a unified system, nevertheless, is daunting and results in reluctance on the part of Vietnamese managers who do not usually proactively replace units until they have broken down. Therefore, Vietnam will obviously have to live with Chinese technology for a long time. This brings on worry about national security, especially with regards to energy security. While Chinese contractors are constructing most of power plants of Vietnam, Vietnam Electricity (EVN) is still contractually obliged to import electricity from China at high rates limiting the purchase of electricity low rate energy produced from domestic hydropower plants.<sup>28</sup> Due to the monopoly of EVN on the Vietnamese electricity market, domestic power plants are hard pressed to find other buyers and are therefore running at only around 70 to 80 percent of their full capacity.<sup>29</sup> This has, as a result, posed a real risk for the energy security as well as hindered the development of the domestic power sector. The technology dependence has another dangerous aspect involving malicious features embedded on Chinese chips, which have been acknowledged to exist by Vietnamese security experts and the local public media.<sup>30</sup>

Although there are other explanations, the reason for the existence of this heavy dependence can be addressed through neoliberal institutionalist theory. The creation of interdependence and dependence, along with attitude changes and the promotion of international pluralism, is thought to be

25 "Vietnam president orders stop to imports of obsolete technologies," *Tuoitre News*, August 29, 2014, <http://tuoitrenews.vn/business/21999/vietnam-president-orders-stop-to-imports-of-obsolete-technologies> (accessed November 10, 2014).

26 "Vietnamese investors regret Chinese technology purchases," *Vietnamnet*, July 31, 2014, <http://english.vietnamnet.vn/fms/business/108589/vietnamese-investors-regret-chinese-technology-purchases.html> (accessed November 10, 2014).

27 *Ibid.*

28 "Vietnamese power sector risks dependence on China," *Dantri International News*, June 20, 2014, <http://www.dtinews.vn/en/news/018/35257/vietnamese-power-sector-risks-dependence-on-china.html> (accessed November 10, 2014).

29 *Ibid.*

30 "Vietnam haunted by hidden threats from Chinese hi-tech devices," *Tuoitre News*, August 9, 2014, <http://tuoitrenews.vn/business/22227/vietnam-haunted-by-hidden-threats-from-chinese-hitech-devices> (accessed November 10, 2014).



the effect of transnational relations.<sup>31</sup> These relations are in turn, according to neoliberal institutionalists, the interaction among private actors in world politics, as distinct from states and international organizations. Private actors can vary widely from multinational business enterprises to foundations, organizations of scientists, international trade union secretariats.<sup>32</sup> While the realist approach to interstate relations has for the most part accepted the role of states as the only significant actors,<sup>33</sup> liberalism has been asserting the importance of non-state actors in policy formation. Arnold Wolfers has pointed out that “the Vatican, the Arabian-American Oil Company, and a host of other non-state entities are able on occasion to affect the course of international events. In such cases, these entities become actors in the international arena and competitors of the nation-state. Their ability to operate as international or transnational actors may be traced to the fact that individuals are able to identify themselves and their interests with corporate bodies other than the nation-state.”<sup>34</sup>

Due to globalization, instances and avenues for transnational relations are increasing and transnational actors are increasingly competitive as they attempt to gain more and more by influencing public policy. These actors typically associate together based on the principle of mutual benefit and form “interest groups.” Nye and Keohane have argued that these actors can “affect interstate politics by altering the choices open to statesmen and the costs that must be borne for adopting various courses of action.”<sup>35</sup> This would, as a result, lead to a situation in which the states lose control. The loss Neo and Keohane mentioned is not the loss of control over “legal sovereignty” but the loss of “political and economic autonomy.”<sup>36</sup> In recent years, the Vietnamese government has acknowledged the increasing influence of interest groups in their country.<sup>37</sup> This is also considered by domestic economists as one of the main reasons of the significant economic dependence on China, as they asserted in a scientific seminar on the topic “Economic Au-

31 Joseph S. Nye and Robert O. Keohane, “Transnational Relations and World Politics: An Introduction,” *International Organization* 25, no. 3 (Summer, 1971): 337-40.

32 Joseph S. Nye and Robert O. Keohane, “Transnational Relations and World Politics: A Conclusion,” *International Organization* 25, no. 3 (Summer, 1971): 737.

33 Scott Burchill et al., *Theories of International Relations* (New York: Palgrave Macmillan, 2005), 30.

34 Arnold Wolfers, *Discord and Collaborations: Essay on International Politics*, (Baltimore: Johns Hopkins Press, 1962), 23.

35 Nye and Keohane, “Transnational Relations and World Politics: A Conclusion,” 724-25.

36 *Ibid.*, 743.

37 “Vietnam PM admits interest groups sway policymaking,” *Thanh Nien News*, January 06, 2012, <http://www.thanhniennews.com/politics/vietnam-pm-admits-interest-groups-sway-policymaking-8743.html>

tonomy in an Interdependent World” held by the Vietnam Chamber of Commerce and Industry on July 3, 2014.<sup>38</sup> The lack of transparency and integrity in Vietnam’s policy making process and the existence of many loopholes as well as serious corruption in the control mechanism of state power have enabled interest groups to collude with some corrupt government officials and influence domestic politics more easily.<sup>39</sup> The fact that Chinese contractors won over 90 percent of Vietnamese government’s EPC contracts over the course of ten years is highly questionable while their projects were usually completed behind schedule and localization rates were always low. As of 2014, there are two bauxite and aluminum industrial projects in Vietnam carried out by Chinese contractors with a localization rate of a mere 2 percent; up to fifteen of twenty coal-fired power plants constructed by Chinese contractors have the localization rate of 0 percent.<sup>40</sup> Having imported almost all machinery and equipment from their country, Chinese contractors have not only deepened Vietnamese commercial but also technical dependence on China. In this way, other alternative plans for construction, maintenance, and operation have become relatively more costly to the government and has therefore kept them in the vicious circle of Chinese import dependence. This excessive dependence would without question put Vietnam in the weaker position in an asymmetrical interdependent relationship and reduce its strength over the maritime territorial dispute.

The superior state in an asymmetrical interdependent relationship has many ways to harm its rival. Keohane and Nye have analyzed two aspects of power in interdependence: sensitivity and vulnerability.<sup>41</sup> Assuming that the policy framework is constant, sensitivity is defined as “the speed and magnitude with which a change in one country is felt in another, within one policy framework.” The more dependent a country, the more sensitive it is. When a country meets a change in the other country, reliance forces non-state actors to adapt or otherwise fail to acclimatize to the new situation and risk damage. These actors consequently appeal to the government to alter its policies in order to match the changes and protect them. Keohane and Nye’s analysis is followed by the definition of vulnerability, which is defined

---

38 Le Dang Doanh (seminar speech, Hanoi, July 3, 2014).

39 “Vietnam PM admits interest groups sway policymaking,” *Thanh Nien News*.

40 Vietnam National Research Institute of Mechanical Engineering, *Report on Foreign Contractors in Vietnam (report presented at the meeting for the summation of 10 years implementing development strategy for mechanical engineering industry held by Ministry of Industry and Trade, Hanoi, April 11, 2014)*.

41 Robert O. Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, 3<sup>rd</sup> ed. (New York: Longman, 2001), 9-16.

as “the relative availability and costliness of alternative policy frameworks, when it becomes necessary to adapt to external changes.”<sup>42</sup> Vulnerability importantly imposes costs on other countries. If there are effective alternatives which are not too costly to implement, then the effects of sensitivity can be dealt with ease. A recent example involved China banning bananas imported from Philippines in 2012. At that time, China accounted for more than 30 percent of Philippine banana exports.<sup>43</sup> Failing to find alternative export markets for perishable bananas, the Philippines suffered from a huge loss of \$33.6 million.<sup>44</sup> China used this and similar means to influence international disputes through punitive economic actions. Thus, Vietnam also needs to prepare itself in case China decides to do the same in the case of ongoing dispute in the South China Sea, considering Vietnam’s heavy dependence on China.

### Policy Recommendation

As asserted above, the primary task of the Vietnamese government at present is to keep their country in a political position balanced with China’s in the dispute over islands in the South China Sea. Above all, it is impossible to achieve that objective without escaping from the asymmetrical interdependent relationship with China, particularly economic dependence on China. On the one hand, the Vietnamese government needs to boost the potential development of domestic firms, especially those in supporting industries, to increase their country’s economic independence. On the other hand, while complete independence is impractical in a deeply globalized world, Vietnam must diversify dependence to other countries and thus reduce dependence on China.

Having pursued the aim of quickly industrializing, Vietnam has invested too much in the manufacturing industry and is now suffering from gaps in the national supply chain. Supporting industries, which provide input materials for manufacturing industry, have received little attention from the government.<sup>45</sup> This, as a result, has led to the country’s over-dependence

---

42 Ibid.

43 “The China-Philippine Banana War,” *Asia Sentinel*, June 06, 2012, <http://www.asiasentinel.com/society/the-china-philippine-banana-war/>

44 Josephine Cuneta and James Hookway, “China Dispute Threatens Philippine Industries,” *The Wall Street Journal*, May 16, 2012, <http://online.wsj.com/news/articles/SB10001424052702303879604577407730408858666> (accessed November 10, 2014).

45 Nguyen Thi Xuan Thuy, “Supporting Industries: A Review of Concepts,” in *Building Supporting Industries in Vietnam Vol. 1*, ed. Kenichi Ohno (Hanoi: Vietnam Development Forum, March 2007), 27.

on foreign input materials. Due to their cheap price and diversity, Chinese materials have gradually taken over the Vietnamese domestic market for input materials.<sup>46, 47</sup> To avoid collapse of the national industry sector, Vietnam must develop its supporting industry to gain back market share from China, which accounts for approximately 80 percent of Vietnamese input materials.

One possible solution is reorganization of the industrial system. The Vietnamese government should invest in and support the development of the selective materials manufacturing industries in which Vietnam has a competitive advantage in areas such as mechanical engineering, textiles, footwear, and electronics. In addition, Vietnam must enhance the processing of natural resources and minimize the export of raw resources to China as a way to raise efficiency.

Solutions strengthening the independence of domestic economy should be carried out while simultaneously diversifying external dependence. Among them, focusing on negotiations of pending trade agreements seems highly promising. As of October 2014, Vietnam is expected to sign fourteen free trade agreements (FTA) with fifty-five countries and territories by 2015 including the important Trans-Pacific Partnership Agreement (TPP) and the Free Trade Agreement with EU.<sup>48</sup> Tariff exemptions and reductions provided by these agreements will allow Vietnam to import more equipment, input materials, and consumer goods from other countries such as the United States of America, Japan, New Zealand, Kazakhstan, Belarus, Australia, the EU, Russia, Canada, and South Korea. These opportunities will also give Vietnam's agricultural exports more destinations to go. However, in preparation, Vietnam has to implement new quality standards to meet the demands of those high quality markets.

From the neoliberal institutionalism perspective, the most effective solution for this problem should be sought in its intrinsic nature. That means the Vietnamese government must deal with interest groups in their country first or risk discovering that tackling Chinese dependence will be in vain. Keohane and Nye have described transnational actors' ability to "create a 'control gap' between the aspirations for control over an expanded range

46 "Businesses urged to invest in supporting industries," *Vietnam Plus*, June 19, 2014, <http://en.vietnamplus.vn/Home/Businesses-urged-to-invest-in-supporting-industries/20146/51731.vn-plus> (accessed November 10, 2014).

47 "Vietnamese manufacturers rely on Chinese materials and machinery," *Tuoitre News*, November 12, 2013, <http://tuoitrenews.vn/business/15912/vietnamese-manufacturers-rely-on-chinese-materials-and-machinery>.

48 Hoang Trung Hai, speech presented at the annual investor meeting, Hanoi, October 16, 2014.

of matters and the capability to achieve it.”<sup>49</sup> This would cause many difficulties for the government if they do not try to gain back power from these groups before pursuing other policies.

During the process of furthering their interests, interest groups in Vietnam have influenced the policy making process and contributed to the creation of many loopholes in Vietnamese law,<sup>50</sup> which are issues the government should address immediately. For example, due to the lack of a quality control mechanism for imports, Chinese low-quality products have easily penetrated the Vietnamese domestic market.<sup>51</sup> These cheap prices have affected Vietnamese manufacturer preference who desire to cut product costs by any means even if it means forgoing domestic high quality products of the same kind.<sup>52</sup> In this way, Chinese firms have almost completely captured the Vietnamese market and crowded out local firms despite a lack of investment in Vietnam.<sup>53</sup> It is impossible to turn domestic supporting industry around if measures are not imposed to ameliorate this situation, particularly to control the flow of products from China into Vietnam and promote usage of domestic products in local firms.

Another issue needing consideration is in regards to the government’s development projects, which usually have a very low localization rate when assigned to Chinese contractors. In order to “fight corruption and to increase the effectiveness, efficiency, and transparency of public procurement systems,”<sup>54</sup> the Vietnamese government revised the Vietnam Bidding Law in 2013. The revised law requires “the foreign contractors work in partnership with a Vietnamese company or sign a sub-contract with a local company. Furthermore, foreign contractors are only allowed to employ foreign workers when there are no qualified Vietnamese workers available for the projects.” The adoption of this revised law in practice as of July 1, 2014, was expected to create fairness for all contractors and promote human resource improve-

---

49 Nye and Keohane, “Transnational Relations and World Politics: A Conclusion,” 743.

50 Le Dang Doanh, “Innovative Thinking and Institutional Reform” in *Macroeconomic Report 2012: From Macroeconomic Instability to the Path of Restructuring*, To Trung Thanh et al. (Hanoi: Knowledge Publisher, 2012).

51 “Vietnam should reproach itself for letting Chinese goods dominate market,” *Vietnamnet*, May 24, 2013, <http://english.vietnamnet.vn/fms/business/74782/vietnam-should-reproach-itself-for-letting-chinese-goods-dominate-market.html> (accessed November 10, 2014).

52 *Tuoi tre News*, “Vietnamese manufacturers rely on Chinese materials and machinery.”

53 “In high inflation, Vietnamese consumer prefer cheap goods,” *Vietnamnet*, June 12, 2011, <http://english.vietnamnet.vn/fms/business/9001/in-high-inflation-vietnamese-consumer-prefer-cheap-goods.html> (accessed November 10, 2014).

54 Nguyen Cong Ngo, speech presented at the UN DPADM In-House Seminar, New York, November 22, 2013.

ment. Nonetheless, it is suggested that additional rules or standards be enacted to compel Chinese contractors of projects currently being constructed, which accounted for a large proportion, to use assured quality materials and employ more local workers. For example, the government could impose a special tax on Chinese materials that are currently unavailable in the Vietnamese market and are imported into Vietnam by Chinese contractors. This would prevent Chinese contractors from Chinese over importation and from further damaging the domestic industry which is already over dependent on Chinese materials. The government could also subsidize Vietnamese firms when they provide Chinese contractors with materials on condition that they reduce their price to become more competitive with Chinese brands. This solution would, of course, create a situation where the government would face an increased budget burden, but the benefit may outweigh possible future costs.

Last but not least, the ultimate goal of Vietnam is not simply to reduce dependence on China but to participate in the dispute settlement more actively. However, due to its economic, political, and military inferiority, Vietnam would definitely be at a disadvantage in the case of a military conflict. Therefore, finding a peaceful solution to resolve the dispute is critically important for the Vietnamese government. Liberal institutionalists have already agreed that international institutions have played a decisive role in the promotion of cooperation and peace.<sup>55</sup> Keohane has proposed the approach of “neoliberal institutionalism”<sup>56</sup> whereby international institutions can encourage cooperation through the provision of information about states and reducing transaction costs in the negotiating of agreements.<sup>57</sup> Institutions in this case are not just understood as the United Nations or World Trade Organization but are instead defined as “sets of implicit or explicit principles, norms, rules, and decision-making procedures around which actors’ expectations converge in a given area of international relations.”<sup>58</sup> In this sense, the United Nations Convention on the Law of the Sea (UNCLOS) and other international laws are obviously seen as the ‘institution’, through which Vietnam can try to make an agreement with China in this dispute and avoid unnecessary military conflict. The Vietnamese government, therefore, should

---

55 Scott Burchill et al., *Theories of International Relations*, 64.

56 Robert O. Keohane, *International Institutions And State Power: Essays in International Relations Theory* (Boulder: Westview Press, 1989).

57 Robert O. Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy* (Princeton: Princeton University Press, 1984).

58 Stephen D. Krasner, ed., *International Regimes* (New York: Cornell University Press, 1983), 2.

continue to settle the dispute in accordance with established international laws, as well as through these institutions, joining with other weak countries who also in dispute with China for greater political influence.

## **Conclusion**

The South China Sea, of which China claims approximately 90 percent, is of significant importance to neighboring countries as well as in regards to international sea commerce. In the case of Vietnam, two disputed islands chains have not only economic but also security and political implications. However, Vietnam's efforts to resolve this dispute have been challenged by its relative lack of power in the international arena compared to China. This paper has analyzed and provided some possible solutions to this problem following the approach of the neoliberal institutionalism.

Neorealist theory treats military power as the most important power of a state and argues that because of a state's desire to survive in a world of anarchy, it will develop military capabilities as a means to increase its relative power. This theory is not completely applicable to Vietnam's situation as the government has already acknowledged a military disadvantage and has decided to pursue a peaceful solution. In this case, neoliberal institutionalist theory, which asserted that states can utilize interdependence as a source of power to influence other states' behavior, is reasonably useful in its application.

This paper has shown a historical example of North Vietnamese dependence on China leading to a failure of that state to exercise sovereignty over the Paracel Islands and how the economic dependence on China in the present day has also played a major role in controlling the Vietnamese government's behavior. The authors have analyzed the situation of that dependence as well as the main cause of it, the effect of transnational relations, and how China can exploit it to the detriment of the Vietnamese economy and benefit of China in dispute settlement negotiations. Finally, this paper has suggested several solutions for the Vietnamese government to carry out in order to reduce dependence on China. Nonetheless, statesmen should keep in mind that no progress can be made until the influence of transnational actors in Vietnamese domestic politics is successfully curbed. **Y**