

PASCN Discussion Paper No. 99-16

The Political Economy of Philippines- China Relations

Benito Lim



The *PASCN Discussion Paper Series* constitutes studies that are preliminary and subject to further revisions and review. They are being circulated in a limited number of copies only for purposes of soliciting comments and suggestions for further refinements.

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Benito Lim

University of the Philippines

September 1999

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CONTENTS

Abstract	1
Pre-Colonial Political Economy	2
Political Economy Under Spain	3
Political Economy Under the US	5
Political Economy After Independence	6
Political Economy Under the Marcos Government	7
Political Economy Under the Aquino Administration	12
Political Economy Under the Ramos Administration	18
FDI into China	21
Conclusion	24

*The Political Economy of Philippines-China Relations**

Benito Lim

Abstract:

Early history of Philippines-China economic relations (10th-17th C) showed that there were many instances when good political relations often led to good economic relations. There was direct and regular trade. It was extensive and covered large portions of the Philippine archipelago and neighboring Southeast Asia. Conducted in a friendly manner, under the aegis of what the Chinese imperial court called “Vassal tributary missions,” it benefited the Filipino traders on the whole. Recent history has revealed that President Marcos followed good political relations with the PRC. Philippine colonial history (17th –19th C) however was characterized by bad political relations. Spanish colonial policy was discriminatory against the Chinese but regardless of all kinds of impediments placed on the Chinese traders, these did not necessarily impede business relations. Vigorous commercial relations continued since they served the needs of rival parties. Spanish colonial administrators despite their fear of the Chinese as a threat to their colonial outpost, learned to co-exist and cooperate with the Chinese who were indispensable economic instruments in preserving and sustaining the colonial economy. American (1902-1945) discriminatory laws against the Chinese, did not deter them from active participation in the Philippine economy. Economic relations with China was suspended during World War II and continued until 1970. Trade with China became more vigorous after diplomatic relations in 1975. During the Aquino administration, when it focused its attention on Taiwan, trade volume with China plummeted significantly. The 1995-1998 China-Philippine trade and investment data have shown that positive economic policies such as trade liberalization and investment incentives can bring about good economic relations despite political tensions brought about by conflicting claims over the Mischief Reef.

* This study is part of the research project “China and Its Implication to the Asia Pacific”, funded in whole by the Philippine APEC Study Center Network (PASCN).

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It appears that for over one thousand years of recorded history, the direction and improvement in economic relations between the Philippines and China¹ have been dictated, molded and forged by good or bad political considerations. There were of course some historical developments that challenged the merit of this observation. Whether the observation that good political relations lead to good economic relations or vice versa, and the applicability of this observation on contemporary times, is the concern of this paper.

For instance, since 1995, the political conflict between China and the Philippines over the Mischief Reef, has occupied media headlines for over three years. The perception of majority of our political leaders and the molders of public opinion as expressed in the mass media is that Chinese occupation of the Mischief Reef is bad politics. The next question is, did it have adverse effects on the commercial relations between the Philippines and China?

Pre-Colonial Political Economy:

From the very beginning of Philippine trade with China, the good trade relations between Philippine chieftains and Chinese traders were forged on the basis of good political relations.

Chinese records show that regular and active trade between China and the Philippines took place only in the tenth century. Earlier trade between China and the Philippines had to be transacted mainly through the Champa (Vietnam) coast.² But Mai-i (Mindoro) traders who previously went through Vietnam before proceeding to China decided in 972 to circumvent Vietnam and instead to trade directly with China by sailing into Canton.³ In order to do so, Mindoro traders had to secure the blessing of the Chinese emperor with a tribute mission. They gifted the emperor with exotic gifts like pearls, frankincense, myrrh, and colorful animals. Thereafter Mindoro delegation was treated as state guests and enlisted as feudatory princes of the empire. They were bestowed with corresponding seals and patents of office.

No doubt, the ceremonial acknowledgment of Chinese imperial suzerainty by tributary missions was good politics, it was in turn rewarded by the grant of accreditation to Mindoro traders to engage in direct commercial activities with China.

* This study is part of the research project "China and Its Implication to the Asia Pacific", funded in whole by the Philippine APEC Study Center Network (PASCN).

¹ Philippines-China relations as used in this paper cover not only commercial relations between the two countries but include the economic role of the Chinese in the Philippines.

² William Henry Scott, "Filipinos in China Before 1500," *Asian Studies*, April, August, December, 1983, pp.1-19.

³ Scott, p.2.

Economic exchanges with the southern countries were so lucrative and extensive that in 972 the first emperor of Sung Dynasty established offices of maritime trade in Kwangchow, Hangchow, and Minchow with separate superintendents to deal with all Arab, Achen, Java, Borneo, Ma-i (Mindoro), and Srivijaya “barbarians.”⁴

Indeed good Sulu political relations and cooperation with China which dated back to the Yuan dynasty (1278-1368).⁵ The Sulu missions had convinced the Chinese to view Sulu as an equal of Malacca. With Chinese co-operation, Sulu subsequently became an international emporium.

Since trade missions were viewed by the Chinese as diplomatic initiatives, the Butuan missions can be viewed as the beginning of official relations between the Philippines and China. The residence of Paduka Batara’s heirs in Techow, can in fact be interpreted as the first Philippine embassy in China. More importantly, from the standpoint of the Philippine side, the Mai-i trade mission, the Butuan and Sulu missions were attempts by separate Philippine chieftains or polities not only to bypass Champa as a trade entrepot but to establish themselves as new centers of international trade.

Luzon ships were also plying the Manila, Fujian, Timor, and Malacca route during this period. By this time, the *tung-yang chen-lu*, the eastern route from the South China Sea to Sulu, Borneo, and the Moluccas was fairly well established.⁶

Political economy under Spain:

Thus by the time of Magellan’s arrival to the Philippines in the 16th century, regular trade and cultural contacts between China and the Philippines was firmly instituted. But the flourishing trade between Filipinos and Chinese deteriorated by the late 16th to the 17th century. The entry of the Spanish colonial government interposed restrictions to direct Philippines-China trade. The Spaniards sought to monopolize and capture for themselves trade and commerce, and to direct it towards her colonies in the Americas and to Spain in what is known as the Manila-Acapulco or Galleon trade 1565-1815.⁷ In the process, the Spaniards took over much of Philippines-China trade to the exclusion of the native Filipino traders and merchants. Moreover, whereas before several Philippine ports were active in the international trade, the Spaniards closed all other ports and concentrated trade in their fortress city of Manila.

To the Spanish colonial officials, the Philippines was a small part of a grand dream of Spain to control if not conquer most of Asia, but above all China.⁸

⁴ *Sung Shih, Monographs (Chih)*, cited by Scott.

⁵ See Wu Ching-hong, “A Study of Reference to the Philippines in the Chinese Sources from Earliest Times the Ming Dynasty” *Philippine Social Sciences and Humanities Review*, 24 (University of the Philippines, Quezon City, 1959) pp. 1-181.

⁶ Wu Ching-hong, “Supplements to a Study of References to the Philippines in Chinese Sources from Earliest Times to the Ming Dynasty,” *University of Manila Journal of East Asiatic Studies*, 7(1958), pp.307-393.

⁷ See William Lyle Schurz, *The Manila Galleon* (New York: E.P. Dutton and Co., Inc. 1939).

⁸ See Martin Nonse, *General History of the Philippines Part I Vol. 1, The Discovery of the Philippines*, Manila, 1986.

In 1573, Diego de Artiega wrote the Spanish crown for permission to survey China preparatory to trade and future conquest.⁹ Governor Aguilar told the Spanish Council in the mainland that a well trained battalion could defeat the Chinese armies.¹⁰ However in 1586 when Governor Santiago de Vera proposed to the King the annexation of China to the Spanish empire, the King disapproved of his plan and instead asked him to win the friendship of the Chinese.¹¹

Discouraged from their plans of conquest, the Spanish governors in the Philippines pursued direct trade with China. Antonio de Morga, president of the Royal Audencia in 1609, proposed direct trade. He argued that direct trade would not only win Chinese goodwill but obstruct Chinese threat. Direct trade was perceived as the means for the Spanish traders in Manila to control prices of imported Chinese goods. Unfortunately for the Spaniards, the Chinese already had earlier arrangements with other Europeans. The Portuguese, French, and Dutch had already established factories in Canton and Macao.

Unable to pursue plans of conquest and direct trade with China, the Spaniards settled for dealing with the Chinese traders as the middlemen. This arrangement led to an increased number of Chinese merchants and émigrés to the Philippines. It also allowed the Chinese to maintain a dominant position in the economy of the Philippines. This trade arrangement eventually became one end of Manila's entrepot trade, wherein Chinese goods, especially silk, were traded for Mexican silver dollars.¹² As a consequence, Spain was forced to pursue a policy of compromise that allowed Chinese entry to the Philippines and play a dominant role in Philippine business activities. In exchange, the Spaniards relaxed its immigration rules, allowed the entry of more Chinese. But this arrangement, while it placed the Chinese in a dominant role in the economy of the Philippines, did not allow the Chinese to enjoy equal status with the Spaniards. Indeed the Spaniards restricted Chinese movement, Chinese residence and Chinese trading to only designated parts in the Philippines. The Spaniards also imposed heavy taxes on the Chinese and required them to render labor on colonial building and construction projects. As a consequence, the political collaboration between the Spaniards and the Chinese traders was characterized by bad faith, lack of trust and betrayals.

Regardless of iniquitous and harsh conditions, the Chinese in the Philippines increased. In 1570, there were about 140 Chinese in Manila, twenty years later, the number increased to 4,000. By 1600 there were over 26,000. In 1603 when the Chinese staged an insurrection, about 24,000 Chinese were slaughtered and only 1,500 were left. During the second Chinese insurrection in 1639, another 23,000 were killed. Ten years after, the population in the *Parian* rose to 15,000. Much of the increase in Chinese populations could also be explained by the lack of political will and failure by lower echelon bureaucratic authorities to implement immigration restrictions and deportation orders.

⁹ William Lyle Schurz, *The Manila Galleon* (New York: E.P. Dutton and Co., Inc. 1939), p.69.

¹⁰ *Ibid.*, p 68.

¹¹ Santiago de Vera, "Memorial to the Council," July 26, 1586, Blair and Robertson, Vol. 6, pp. 197-229.

¹² Schurz, p. 73-74.

Despite intermittent massacres trade and commercial networks were continued. The Spaniards and the Chinese not only co-existed but depended on each other to maintain a viable and lucrative commercial relationship, albeit, uneasily. Although most Spaniards hated the Chinese, they could not manage the colony's economy without them. The Spanish bureaucracy relied on trade and other commercial activities with China and the Chinese as a source of income for the annual subsidy of the Spanish colonial bureaucracy which was sorely inadequate, and it often arrived late or not at all. The Chinese, for their part, needed the Philippine market to ply their trade. This uneasy political compromise was maintained by the Spaniards for over 250 years of its colonial history. The long fitful history of this partnership revealed political policies from higher colonial authorities were subverted by the rank and file for personal considerations and economic gains.

But Spanish political relations with China were not totally bad. In 1858 the Spaniards tried again, after failures in 1820 and 1840, to negotiate with China to facilitate Chinese immigration to the Philippines and to provide favorable trade arrangements. By 1864, the Chinese entered into a treaty with Spain to allow more favors to Spanish ships at Chinese ports. In return, Spain granted the most favored nation treatment to Chinese merchants coming to the Philippines.

Despite the treaty of 1864, trade between the Philippines and China during the second half of the nineteenth century saw a decline compared to Philippine trade with Great Britain and the United States.¹³ However if we look at Philippines-China trade statistics over the years, it remained relatively constant from 1850 to 1872. After 1872, there was a decline of Philippine exports to China. No doubt, when the other Western traders started to join the Manila-China trade, they cut into the pre-existing junk trade. Indeed by 1870, junks stopped going to Manila, although some went to other Philippine ports.

This clearly indicates that, contrary to widespread expectations, good political relations did not always lead, to good commercial relations.

Political Economy under the U.S.:

When the United States took over the Philippine government by virtue of the Treaty of Paris of 1898, the American colonial administrators tightened further the Spanish discriminatory laws against the Chinese. The first few proclamations were the implementation in the Philippines of the Exclusion Law applying to the Chinese in the United States. They also abolished the *Gremio de Chinos* as well as the positions of the *cabecillas* and *governadorcillos*. These were positions given to the Chinese by Spanish authorities to help the Spanish colonial government in collecting taxes from their fellow Chinese. It also allowed the Chinese to settle problems and differences among themselves.

The US Congress in 1902 formally extended the Exclusion Law to the Philippines, despite the immediate protest of the Chinese Consul. The law which prohibited Chinese immigration to the Philippines, was intended mainly to regulate

¹³ See Benito F. Legarda, "Foreign Trade, Economic Change, and Entrepreneurship in the Nineteenth Century Philippines," Ph.D. dissertation, Harvard, 1955.

Chinese economic role in the Philippines and hence Philippines-China trade relations. These developments plus American desire to keep the Philippines as its exclusive market, led to a decline the volume of trade between China and the Philippines.

However, in 1904, when the Americans successfully subdued Filipino armed resistance to the U.S. rule in Manila, commerce and industry started to flourish. The application of the Chinese Exclusion Law in the Philippines did not reduce the number of Chinese. On the contrary, the number of Chinese increased by threefold between 1903 and 1909. Although the increase in the number of Chinese was due to the American colonial government's need for both coolie and skilled labor, these new immigrants eventually became middle men of American imports and traders. The Exclusion Law which was bad politics and which failed to anticipate the manpower and other economic needs of American colonial officials. This led American immigration officers in the face of reality, as with their Spanish predecessors, to look the other way on the rampant practice of illegal Chinese entrants who came in as relatives of the legitimate Chinese residents in the Philippines. This started the entry of Chinese who had to recourse to the use of two names in immigration documents. The first were legal names or the names of their sponsors that appeared on their immigration papers, and while their second were aliases, their real names in China.

But political and legal differences notwithstanding, the total Chinese investments in the Philippines in 1939 reached \$100 million, second only to US investment of US \$331 million. That same year, the Chinese government opened a branch of the Bank of Communications in Manila. The bank financed many of Chinese mercantile and industrial activities in Manila as well as in the remotest places in the Philippines.

Trade between China and the Philippines came to a complete halt during WWII and was resumed in 1945. The trade figure for 1945-1946 was \$40 million.

Philippine colonial history has shown that the Philippines-China commercial relations survived and flourished despite a hostile colonial government and intermittent rebellions by Chinese traders and workers when conditions became unbearable. These sporadic uprisings were caused by a combination of discriminatory immigration laws, excessive tax and labor levies imposed by the colonial government and extraction of exorbitant bribes by rank and file colonial bureaucrats. However, inspite of all these negative practices, the market forces were stronger than the political policies of the colonial governments. Discriminatory domestic laws did obstruct commercial activities but may have intensified consumer demands for Chinese goods and products. Market forces, revenue needs of the colonial government and personal greed of the law enforcers ran counter to stated government policies.

Political Economy after Independence:

The Philippines-China commercial relations was suspended after the Chinese Communist Party captured political power in China on October 1, 1949. In the same year, the Philippines immediately instituted anti-Communist policies which isolated China from the rest of the "free world," prohibited Chinese immigration and banned travel to or from China. At the same time the Philippine government signed an agreement with Taiwan on trade relations, exchange of specialists, and information

which led to our very close ideological and economic partnership with Taiwan .¹⁴ In 1956, President of Carlos P. Garcia opened a Philippine Embassy in Taiwan.

During the early days of the Cold War, this political and economic arrangement was not questioned. Furthermore, the Philippines considered partnership with the U.S. and its allies as the only assurance for its survival. The Philippines agreed to play down its growing economic friction with the U.S. due to the unequal terms of trade as stipulated in the Laurel-Langley agreement. Although many Filipino leaders could no longer tolerate what they considered as unfair American trade policy, they refrained from pursuing trade disputes lest it jeopardized our security alliance with the U.S. Their position at the time was to wait until the Laurel-Langley agreement expired.

Political Economy under the Marcos Government:

When President Ferdinand Marcos opened diplomatic relations with China in 1975, nearly after a quarter of a century, commercial relations with China were renewed.

Since his election as President in 1965, President Marcos had initiated a program to review Philippine foreign policy. One of the key points of the new policy called for a closer study of Asia and for the Philippines to accelerate trade with other Asian and socialist countries. The Philippines' primary trading partner was, the U.S., and trade with her was on the decline. The downtrend in Philippine-U.S. trade together with near expiration of the Laurel-Langley Trade Agreement, and compounded by the oil crisis of 1973, forced Marcos to search for new markets and alternative trade partners. The Marcos government saw in socialist countries new markets and wider scope of economic possibilities that could also put an end to the "special relations" with the U.S. Thus the opportunity for new business ventures led to the formulation of new foreign policy. Thus the Marcos government prepared the country for the establishment of diplomatic ties with China and the Soviet Union.

To facilitate the search for new markets, in 1966 President Marcos lifted the travel ban on Philippine citizens to socialist countries. He argued before Congress that the lifting of the travel ban would make some of our countrymen who traveled to Russia and China, "a bit wiser":

We adopted a liberal view on travel to communist countries. This gave some of our countrymen a chance to see for themselves what economists call the Russian and Chinese models. These travelers returned, I think, a bit wiser, and they are probably much wiser because of recent developments in the Chinese mainland.

On January 27, 1969, President Marcos in his state of the nation address to Congress unveiled his new foreign policy:

We, in Asia must strive toward a *modus vivendi* with Red China. I reiterate this need, which is becoming more urgent each day. Before long, Communist China will have increased its striking power a thousand fold with

¹⁴ *Diplomatic Agenda of Philippine Presidents*, p.9.

a sophisticated delivery system for its nuclear weapons. We must prepare for that day. We must prepare to co-exist peaceably with Communist China.¹⁵

The new Philippine foreign policy was precipitated to a large degree by international developments. By the 1960s, a serious rift occurred between China and the Soviet Union; Nixon announced the withdrawal of American forces in Asia, the relaxation of cold war tensions, and America's détente with the Soviet Union. The looming worldwide monetary crisis, coupled with worsening domestic economic difficulties as a consequence of deteriorating trade with the US and other industrialized nations, led President Marcos to announce a new policy which was to normalize commercial relations with the socialist states.

On December 12, 1970, Secretary Romulo recommended to President Marcos the establishment of preliminary contacts with selected Socialist countries to determine the possibility of concluding executive agreements to be preceded by diplomatic or consular relations as the need arose.

On September 21, 1972, Marcos declared martial law. The announced intention was "to stop the rebellion from the left and the right" and "to continue the economic development of the Philippines." Critics disagreed and claimed that he declared martial law to extend his term of office indefinitely.

One year after the declaration of martial law, "developmental diplomacy" was launched. The Philippines normalized relations with Bulgaria, Poland, Czechoslovakia, East Germany, Hungary and Mongolia. By March 1974, trade relations with these countries, as well as with China and the Soviet Union reached \$80,398,309.00, with exports totaling \$46,376,372.00, and imports \$34,021,936.00.¹⁶ Forty nine percent of the overall trade with socialist countries was with China.

With these trade figures, the prospect for expanded trade looked bright especially with the impending expiration of the Laurel-Langley Trade Agreement on July 3, 1974. The Philippines received assurance from these countries that they were interested in importing traditional export products which the Philippines exported to the US, and which were also the Philippines' principal foreign exchange earners. The East Europeans expressed interest in buying abaca, copra, sugar and sugar products. The Soviet Union and the Chinese lists included nearly all Philippine export products.

In March 1974, Ambassador Benjamin Romualdez went to Beijing to continue talks for normalization of relations. In July-August of the same year, Ambassador Romualdez made three more trips to arrange for Mrs. Imelda Marcos proposed visit from September 20 to 27, 1974 upon the invitation of Prime Minister Zhou Enlai.¹⁷

Mrs. Marcos concluded a trade agreement providing for sale by China of petroleum, and purchase of major export products from the Philippines. In November

¹⁵ Ferdinand E. Marcos, "New Filipinism: The Turning Point," State of the Nation Message to the Congress of the Philippines, January 27, 1969.

¹⁶ "RP-Red Trade Surplus: \$12.3 M," *Philippine Daily Express*, September 21, 1974.

¹⁷ *Diplomatic Agenda of Philippine Presidents*, pp.227-228

of the same year, Beijing signed an agreement to import coconut oil, logs and plywood, copper concentrates, and sugar.¹⁸

Ten months before normalization, the PRC government had already demonstrated their willingness to help ease the economic difficulties of the Philippines brought about by the steep increase of oil prices. On September 25, 1974 an agreement was signed for China to sell high quality petroleum to the Philippines and in turn buy Philippine products such as coconut oil, lumber, sugar, copper ore, and other metals. The initial shipment of 125,000 barrels of crude oil was delivered in October of that year.

On June 7 to 9, 1975, President Marcos went to the People's Republic of China and signed a Joint Communiqué normalizing relations between the Philippines and China.¹⁹ Among other things, the Communiqué recognizes that “there is but one China and that Taiwan is an integral part of Chinese territory...”

Thereafter, the Philippines terminated all extant official relations with Taiwan. The Taipei embassy in Manila was renamed the Pacific Economic and Cultural Center now known as the Taipei Economic and Cultural Office, while the Philippine Embassy in Taiwan was renamed Asian Exchange Center, Inc. also subsequently renamed as Manila Economic and Cultural Office, and lodged under the Office of the President.

Barely two months after normal relations, more agreements were signed to increase trade, cultural and scientific exchanges, official visits, and to obtain loans. On March 12, 1978, China's Vice Prime Minister and Vice Chairman of the Chinese Communist Party, Li Hsien-nien and Foreign Minister Huang Hua visited the Philippines. An agreement on scientific and technical cooperation was signed between the two countries aboard the presidential yacht, “*Ang Pangulo*.”

On October 13, 1980 a loan amounting to US\$30 million from the People's Republic was obtained to pay for the purchase of 500 mini-hydro power plants. The agreement was signed by President Marcos and Ambassador Chen Hsin Jen.

On August 6, 1981, for the first time in the Philippines' post war history, a Chinese Prime Minister came on a four-day state visit to the Philippines. Prime Minister Zhao Ziyang's entourage included Li Qiang, Minister of Foreign Trade, Chen Chu, Deputy Secretary General of State Council and others.

Zhao agreed to continue to supply crude oil to the Philippines at concessional prices. The oil deal was one of the three issues President Marcos discussed with Prime Minister Zhao. Other issues were Philippine purchase of high grade coal from China and increased Chinese importation of Philippine coconut oil.

Prime Minister Zhao also pledged that China would not intervene in the internal affairs of the Philippines nor will it seek to impose its policies in Asia.²⁰

¹⁸ Ibid.

¹⁹ Ibid., pp.239-240.

²⁰ *Diplomatic Agenda of Philippine Presidents*, pp.344-345.

During a 1984 visit of Imelda Marcos, the Chinese agreed to increase its trade volume with the Philippines from the targets of US\$20 million in 1974, and US\$30 million in 1978 to US\$500 million. The Chinese also agreed to buy more Philippine products to balance the two-way trade. The trade in 1984 in fact had reached US\$300 million. Mrs. Marcos also negotiated an agreement for China to supply US\$60 million worth of oil on deferred payment basis.

The PRC also kept its word not to interfere in the internal affairs of the Philippines and refrained from providing any substantial support to the Communist Party of the Philippines. This hands-off policy delighted the Filipino Armed Forces leaders and surprised President Marcos himself. However it also gave the opposition KMT opportunity to expand its influence among the local Chinese in the Philippines.

There is no doubt that under the Marcos administration, trade volumes between China and the Philippines increased. It was the outcome of deliberate positive political decisions made by the leaders of both countries. From zero volume in 1970 to a target of \$20 million in 1973, the amount nearly doubled in 1975 and again in 1977. China moved from an insignificant trade partner in the early 1970s into the Philippines' sixth largest trading partner in 1985. (See Table 1) In 1985, the PRC even dislodged Taiwan as the Philippines' sixth largest trading partner.

Table 1. Foreign Trade of the Philippines with China*
(F.O.B. value in US Dollars)

Year	Total	Imports	Exports
1971	1,408,195	1,006,390	401,805
1972	6,312,859	5,530,309	782,550
1973	27,889,132	21,924,670	6,571,480
1974	37,231,327	23,924,670	13,306,657
1975	72,251,804	47,036,027	25,215,777
1976	93,344,544	53,792,649	39,551,895
1977	186,372,229	78,351,890	108,020,339
1978	159,085,110	111,627,098	47,458,012
1979	172,417,464	120,953,005	51,464,459
1980	250,691,740	205,705,312	44,986,428
1981	272,742,410	194,516,918	78,225,492
1982	311,531,991	206,327,132	105,204,859
1983	151,542,102	122,150,595	29,391,507
1984	280,441,795	220,255,977	60,185,818
1985	355,877,664	276,084,896	79,792,768

*Source: Foreign Trade Statistics of the Philippines

The Marcos administration indeed demonstrated that good political relations with China can lead to good business relations. China's purchase of Philippine products had followed the number of diplomatic missions Marcos sent to China.

Despite friendly political decisions to keep trade mutually beneficial for both China and the Philippines, the balance of trade, except for 1977, had been in China's favor ever since the opening of diplomatic relations between the two countries. The drop in trade volume from \$311.5 million in 1982, to \$151.5 million 1983, and from \$355.8 million in 1985 to \$215.3 million in 1986, were the outcome of political economic developments. The drop in 1983 was due to the Philippine balance of

payment crisis as a consequence of the assassination of Senator Benigno Aquino. The drop in 1986 was due to the political uncertainties during and immediately after the SNAP elections.

China's main exports during this period were mainly energy products, from crude oil, petroleum products, steel billet, chemical raw materials, machinery products, canned goods, textile, to coal and coal products. The main reason for the imbalance was due to the Philippines' purchase of large quantities of crude oil at a "friendship price." Other products which were the outcome of China's Four Modernization Program which started in 1979, such as generators, tires, and processed food were not among the Philippines' top imports. Similarly Philippine exports were limited to coconut oil, lumber, fertilizer, timber, plywood, sugar, copper ore, and other metals. Moreover, due to its Modernization Program, China's shopping list consisted of items such as: complete turn-key plants for steel, fertilizer, combustion engines, computers, chemicals, advanced electronics, air crafts, scientific equipment, precision machinery, nuclear plants, robotics, and raw materials in little quantities or not available inside China. Except for copper concentrates, the Philippines had very little else listed in China's shopping list.

Another reason for the trade imbalance stemmed from the fact that the Philippines and China produced similar products, putting the two countries in competitive rather than complementary footing. Moreover China purchased only those items listed in the Trade Protocol, new products that were not incorporated in the protocol were not purchased by the Chinese.

Finally although the Chinese listed a lot of items in the trade protocol, the Chinese pegged their prices way below the prevailing prices in the world market. Clearly, the Chinese wanted the Philippines to sell its exports at "friendship price" the way the Philippines pegged Chinese crude oil on a "friendship price" basis.

No doubt even good political policies during the Marcos administration, including provisions of a trade agreement granting most favored nation treatment to each other cannot erase decades of propaganda that inculcated the fear of communism among majority of the Filipinos, including Filipino-Chinese. Among the Chinese leadership there were those who harbored fear of capitalism and its concomitant moral decadence. Thus political rapprochement did not remove protectionist policies that demanded strict adherence to the maintenance of trade balance. The Philippines-China Joint Trade Committee had to meet every year to come up with a trade protocol which set the target amount and volume of trade for the two countries. Difficulties arose since both negotiating teams could not ensure production and quantities of goods for which they negotiated.

Compounding the problem was that the Marcos government development program relied on unpredictable preconditions: a strong government shored up by military force; government intervention in the market; authoritarian control of labor activities and other forms of oppositions, all of whom were excluded from political and economic decision-making, and nurturing of a few selected businessmen known as "crony capitalism."

In the case of trade with China, President Marcos pursued neo-mercantilist interventionism. Beginning 1977, both China and the Philippines held annual meetings of the Joint Trade Committee, alternatively in Beijing and Manila, specifically to pursue a “trade balance policy” and “to set target for trade.” No doubt, this was intended to cultivate “good political relations” with China which complemented China’s command economy at the time.

After Marcos was deposed from office and the dissolution of the Martial Law regime, it was widely expected that many of the Marcos economic policies would be dismantled and that new priorities would implement more liberal economic policies.

Political Economy under the Aquino administration:

No doubt the Aquino administration marked a return to democracy and the restoration of civil rights in the Philippines following fourteen years of Marcos martial rule. Congress was re-instituted, governmental control changed hands, and the military, which earned notoriety as the most repressive and most brutal instrument of martial rule, was placed under civilian control. Most political prisoners including leading member of the Philippine Communist Party were freed; some of them were even given a role in the government. Civilian control however led to a succession of coup d’etats.

President Aquino faced enormous economic, political and social problems. Government was bankrupt, there was double digit inflation, unemployment rose, strikes and demonstrations by farmers, laborers, and students were staged regularly. There were assassinations and counter-assassinations between the adherents of left and right ideologies. In general, the government suffered from disorder and confusion even within the highest administrative echelons. Worse, the Philippine elite which had united against the martial law regime, fought each other fiercely to gain control of the machinery of government. Many of the military officers who helped depose Marcos staged several coups against the government.

Economic production and business activities were also hamstrung by questions of ownership of Marcos-established enterprises and prosecuting former “Marcos cronies.” Much government effort was expended in the search for, and the recovery of the “Marcos ill-gotten wealth” by the Presidential Commission on Good Government.

In the meantime, the presence of progressives, nationalists, left-leaning elements within the Aquino administration stoked the agitation to rescind the United States bases agreement which was due for re-negotiation.

Still it was clear that the Aquino administration had two major goals: to rid the country of the lingering legacy of military authoritarianism, to overcome the economic crisis and to stop graft and corruption spawned by the Marcos administration

Under these circumstances, the Aquino government was in no position to formulate a coherent foreign policy, much less attend to the Republic’s relationship with the PRC. In fact the Aquino government did not come up with a coherent foreign policy to give direction to foreign trade.

Although China was one of the first few countries that recognized the Aquino government two days after the EDSA “people power revolution.” The Aquino government did not give due attention to China. China was the one who took the initiative to revitalize its relations with the Philippines. One month after EDSA, the Chinese Minister of Culture came Manila to sign a Cultural Agreement Executive program. In May of the same year the Chinese agreed to:

1. restructure payment of \$11.2 million dollars in rice import credit given to the Marcos administration in 1985, and
2. renew a credit line for \$20 million dollars given to the Philippines by the Bank of China.

Given these developments, it was widely expected that Philippines-China relations under the Aquino administration was headed to a good start. It was speculated by many observers that Aquino would seek some form of economic cooperation with China. Some even believed that she would continue the Marcos era of good relations with China.

Expectations, however, were proven wrong. In sharp contrast to the earlier Marcos policy , when commerce, security and friendship were the substance of Philippines-China relations. President Aquino’s East Asia policy was clearly dominated by Taiwan. Indeed from the start of the Aquino administration, several “unofficial” trips were made to Taiwan by Aquino officials at all levels. Cabinet members, legislators, provincial, city and even municipal officials traveled to Taiwan, presumably, to observe Taiwan’s land reform program and other development projects. These unofficial trips did not escape the attention of the Chinese Embassy in the Philippines. Taiwan press agents made it a point to provide the names, full accounts, and details of these visits to the Philippine press and the staff in the Chinese Embassy. According to the Chinese Embassy staff these Taiwan visits by Filipino officials contradicted Philippine one-China policy. The PRC embassy ostensibly filed diplomatic protests but they were ignored, denied, or dismissed by the Philippine officials who argued that the Taiwan-China dispute was a “private or family quarrel.” An Assistant Executive Secretary and Chief of Staff of President Aquino told a public forum on Taiwan,

“RP-Taiwan Relations must be viewed within existing realities. We need to face the fact that Taiwan exists...We also cannot ignore the fact that there are Filipinos there whom the Philippine government should protect.”²¹

It took the Aquino government almost three years to reactivate RP-China relations, albeit, mainly through the initiative of Filipino Chinese who supported her presidency. In December, 1988, before her trip to China, she signed Executive Order No. 313 which prohibited Philippine government officials from visiting Taiwan. In the interim between 1986 and 1988, Taiwan continued to intensify its economic activities which could not but have political repercussions.

Although the Aquino administration officially maintained Marcos’ One-China policy, Philippines-China relations under her administration came to a near standstill.

²¹ In Raphael Lotilla’s “Comments,” *Reflections on the Framework of Manila-Taipei Relations and Current Bilateral Ocean Disputes*, IIS, UP Law Center, 1993.

The policy of maintaining trade balance continued, but was compounded by the creation of the Philippine International Trading Corporation which literally replaced the Joint Trade Committee (JTC). The JTC required importers to insure that the equivalent value be exported to China. While this requirement improved somewhat Philippines' trade balance with the China, it also brought down imports from China.²² Volume of trade may have also diminished due to political decisions to accommodate Taiwan which was seen by China as an attempt to pursue a two-China policy.

Accommodation with Taiwan was not a unilateral act of the Aquino administration alone. Although the Marcos administration opened diplomatic relations with China, it encouraged its Ministry of Trade to continue to pursue vigorous economic and trade relations with Taiwan (See Table 2).

Table 2. Philippine-Taiwan Trade*
(F.O.B. value in US\$ Dollars)

Year	Total	Import	Export
1974	107,035,517	78,888,794	28,146,723
1975	108,325,591	79,622,111	28,703,480
1976	116,449,716	74,117,624	42,332,092
1977	108,735,870	81,404,387	27,331,483
1978	173,092,353	131,816,634	41,275,719
1979	242,575,129	173,261,298	69,313,831
1980	283,220,829	182,665,981	100,554,848
1981	306,440,007	204,880,527	101,559,480
1982	276,774,230	220,114,928	56,659,302
1983	288,128,482	213,242,042	74,886,440
1984	269,205,086	177,756,435	91,448,651
1985	264,008,733	177,909,368	86,099,365
1986	403,328,904	279,662,720	123,666,184

*Source: Foreign Trade Statistics of the Philippines

Due to the long term and close Philippine relations with Taiwan based mainly on a common anti-Communist stance from 1946 to 1975, trade continued with the island state even when diplomatic relations with China was established. And KMT influence on the local Chinese and Philippine policy makers and institutions lingered.

Two other factors had prejudiced Philippine view of China during the Aquino administration. First was Taiwan's twin decision to reduce reliance on the US and Japanese markets and to corner a larger share of the Asian market. Second was Taiwan's use of flexible diplomacy to campaign for political recognition from as many countries as possible, by rejoining the UN and greater participation in world affairs through its economic clout. In the Philippines, the campaign took the form of linking political concessions to Taiwan with economic investments and aid. Officials of the Taiwan Chamber of Commerce even lobbied Philippine government to allow 100 percent foreign ownership of real estate, removal of constitutional limits on foreign ownership of stocks of Philippine corporations, and foreign participation in

²² Interview with Xue Ruixhia, Economic and Commercial Attaché of the Chinese Embassy in the Philippines, March 4, 1999.

retail trade.²³ Indeed Taiwan's initial campaign was so successful that many Philippine legislators competed with one another in initiating a review of the country's One-China policy, the passage of a Philippine-Taiwan relations Act, and granting diplomatic status to Taiwan officials and businessmen in the Philippines. No less than five bills were filed in the Philippine House of Representatives to promote trade, commercial, economic, cultural, educational and scientific cooperation. According Congressman Jaime Lopez, Vice-Chairman, House Committee on Foreign Affairs:

“Taiwan would like to have a law that will protect their investments, business interests, and properties in our country. They are probably apprehensive that if there would be unification of the PROC and Taiwan, there might be a change in the political system which would adversely affect their investments, business interest and properties in foreign countries.”²⁴

The second reason may be the propensity of the Aquino government to reject, halt, or set aside, projects initiated under the Marcos regime. Since diplomatic and good economic relations with China were initiated by Marcos, the Aquino government showed little interest in continuing such a policy.

However, Taiwan's diplomatic offensive made headway due mainly to what they themselves called “money diplomacy.”

The Taiwan campaign for diplomatic recognition was so successful that a content analysis of the major Philippines papers at that time showed much coverage of news about Taiwan financial investments. Media coverage centered on Taiwan's readiness to help the Philippines out of its economic trouble, Taiwan's superior political system following Philippine's democratic path, Taiwan's plan to establish a futuristic city in Manila, provided the Philippines can extend official protection to these economic ventures. These media blitz edged out any positive coverage about Mainland China, which had already been very skimpy to begin with.

A year of massive Taiwan media campaign and pro-Taiwan lobbying in the Congress, helped spark enormous enthusiasm for Taiwan among many Filipino political leaders. Several believed that Taiwan might indeed help set the Philippines' sinking economy afloat. After two more years of “money diplomacy,” some Filipino leaders were already talking about reconsidering the merit of the country's “one-China” policy. In Congress bills were filed proposing either to officially recognize Taiwan as separate from China, or at the very least to grant to Taiwanese citizens undertaking business in the Philippines the same rights as Filipino citizens in the acquisition of real estate and ownership of enterprises. Taiwanese officials, it was proposed, should be granted the status of diplomats. Advocates of a two-China policy in the Philippines asked: “Why not two Chinas, when the smaller one is offering to give us the resources we need for our economic recovery while the bigger one cannot?” For those who were pushing for Taiwan's line of “one-China, two governments,” they maintained that diplomatic status and the right to buy real estate

²³ “Manila Hopes for Excess Taiwan Capital,” *Manila Chronicle*, September 17, 1993. See Lee Chipongian, “Taiwan to Lend P100M for SMEs,” *Manila Chronicle*, March 21, 1994.

²⁴ Lotilla, pp. 46-47.

are small concessions in exchange for loans and investments that will help the Philippine economy turn around.

They raised question on whether it will serve Philippine national interests to isolate Taiwan in view of its rise as Asia's largest economic tiger next to Japan. Taiwan was now a member of to the Asian Development Bank and GATT.

In the Filipino Chinese community the pro-Taiwan members of the Federation of the Filipino-Chinese Chamber of Commerce, who suffered setbacks under the martial law regime, were in the forefront of Taiwan propaganda efforts.

From 1987, Taiwan's trade figures with the Philippines continued to rise dramatically, from \$264 million in 1985 to \$403 in 1986 and \$515 million in 1987. Dislodging China as the fifth largest trading partner of the Philippines. In 1988, Taiwan became the Philippines' number four trading partner (\$711,571,647), next the US, Japan, and Hong Kong, while China plunged to number twelve (\$309,084,635). From 1989 to 1991, Taiwan became the Philippines' number three trading partner, dislodging Hong Kong (See Table 3).

Table 3. Philippine- Taiwan Trade*
(F.O.B. value in US dollars)

Year	Total	Imports	Exports
1986	403,328,904	279,662,720	123,666,184
1987	516,818,930	372,430,385	144,388,545
1988	711,511,467	510,737,872	200,833,775
1989	912,097,478	701,799,164	210,298,314
1990	1,014,832,191	805,569,506	209,262,685
1991	1,034,319,245	824,596,914	209,722,331

*Source: *Foreign Trade Statistics of the Philippines*

Soon government officials were saying that the invitation to Taiwan businessmen and the Taiwan government to invest is merely an attempt to rehabilitate the country's economy rather than an outright rejection of the "one-China" policy.

In February 1989, three years after President Aquino assumed office, the Philippines and China signed an agreement to expand bilateral trade to between \$400 and \$450 million. This was lower than the target set by Marcos in 1978. The primary item that motivated the Aquino government to sign the agreement was crude oil.

On April 14, 1989, President Aquino left for China seeking to strengthen diplomatic ties and to retrace her roots in Hongjian, Fujian.

In Beijing, President Aquino met Deng Xiaoping, Premier Li Peng and President Yang Shangkun. They reiterated China's policy of non-interference in Philippine domestic affairs and their support of President Aquino's government. President Aquino was given a donation of 10,000 metric tons of rice by the PRC government. There was an agreement to further increase bilateral trade over a five year period to \$800 million.

President Aquino's state visit did not significantly change her policy on Taiwan. A year after her "sentimental journey" to China, when the Tiananmen Incident broke out, she and Filipino prelate Jaime Cardinal Sin, expressed sadness "over the violent dispersal of the student-led protest movement" in China.

On July 16, 1991, near the end of her term, Assistant Executive Secretary Rafael Lucilla, acting as Chairman of the South Sea Fishery Dispute Settlement Committee signed a Manila-Taipei Agricultural and Fisheries Agreement with Taiwan officials. Immediately after Beijing learned of the agreement, it sent a very strong protest to the Department of Foreign Affairs claiming that the agreement was illegal, for it violated the "one-China" policy. In a press interview, Foreign Affairs Secretary Raul Manglapus told the press that the Department of Foreign Affairs (DFA) had warned that such action would violate the "one-China" policy and that the DFA "has always opposed such an agreement." President Corazon Aquino announced a review of the agreement, but took no action. It was only in 1996, during the Ramos administration, that the Philippine Senate passed a resolution nullifying the Fisheries Agreement with Taiwan. On August 6, 1991 when the National Electrification Administration asked the Chinese for concession to cancel Philippine orders for hydro power machines costing \$420 million, the Chinese readily agreed to the request.

On November 2, 1991, when Fu Hao, a Chinese parliamentarian working with the United Nations called on President Aquino, the Taiwan issue was raised. President Aquino and Executive Secretary Joker Arroyo, told Fu Hao: that the Philippines pursued ties with Taiwan to help solve economic difficulties, and that such relations were strictly economic and not political relations.

During President Aquino's six years in power, her attention became more and more focused on talks with Taiwan officials for economic support and investments but such efforts achieved little progress. As one paper noted:

"Taiwan has taken an exploitative attitude towards us mainly because of our unstable economy, the beggarly attitude and ulterior motives of our government officials frequenting Taipei and a faint hearted political leadership."²⁵

Indeed near the end of Aquino's term, Taiwan withdrew several of their so-called mega-industrial investment projects slated in the Philippines, including the controversial Luzon Petrochemical Plant. Chairman Joker Arroyo of the Philippine National Bank claimed that the Luzon Petrochemical Corporation did not intend to bring in capital but will borrow heavily from local banks. Subsequent to Arroyo's revelations news about Taiwanese maltreatment of Filipino overseas contract workers, Taiwanese speculation in real estate, Taiwanese involvement in kidnapping, and smuggling of Taiwanese agricultural products into the country and smuggling out of Philippine rare resources into Taiwan began to fill the pages of Philippine newspapers. Close Philippine-Taiwan relations during the Aquino administration had turned back the RP-PRC cooperation cultivated earlier by President Marcos.

²⁵ *Philippine Daily Globe*, "Tact and Taiwan," September 17, 1989.

There is no doubt that Philippine diplomatic dalliance with Taiwan and the creation of the PITC had contributed to the downward trend in RP-PRC trade. Conventional wisdom that bad political relations led to bad economic relations was proven correct by events during the Aquino administration.

Unfortunately President Aquino's pursuit of economic diplomacy with Taiwan did not progress beyond her administration. Taiwan's promises to help build the Philippine economy failed to materialize when Aquino stepped down as President.

The Aquino government was so single minded in seeking Taiwan economic support that it overlooked the phenomenal rise of China's economy and therefore failed to use it as a "benevolent stimulus" to its own economic growth.

Political Economy under the Ramos administration:

Unlike President Aquino, President Ramos took immediate steps to mollify the Chinese. He made a state visit to China from April 26 to May 1, 1993. His agenda ranged from the expansion of commercial relations with China to the resolution of the Spratlys dispute. To emphasize the agenda, President Ramos not only ordered the termination of the trade balancing program but brought with him six top Filipino Chinese tycoons to China. The new trade protocol encompassed pledges of best-efforts on the part of the Philippines to buy Chinese power plants, transmission lines and towers, transformers, metal manufacturing and road building equipment, electrical products, coal, textiles, steel billets, mineral products, chemicals, cotton, foodstuff and other consumer items. For China's part it will buy Philippine phosphatic and compound fertilizers, chromite ores, copper cathodes and concentrates, tin plates, cold-rolled steel, manganese, coconut oil, fatty acid and alcohol, bananas, coffee beans, and shelled cashew.

The Ramos delegation also signed fourteen joint venture agreements. China offered a \$25 million energy loan for the construction of mini-hydro electric plants and the commercial credit for two coal-fired power plants. At the same time, President Jiang Zemin donated \$434,000 to victims of Mt. Pinatubo.

During the meeting between Presidents Ramos and Jiang Zemin, the Chinese host assured President Ramos that China does not have any expansionist ambition and that its arms build-up was part of its modernization program. The Chinese emphasized the importance of shelving the sovereignty issue over the Spratlys while President Ramos reiterated the importance of abiding with ASEAN's Manila Joint Declaration to settle differences peacefully. President Ramos reassured the Chinese that his administration will adhere to the one-China policy despite his meeting with Lee Teng Hui at Subic.

The Sino-Philippine Joint Committee on Scientific and Technological Cooperation held its tenth session in Beijing on June 23-26, 1994 and signed the Tenth Protocol on Scientific and Technological Cooperation between China and the Philippines.

During the end of his visit, President Ramos invited President Jiang Zemin to visit the RP. President Jiang Zemin accepted the invitation and immediately after the APEC Summit in November 1996, he made a state visit to the RP. It was the first

time in Philippine history that the highest Chinese official made a state visit to the country.

During President Jiang's visit, two agreements were signed between the two countries on November 26, 1996. One was Agreement Between the Government of the Republic of the Philippines and the Government of the People's Republic of China on the Establishment of Additional Consulates.

The Chinese government gave its consent to the Philippines' establishment of a consulate-general in Guangzhou, with a consular district comprising Guangdong Province, Guangxi Zhuang Autonomous Region, Hainan Province and Hunan Province. In addition, consular district of the Consulate-General of the Government of the Republic of the Philippines was established in Xiamen comprises Fujian Province, Jiangxi Province and Zhejiang Provinces.

The Philippine government gave its consent to the Government of China for reserving the right to establish a consulate-general in Davao, with a consular district comprising Basilan, Sulu, Tawi-Tawi, Zamboanga del Norte, Zamboanga del Sur, Agusan del Norte, Agusan del Sur, Davao del Norte, Davao del Sur, Davao Oriental, South Cotabato, Surigao del Sur, Lanao del Norte, Lanao del Sur, Maguindanao, North Cotabato, and Sultan Kudarat.

The other agreement was for the Maintenance of the Consulate-General of the Republic of the Philippines in Hong Kong Special Administrative Region of the PRC.

The most controversial issue between the Philippines and China during the Ramos administration centered on rival claims on the Spratly islands West of Palawan. This occurred even after an agreement was signed during President Ramos' state visit to the PRC. The agreement stated that both countries would shelve the sovereignty issue, and adhere to the 1992 ASEAN Manila Declaration enjoining all claimants in the Spratlys to settle their conflicting claims peacefully.²⁶

After the Ramos visit, cooperation between the two countries went on smoothly until China's occupation of the Mischief Reef in 1995, recurrent entry of

²⁶ China, Taiwan, and Vietnam claim all the islands in the Spratlys. The Philippines essentially claims only the western section of the Spratlys, or the Kalayaan Island group, an assortment of about 51 islands, islets, reef, shoals, cays, and rocks, depending whether it is high or low tide, the group is nearest to Palawan but which also contains most of the larger islands in the archipelago. Malaysia claims only three islands it presently occupies, as well as Amboyna Cay which is held by Vietnam. Brunei has staked its claim to Louisa Reef, one of the Southern Shoals of the Spratlys which is underwater. Vietnam occupies 25 islands with its main base on Spratly island (Truong Sa). The Philippines holds eight islands with its base on ThiTu Island (Pagasa). China holds eight islands. Malaysia has three and has opened Swallow Reef (Torumbu Layang Layang). Taiwan holds Itu Aba, the largest of the Spratlys.

Actually the conflicting claims on the Spratlys were considered resolvable by the Chinese even as early 1972, long before diplomatic relations was established between the Philippines and China. The issue of ownership was raised with the PRC when Senator Salvador Laurel visited China in March, 1972.

Senator Laurel reported that then China's Vice Minister for Foreign Relations "made it clear that China had always regarded the Nansha Island as part of her territory. When I advised him that the Philippines also has an interest in the islands, he politely replied that in view of the absence of diplomatic relations our conflicting claims could not be discussed. The Vice Minister said that the potential dispute could be settled over the conference table." (See *Laurel Report: Mission to China*, (March 12-22, 1972), 185 pages.

Chinese patrol boats, fishing vessels, and the attempted occupation of the Scarborough shoal. These developments not only engaged the attention of the Ramos government but led to confrontational behavior that soured Philippine-PRC diplomacy over the Spratlys. It also gave the Department of Defense reason to lobby for an increase of its budget in order to modernize its defense structures. And it led the Department of Foreign Affairs to shift its strategy from quiet diplomacy to “internationalizing the issue,” by questioning the legitimacy of China’s occupation of the Mischief Reef in international forums. It has also brought Congress into the controversy, and has convinced many of its members to seek stronger security arrangement with the United States of America. Some of its members have questioned the wisdom of the Philippine Senate in rejecting a new agreement on the American military bases rejected during the Aquino administration. They claimed that with the presence of the American bases, the Chinese would not dare occupy the islands. The Philippine military interpreted Chinese presence as: “invasion,” “intrusion,” “violation of Philippine territorial sovereignty,” and “occupation” of Philippine territory and waters. Since 1995 the Philippine military considers Chinese presence in the Mischief Reef as a threat to Philippine security.

In 1995 it was feared that friendly relations between China and the Philippines would deteriorate after Chinese occupation of the Mischief Reef. In fact most observers linked Chinese occupation of the Mischief reefs with commercial and trade issues. They argued that commercial relations would only improve if and when the Chinese occupation of the Mischief Reef was resolved. Several Filipino political leaders demanded that the Chinese leave Mischief Reef as a precondition to improved Philippine-China relations.

Indeed over the past decade there has been a tendency by many observers to associate political developments with economic performance. For instance some quarters have claimed that rampant kidnapping of ethnic Chinese in the Philippines have led to flight of their capital to China. There is also talk that the tension in the Mischief Reef could only exacerbate our commercial relations with China.

We were told that from an international relations perspective and particularly from a political standpoint security concerns that are given primary importance as in the case of Chinese occupation of the Mischief, would reduce trade activities. Yet a review of trade statistics from 1995 to 1998 appears to prove these observers wrong (See table 4).

It appears that despite the China’s construction of a structure over the Mischief Reef in 1995 and with the controversy it has spawned since then, trade volumes between the two countries have increased dramatically over the same four year period. (See Table 4)

Trade volume increased from \$456.7 in 1994 to \$1306 in 1995 or an increase of 65 percent. Indeed the trade volume increased more markedly in 1997 when the Mischief Reef controversy became more pronounced and the Asian financial crisis occurred. More striking perhaps is the fact that while the trade volume between China and the Philippines increased during the 1997 financial crisis, China’s trade volume with other ASEAN countries plummeted significantly.

Table 4. Philippine Trade With China
(in million US\$)

Year	Total	Exports	Imports
1998	2013.00	512.00	1501.00
1997	1666.00	327.00	1339.00
1996	1387.00	372.00	1015.00
1995	1306.00	275.00	1030.00
1994	456.97	163.94	293.03
1993	354.53	173.87	180.66
1992	297.64	113.9	183.74
1991	351.27	127.77	223.5
1990	223.86	61.76	162.1
1989	271.33	50.23	221.1
1988	309.08	66.8	242.28
1987	293.51	87.95	205.96
1986	215.38	104.69	110.69

This is also true with Chinese investments in the Philippines. From 1995 to June 1998, when the Mischief Reef issue was smoldering, China opened over 100 enterprises with a total investment of over US\$140 million. And then at the height of the Mischief Reef controversy, when the Philippines threatened to internationalize the issue, two of the largest corporations in China set up subsidiaries in the Philippines. The Haier Group of China setup a subsidiary company for production and marketing of air conditioners in the Philippines and the China National Technical Import and Export Corporation (CNTIEC) established the CNTIEC Philippine Mechanical and Electrical Products Co. Ltd.. Currently Harbin Power Engineering Company Ltd., is engaged in a project of coal power station in Mindanao, the investment totals \$220 million. For this project China will provide \$165 million of seller's credit.²⁷

It appears that these new subsidiaries are direct mainland ventures and have no capital contributions from the Filipino Chinese. Chinese investments were brought in by the Ramos liberalization policy and as part of the broader incentive measures extended for foreign investments. Moreover the Chinese believe that they have comparative advantage over competing industries as they have newer technology and machinery. Chinese FDI ventures was started in 1995. The investments were mainly in selected ASEAN countries such as Malaysia, Thailand and in 1997, the Philippines. These ventures were undertaken with Chinese government encouragement.

Foreign Direct Investments in China

It is significant to note that Filipino-Chinese businessmen did not make significant investments in China until 1984-1985. Notwithstanding close accommodation between the Marcos regime and the Chinese government, and despite frequent trips (10 years) made by Filipino-Chinese businessmen to China to explore business opportunities there, no large investments were made. This is surprising considering that there was a flurry of foreign businessmen wanting to invest in China once the country opened up its economy. China shifted its policy dramatically on FDI,

²⁷ "The Sino-Philippine Economic Trade Relations toward the New Century," paper presented by Ambassador Chen Shenglou at *The Philippines and Northeast Asia in the 21st Century*, February 8-9, 1999, Manila, Philippines.

from prohibition to active encouragement of FDI. In 1979 China instituted its Four Modernisations Program and passed the Joint Venture Law in the same year. Most Filipino-Chinese businessmen who have businesses in China before 1984, explained why they were hesitant in investing in China. They were uncertain of the Chinese “Command economy.” Moreover there were no clear rules on protection and security of foreign investments, and they were fearful that under the Communist system, their investments to be under the control of the Communist regime. Furthermore, the centerpiece of China’s formal FDI promotion during the early 1980s were confined to the Special Economic Zones (SEZs) in southern China and the Export Processing Zones (EPZs) whose operations were unfamiliar to the Philippine Chinese. Records of foreign direct investment (FDI) into China from the Philippines confirmed these accounts (See Table 5). In contrast between 1979 and 1983 there were already increasing foreign direct investments into China increased from Japan, Hong Kong, Macau, Singapore, Thailand, United Kingdom and even the United States. These foreign firms, to use a phrase of Krugman, took advantage of the “fire sale” in China in the opportune time.²⁸ FDI into China reached US\$386 million in 1982, going up to US\$4 billion in 1991, US\$7 billion in 1992, US\$23 billion in 1993 and US\$33 billion in 1994. The only other country that surpassed the volume of FDI was the U.S.

Except for San Miguel Corporation, most FDI into China has been undertaken by the ethnic Chinese in the Philippines. Parenthetically some political analysts claim that Philippine Chinese FDI flow cannot be regarded as foreign since Filipino-Chinese share common language and culture with the Chinese. However such investments still fall under the category of FDI since they emanate from the Philippines and from Filipino citizens.

Unlike overseas Chinese investors from the U.S., Hong Kong, Singapore and Thailand who invested in hi-tech industries and heavy industries,²⁹ most Filipino-Chinese investments are mostly in medium and small scale enterprises. These were limited banking operations, travel agencies, processing of junk food, manufacturing of nails, bolts, nuts, road and building construction, bags, umbrellas, wallets, shirts, groceries, bakeries, printing shops, real estate directed at residential housing, retail complexes, and assembly of computers. Philippine FDI into China went down from \$15.53 million in 1988 to \$4.71 in 1989 due mainly to the Tianamen Incident. But from 1991, due to liberalization of foreign capital participation in property development led to significant inflows of Philippine FDI into China (See Table 5). The investment increased from \$17.44 million to \$276.11 million in 1992 and more than doubled to \$630.63 million in 1993.

Filipino-Chinese who have good knowledge of business in China, distributed their investments among different and already established industries in China such as breweries, cigarettes, hotels, recreational resorts, manufacturing of rubber shoes, air-conditioners, and household appliances. One of the reasons given for investing in established Chinese industries was to take advantage of product identity in the host country. Many products of the newly established industries are not known to the Chinese customers. Except for San Miguel Beer, the Philippines has no other brand

²⁸ See P.R. Krugman, “Fire-sale FDI,” MIT, <<http://web.mit.edu/krugman/www/>>.

²⁹ See Tao Qu and M.B. Green, *Chinese Foreign and Direct Investment: a substantial perspective on location*, 1997.

names known in China. Partnerships were also preferred for these allowed them to overcome impediments arising out of local and arcane “rules of the game.”

Table 5. Foreign Direct Investment into China from the Philippines*
(Amounts in US\$ million)

Year	Number	Amount
1984	4	2.1
1985	22	40.56
1986	9	3.81
1987	10	30.5
1988	22	15.53
1989	12	4.71
1990	18	10.78
1991	30	17.44
1992	153	276.11
1993	302	630.63
1994	162	290.69

Source: Department of Trade and Materials Business, *China Foreign Economic Statistics 1979-1991*, 1992. *China's Statistical Yearbook 1995*, 1996. *Almanac of China's Foreign Economic Relations and Trade 1995-1996*.

Compared to Hong Kong's 60%, Japan, Taiwan and the U.S. 10% respectively, and EU's 5%, Philippine FDI in China is miniscule only 0.5% of the total FDI into China in 1992.³⁰ As with all early foreign investors, a large number of these investments were not profitable. Interviews with most medium and small enterprise Filipino-Chinese investors in China from 1987 revealed that their investments in real estate and small scale manufacturing were wiped out long before the 1997 financial crisis. This is particularly true to real estate investments which is a “high-risk and high-return investment.” Their early loses were due to fierce competition from other overseas Chinese investors from Hong Kong, Taiwan, Malaysia, and Thailand. They also found that after the first five years of tax and other incentives there was no other support from the local Chinese government. After five years when tax exemptions and other investment incentives lapsed, their competitive advantages virtually wiped out by businesses of the host country. It appeared too that by the mid 1990s, China was more interested in drawing FDI into technology intensive industries. Moreover China was more interested in channeling FDI into large-scale, and advanced technology intensive industries. On the other hand, China was no longer interested in attracting FDI whose products were intended solely for the China market. They want production for both domestic and foreign markets. This rules out most of the FDI in medium and small scale industries. “By 1994 foreign-funded enterprises accounted for 15 times more exports than would have been expected on the basis of their contribution output.”³¹

³⁰ See China's Ministry of Foreign Trade and Economic Cooperation, Reported by *Business China*, June, 1993.

³¹ See Nicolas Lardy, “The Role of Foreign Trade and Investment in China's Economic Transformation,” in A.G. Walder, *China's Transitional Economy*, Clarendon Press, Oxford, 1996.

Conclusion:

It is clear that from the 1995 to 1998 trade and investment data, that bad political relations such as the conflict over the Scarborough Shoal and the Mischief Reef did not lead automatically to bad business relations. Neither did the investment data show that the increase in Philippine investments in China were capital flights or the direct outcome of rampant kidnapping of Filipino Chinese. Rather it was the result of the attempt of some Filipino Chinese to take advantage of China's liberalization policy that allowed foreign capital participation in real estate development in that country. The trade and investment data also show that it was President Ramos' policy under Executive Order 244 that abolished the strictures on trade balancing policy that led to the remarkable increase in trade volume between the Philippines and China. It is also clear that not only correct economic policy such as EO 244 can hardly be deterred by bad political relations, it can even overcome the adverse effects of the 1977 financial crisis in Asia.

In principle, there is no necessary connection between good politics and good commercial relations but they can be complimentary. In the history of the political economy of Philippines-China relations they need not go hand in hand.

A major concern which is not explored in this paper is when does bad political relations affect good economic relations. Given the difficult sovereignty issue on the Mischief Reef, Taiwan pressure for the Philippines to issue a visa to President Lee Teng Hui, and the periodic threat of our legislators to pursue a two-China policy, at what point will China continue to regard the Philippines as a good market and good environment for investment. Conversely given so much the heated controversy over the Kalayaan Island Group, illegal entry of Chinese traders, hostesses, and fishermen in our waters, will Philippine political leaders provide a more favorable investment environment to the Chinese? Will they grant the same incentives extended to other favored nationalities in the Philippines?

Given China's economic growth for the past twenty years, China's trade and investment policies are beginning to be governed by more objective economic considerations. But many Chinese political leaders still maintain the long-held view that politics is an important factor in foreign and economic policies. This means that the size of our trade and China's investments in the Philippines will depend in part on our wise cultivation of friendly and cordial relations with each other.

The principal issue for the Philippines is not whether our economies are complementary or competitive, whether the sovereignty issue over the Spratlys should be resolved bilaterally or multilaterally, but the extent to which we could convince China that cooperation in all fronts is in our mutual interest. Certainly a modernized China and an economically strong Philippines will make good political allies.

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