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Geoeconomic Dynamics in a Changing Regional Order: A Primer for Sri Lanka's Foreign Policymakers

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Geoeconomics, i.e. the intertwining of economic and geopolitical factors, has come to affect the Asian region in three ways. Firstly, it has led to the rise of an economically interlinked pan-Asian region. Secondly, this pan-Asian economic space has become a site of competition between various ‘rules regimes.’ Finally, geoeconomic forces are increasingly reshaping countries’ domestic institutions and policies, resulting in a ‘domestication of foreign policy.’

I. Introduction

It is commonplace to argue that one of the defining features of the current global order has been the emergence of geoeconomic strategies and instruments to pursue both commercial and diplomatic interests. The term ‘geoeconomics’ can broadly be defined as the [interplay between economic and geopolitical factors](#)¹ – referring to either the geopolitical consequences of economic policy or phenomena, or the economic consequences of geopolitical trends and national power.

There is ample evidence that global conflict and changes entangle both, economic and geopolitical factors. Take, for example, the South China Sea (SCS) dispute, which is often considered to be a prime example of geopolitical conflict. Much of this dispute is driven by economic factors, namely, the struggle for the SCS’ energy and fishing resources. Another example, is the Australian Aid programme that has been reorganised to pursue more clearly the commercial rather than political objectives of the Australian government; a development that can be described as a [geoeconomic shift in Australia’s foreign aid](#).² In Sri Lanka, the long lease of land and associated sale of equity in the Hambantota port to Chinese interests, along with the wider domestic and international political and strategic ramifications of this sale, demonstrate how geoeconomic strategies affect the regional political and strategic order.

This *Policy Brief* analyses the nature of this geoeconomic order that is reshaping the regional order, and considers its implications for the conduct and management of Sri Lankan foreign policy. As such, this is a heuristic paper that is intended for policymakers.

This brief explains basic aspects of and challenges to geoeconomic theory, before making three key arguments about the emerging geoeconomic forces that are shaping the region. First, there is a process of ‘Asianisation’ that is creating a coherent and contested economic and strategic space across the Indian and the Pacific Oceans. Second, there are multiple organisational frameworks that govern these coherent strategic spaces, which involve several competing ‘rules regimes’ that are now evident across the region. Finally, geoeconomic strategies and associated conflicts are being funnelled through national political systems in way that is reshaping the state apparatus. This is a process that can be described as the domestication of foreign policy. Foreign policy makers, therefore, need to adapt to a complex web of policy and politics that cuts across traditional national and international divides that has defined traditional diplomacy.

II. How does Geoeconomics Work?

The logic of geoeconomics was [spelt out by Edward Luttwak](#),³ who popularised the term ‘geoeconomics’ in the early 1990s as a way of describing the changed commercial and security dynamics of the post-cold war period. At the time, the term did not have much of a

scholarly impact, but it came to take on greater significance in the early part of the 21st century with the economic rise of China. Luttwak's key point was that the waning of the Cold War reduced the importance of military power and correspondingly, it increased the importance of commercial tools and power.

Despite this valuable insight, Luttwak's explanation remains somewhat unsatisfactory for three key reasons.

1. Firstly, Luttwak's analysis separates economic forces from geopolitical forces, obscuring the way in which the two remain deeply intertwined. Luttwak and other neoconservatives such as Fukuyama, displayed a post-cold war optimism that left behind the cold calculation of military conflict for the less threatening conflicts of commercial interdependence. Yet, their perspective missed the fact that it is the entanglement of the economic with the geopolitical that is the most defining feature of the post-cold war era. One only has to see how the Belt and Road initiative (BRI) sponsored by the Chinese government is an economic as well as a security initiative. This is a point that is evident for many Sri Lankans.
2. Second, Luttwak's perspective too quickly dismisses the continuing relevance of territoriality in new geoeconomic spaces, such as the space of 'Eurasia' associated with the BRI, and the 'Indo-Pacific' now advocated by the US and its allies. These spaces are not simply a matter of moving commodities, data or labour but have a distinctive cartography. The BRI is explicitly cartographic with its sea and land routes, and it has – in keeping with its infrastructure – a discursive and material focus on creating land and related infrastructure. A Sri Lankan example would be the 'Port City' (renamed by the current government as the Colombo International Financial City), with its reclaimed land and infrastructure being built near the Colombo harbour.

In a similar way, the US – particularly through its [military command](#) plan – has created territorial rights of way for its military and commerce, especially in what it now defines as the Indo-Pacific region. The US Central Command, for instance, aims to strategically control territory in the Middle East for both commercial and military purposes. The US Pacific Command champions freedom of navigation, underlining the centrality of territorial control for US commerce and security. Such assertions of freedom of navigation – under the broader rubric of 'free and open Indo-Pacific' have taken on greater salience with the rise of China and its strategic challenge for the role of the United States in the Indo-Pacific. The foregoing examples demonstrate the continuing relevance of territorialisation – albeit in very different ways – in which economic and security concerns remain intertwined.

3. Third, in Luttwak's geoeconomic argument, domestic politics and state institutions are not sufficiently explained or understood. He overlooks a constant in geoeconomic strategies, which is the domestic political conflict that has resulted from geoeconomic strategies and projects. For example, Chinese investment has led to intensified domestic political concerns and conflicts in states like Sri Lanka and Myanmar. Geoeconomics is as much about the domestication of external conflict and emergence of commercial and political intermediaries linked to these investments and associated rule systems as it is about the pursuit of foreign economic strategies.

Simultaneously, alongside these economic strategies, there have been significant changes in the nature of the state institutions and policies that have been pursued. The integration of trade policy into the Australian and Canadian foreign ministries and of economic diplomacy into the lexicon of Sri Lanka's [foreign ministry](#),⁵ for instance, highlights the increasing geoeconomic mission of foreign ministries. At the same time, geoeconomic strategies have become the focus of a whole host of other ministries and government agencies. India initiated its 'Act East' initiative which, even if a largely rhetorical strategy, enjoins national and subnational actors to actively participate in a geoeconomic approach. The prevailing geoeconomic trend and climate have the evident potential to unsettle domestic or national political and social structures, and to transform state institutions and processes.

The next section of this brief charts the way in which such geoeconomic strategies have reshaped the Asian region. It explores the impact of geoeconomic forces in three key respects: first, in the emergence of an economically interlinked pan-Asian region; second, in the contest between multiple and competing regulatory regimes; and third, in a domestication of foreign policy. In each of these respects, I note the implications of these dimensions for Sri Lankan foreign policy.

III. The 'Asianisation of Asia'

Throughout the twentieth century as well as in this twenty-first century, there have been a number of attempts to imaginatively and materially construct a pan-Asian economic, political, and cultural sphere. In the early part of the twentieth century, Rabindranath Tagore dreamt of a pan-Asian community linked through a common pan-Asian spiritual heritage. The wartime Japanese project conceived an imperialist vision of a [pan-Asian continent](#),⁶ indeed similar in territorial shape to what is currently being conceived of as the Indo-Pacific. In recent decades, former Malaysian Prime Minister Mahathir Mohamad advocated the East Asian community as a [pan-Asian region](#).⁷ These regional political projects were all shipwrecked on shores of geopolitics.

However, the rise of China – or more precisely the capitalist transformation of China – is binding the region in a way that was previously inconceivable. In both demographic and economic changes, the broader Asian region, from West Asia through South Asia and into East Asia, is being bound together. This is most evident in the increasing rise of intra-regional trade. Intra-regional trade in East Asia has risen significantly over the last decade, with this subregion being much more integrated than other subregions - especially when compared to South Asia. A report published by the [ADB in 2016](#),⁸ however, also points to the growing share of inter-regional trade across the South Asian subregion.

This growth in intra-regional trade should be seen in the context of China's export of capital to the region. This export of capital is driven by China's investment regime, which relies heavily on investment for economic growth. This has resulted in the export of excess capacity through various mechanisms such as the BRI. A look at the cartography of the BRI makes the [pan-regional nature of this investment](#)⁹ starkly evident. It is clear that this investment is being spread across the Asian region, helping to bind the various subregions. In short, the capitalist transformation of China is now creating a more integrated region.

The upshot of these sweeping changes is that the post-cold war order, driven by transnational economic forces that are increasingly centred endogenously in Asia, have reversed the colonial and cold war segmentation of Asia. This order has accelerated inter-Asian connections and brought with it new social forces, such as business capital; linked (albeit not exclusively) to China-focused economic circuits. In a recent stimulating paper, Nick Bisley has argued that this enhanced connectivity is producing an integrated Asia with a strategic coherence. He [notes that](#):¹⁰

“Integrated Asia’s strategic environment will be shaped by the interplay of a small number of very large powers, and a larger number of lesser powers. Due to the constraints of scale as well as their economic interdependence, none of Asia’s powers will be able to become hegemonic, nor will they produce some new version of US primacy.”

The implications of these developments for Sri Lankan foreign policy are far reaching. Two key implications can be described as follows:

- Sri Lanka needs to pursue its political and economic diplomacy from a more integrated and strategic ‘whole of Asia’ perspective which Bisley is suggesting is now at the core of diplomatic and strategic initiatives. This would mean placing less emphasis on subregional issues and more focus on building coalitions and niches across an integrated Asia. One practical policy that may ensue from such an approach is for Sri Lanka to work incrementally towards joining pan-Asian multilateral free trade agreements like the Regional Comprehensive Economic Partnership (RCEP).
- An integrated Asia also calls for a ‘turning east’ in Sri Lanka’s foreign and economic policy towards countries such as Vietnam, Indonesia and South Korea, with whom Sri Lanka needs a more concentrated diplomacy. To reorient its foreign policy in this direction, Sri Lanka should expand its expertise and connections – both economic and cultural – in East Asia. There is already evidence of such a geoeconomic policy shift, as indicated by Sri Lanka’s recently signed Free Trade Agreement (FTA) with Singapore and its [potential FTAs with Malaysia, Indonesia and other Asian countries](#).¹¹

IV. Contested Regulatory Systems in Asia

Alongside this increasingly integrated economic and strategic system in Asia, there is growing contestation over the different rules and rule systems that may apply to competing transnational projects in Asia.

There are three key developments or elements of these regulatory systems to bear in mind.

- First, there is a fracturing of the US-centred multilateral trade systems, including the World Trade Organization (WTO), and regional groupings such as Asia Pacific Economic Cooperation (APEC), which are now weakened or unable to advance trade initiatives
- Second, the Cold War-based subregional strategic systems in the Pacific are also in decline. They have been replaced by more competitive pan-Asian or Indo-Pacific

systems of regulatory control, such as the Trans-Pacific Partnership (TPP) and competitive Chinese-centred regulatory systems like RCEP and the Asian Infrastructure Investment Bank (AIIB). It is these competing regulatory systems and geographies that increasingly characterise the Indo-Pacific.

- Third, there is an economic and security nexus that lies at the heart of these competing regulatory systems and geographies. For example, the recently resurrected TPP is both a trade and regulatory agreement as well as bringing into its fold US allies and strategic partners. Indeed, strategic partnerships have become increasingly important for the US and these partnerships are commercial as well as strategic. In the similar way, the Pakistan and China economic corridor is both a commercial, financial and strategic complex that ties economic and security within novel forms of territorialisation. It is this security and economic nexus that drives the competition between what we term systems of regulatory geographies.

Implications of the TPP

The TPP provides an insight into this emerging and contested regulatory framework in the Indo-Pacific. Since the election of Donald Trump, the [TPP has proceeded without the US, but there are signs of renewed US interest](#).¹² I would suggest that the geoeconomic strategy of the TPP is not about containment, but about the ‘regulatory disciplining’ of China and the broader regional economy. The TPP seeks to bring its own particular version of regulatory order and coherence to the increasingly interlinked regional economy.

If we adopt this perspective, we see that the TPP is constructing and shaping regional regulatory regimes that overlap and reach into domestic institutions, including those that nationally govern law and trade. While China is perhaps, the most important facet of this emerging regulatory geography, we should not overlook the broader regional implications of the TPP.

For example, in the area of public health, the TPP may lead to changes in intellectual property laws and regulation, which will shape the cost of drugs and the availability of generics – all of which are crucial to public health in the region, even in non-TPP countries. In essence, the TPP has to be seen in terms of a broader regulatory contest that is taking place across the Indo-Pacific region, on varied issues. These regulatory contests are also at play in the evolving discussion over the Transatlantic Partnership, which is similarly driven by geo-regulatory concerns.

Implications of RCEP

The Chinese-led RCEP was first [announced in Bali in 2011 at the ASEAN Leadership Summit](#),¹³ as a multilateral trade initiative that seeks to give regional coherence to trade agreements across the region. Although promoted by China, RCEP recognises the central role played by the Association of Southeast Asian Nations (ASEAN) in Asia, and accordingly, ASEAN has been pivotal in shaping the nature and form of this trade agreement.

A key dimension of RCEP has been its focus on coordinating trade facilitation regimes across Asian jurisdictions. This focus can foster greater regional coherence in industrialisation, and especially of the supply chains that are linked to the Chinese economy

which form a key feature of the ‘Asianisation of Asia.’ Hence, RCEP’s rules of trade facilitation and its other measures of liberalising trade, amount to a [distinctive framework of regulatory control and governance](#);¹⁴ through which Chinese state projects can (i) mediate contradictions that stem from uneven national systems, and (ii) further China’s capitalist transformation.

Net Implications for Sri Lanka

The emerging contested regulatory systems in Asia have a number of implications for Sri Lankan foreign policy, including the following.

- Sri Lanka should give a high priority to understand and possibly, join these regionwide regulatory initiatives, in comparison with subregional proposals. This does not mean abandoning subregional proposals – like the proposed FTA of the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) – but rather, consider and pursue such subregional proposals in the broader context of competing systems of regulatory geographies.
- As a related matter, the emergence of such regulatory geographies will require significant national investment in technical and policy expertise that can feed into foreign policy.
- All trade and security proposals need to be seen in the context of the nexus between economics and security that is driving these transnational state projects such as RCEP, BRI, and TPP.
- Finally, competitive regulatory systems may allow some countries greater flexibility and potential bargaining power that could be used in a nimbler foreign policy. The competition allows a greater ‘voice’ for smaller states in the construction of such regimes. Such flexibility, however, will require coalition-building on issues with like-minded states and other actors, and which should be a significant dimension of policy planning.

V. The Domestication of Foreign Policy

The rise of competing systems of regulatory geographies – like BRI, TPP and RCEP – is underpinned by a broad range of domestic economic and social forces. These political and commercial intermediaries are crucial to the domestic coalition that underpin these competing regulatory geographies. Consequently, these competing regulatory geographies are breaking down the boundary between the internal and external, in a way that is challenging traditional ways of making foreign policy. For example, in Australia, there has been a perception that local [political leaders have become increasingly involved on the boards of key Chinese companies](#).¹⁵ The emergence of such intermediaries linked to the state and political apparatus creates the possibility that competing rules systems points to fractures and contestation within the state.

The distinctive nature of China’s transnational capital – especially, in its state enterprises – makes the involvement of other countries’ political actors crucial to the success of these enterprises, especially as the enterprises often depend on national regulatory approvals and carry security implications. [China’s long lease of the port of Darwin in Australia](#),¹⁶ which

had domestic political repercussions in Australia, is a prime example of this scenario. The nub of the issue is that the increasing geoeconomic veneer of these competing rules systems will puncture the walls between domestic and foreign policymaking, in a process that can be described as the ‘domestication of foreign policy.’

The domestic impact of these new regulatory and geoeconomic pressures has three main aspects, as explained below.

1. First, the expansion of transnational capital from China and elsewhere creates a set of domestic business and political interests that are linked to this export of capital creates supportive coalitions for competing regulatory systems. In other words, not only is foreign policy increasingly shaped by domestic politics, but domestic politics is also shaped by complex geoeconomic forces. Understanding the nature of such domestic-foreign linkages is pivotal for understanding the complex terrain on which foreign policymakers currently operate.
2. Second, economic and security linkages will shape and possibly fuel domestic political conflicts. In Myanmar, for example, the construction of dams by Chinese interests has exacerbated domestic conflicts because these large hydropower dams have been associated with serious violations of human rights, including forced relocation and the increasing militarisation of areas surrounding the dams. These projects have, therefore, given rise to political resistance by local inhabitants, which in turn led to increased repression by military authorities. Such politics and associated conflicts bring into play a wide range of actors – both domestic and foreign – whom policymakers need to understand.
3. Finally, this domestication of foreign policy takes place both within and across state and political institutions. The complexity of domestic conflicts and the range of actors involved means that geoeconomic initiatives often entangle very different parts of the state apparatus. These include defence ministries and core economic agencies such as ministries of finance and central banks, all of whom play an important role in the negotiation of the regulatory systems described above.

The increasing involvement of these state agencies, as well as the resistance and conflict around various projects – at the regional or the local level – may lead to fragmentation and even political paralysis. Similarly, subnational actors could come to play a crucial role in these projects. For example, the provincial government of Yunnan has played a significant role in managing and advocating projects across the Mekong region. The thrust of the argument here is that geoeconomic strategies involve shifts of power and authority within the apparatus of the nation-state, which has substantive implications for the conduct and management of foreign policy.

Implications for policymakers

The domestication of foreign policy has the following implications for policymakers.

- Policymakers need to understand that formulating and implementing foreign policy involves a greater range and diversity of actors than previously. This means that policymakers need to understand the political economy of support and resistance for

various projects that the government might adopt or reject. This form of applied political economy analysis is being increasingly used in the area of aid and development, and such analysis should be extended to the field of foreign policy. An effective and politically sustainable foreign policy will require greater capacity and expertise to undertake such an applied political economy.

- Policymakers also need to consider developing more cohesive and strategic units to bring together various agencies and actors within the state. In a recent paper published in Australia, [Michael Wesley has argued](#)¹⁷ that Australia needs to consider “the structures for integrating our international economic and strategic decisions.” He suggests that a central executive agency be situated in the Prime Minister’s Office to undertake such strategic tasks. The same can be said for Sri Lanka, even if the location of such an agency will be a politically and bureaucratically sensitive issue.

In the context of the new reality of a multipolar global economy, Sri Lanka can be seen as updating – rather than abandoning – its traditional stance of non-alignment. Sri Lanka played a historically important role in the non-aligned movement that emerged during the Cold War. The question Sri Lanka faces today is how it should practise that non-alignment in a world where the established Western powers are in a state of flux and where the new and rising powers are much closer to home, as seen by China becoming the [world’s largest economy in terms of ‘purchasing power parity \(PPP\)’](#)¹⁸ and India being predicted to overtake the US as the world’s second-largest economy in PPP terms by 2050¹⁹.

Sri Lanka’s move to a new non-alignment is manifesting itself in several ways, two of which will be mentioned here. The first is that Sri Lanka appears to be distinguishing more between the principle of non-alignment and the political grouping of the Non-Aligned Movement (NAM), with a stronger focus on the principle. This is because the principle of non-alignment remains helpful in maintaining and strengthening Sri Lanka’s good relations with a range of new and emerging powers closer to home, including members of NAM like India and Indonesia.

Given that the new global powers are closer to home, the second way in which Sri Lanka is beginning to adapt non-alignment is by actively engaging with the regional powers – as compared to its relatively passive relations with the great powers during the Cold War and immediate post-Cold War era. That active engagement is apparent in some of the economic aspects mentioned earlier, such as prioritising bilateral trade agreements with India and China, and seeking a diversity of partners to develop Sri Lanka’s infrastructure.

This active engagement with regional powers is also apparent in other ways. It has been observed that between 2009 and 2017, almost [400 military vessels](#)²⁰ visited the Colombo port, the top three countries making port visits being India, Japan and China (in that order). It is further apparent in the vigour with which Sri Lanka is engaging with multiple regional frameworks, including with IORA, the Belt & Road Initiative (BRI), and the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC). This factor leads to a discussion of the fourth emerging contour of Sri Lanka’s role in the region and beyond.

VI. Conclusion: The Urgency of Geoeconomic Understanding

There is no doubt that we are living in a time of political and social transformation in the global polity and political economy. It is far from certain, however, what form the new regional order might take. What is clear is that the tectonic plates of the regional order are moving, and that this movement will transform the terrain on which foreign policy is made. It is crucial that policymakers understand the nature of this shifting terrain, and their location within it, to produce coherent and sustainable policies. Effective and sustainable foreign policymaking in Sri Lanka will require an understanding and analysis of the geoeconomic forces that are buffeting the island state. The state's response to these powerful geoeconomic forces will shape the future of the Sri Lankan polity.

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