Testimony before the US-China Economic and Security Review Commission

'Crossroads of Competition: China in Southeast Asia and the Pacific Islands'

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Hearing Co-Chairs Commissioner Price, Commissioner Schriver, and distinguished members of the Commission:

I am grateful for this opportunity to provide statement for the Commission's consideration on this important topic of 'Crossroads of Competition: China in Southeast Asia and the Pacific Islands'. My statement will primarily focus on the implications of China's economic engagement with Southeast Asia as I know too little of the Pacific Islands to offer anything useful. In particular, I want to discuss three themes: wider economic architecture linking Southeast Asia to the rest of the world; foreign direct investment (FDI) flows; and the structural issues preventing higher quality growth in the region. After examining these three themes, I will conclude with brief recommendations for US Congressional action.

First and foremost, there are very few regions within the Global South that have grown as steadily as Southeast Asia since the late 1990s. Its size (about 680 million people), relatively young demography, and generally pro-business environment present major opportunities for transnational corporations (TNCs), regardless of country of origin. It should, therefore, not be surprising that firms like Huawei, BYD, and Lenovo are eyeing the region. The more important question is – how are TNCs from the US and other nations faring in this seemingly intensifying economic competition?

The good news? US firms have been leading the way in the region, notwithstanding some alarmist narratives oft paddled by the popular press. US businesses consistently outinvest their counterparts from China, Japan, and elsewhere, as will be shown later on. This is not to deny the growing influence of China Inc. – Chinese business groups have indeed expanded their market share. However, apart from the less-developed markets like Cambodia and Myanmar, they are far from being a dominant force. In key industries – semiconductor and automotive – long-established Western and Japanese firms still set the standard in the region. However, staying ahead requires more than just FDI. The US must strengthen industrial partnerships, invest in workforce development, and ensure Southeast Asia remains an integral part of the global supply chain. By doing so, the US and its allies can not only consolidate its economic heft, but also create a 'rising tide lifts all boats' effect for TNCs – regardless of nationality – to continue growing the economic pie.

Southeast Asia as a Market for All

China and virtually all other nations share key economic interests with the US in Southeast Asia, particularly in investment, trade, and infrastructure provision. In general, the TNCs from all these economies – including the US – want to maintain open markets, strengthen supply chains, and expand cooperation.

*: All statements of fact and expressions of opinion contained in this testimony are the sole responsibility of the author.

One of the clearest ways such interest has unfolded is in the various economic partnership agreements (EPAs) that have come to fruition over the last decades. For example, there is the Trans-Pacific Partnership (TPP), which supposedly promotes high standards in trade liberalization, intellectual property, labor rights, and environmental protections.[1] While some analysts believe that the TPP, by excluding China, is created to counterbalance China's growing economic influence, this is not a universally agreed upon position.[2] In either case, there were fears that the TPP would collapse after US withdrawal in 2017. Instead of abandoning the agreement, the remaining 11 countries – led by the Japanese government – renegotiated the pact. It has since been salvaged and in 2018 was renamed the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP).

Since then, several other nations have either officially joined the CPTPP (i.e. the UK) or submitted formal applications to join (e.g. China and Ukraine). Despite the absence of the US, the CPTPP is still regarded as a blueprint for rules-based economic governance. It also complements the other mega EPAs in the region, especially the Regional Comprehensive Economic Partnership (RCEP). The latter connects the ten Association of Southeast Asian Nations (ASEAN) member states to the '+5 partners' with which ASEAN has existing EPAs (Australia, China, Japan, Korea and New Zealand).

While Chinese firms have deepened their presence in Southeast Asia through these EPAs, they still face significant competitive disadvantages compared to long-established Western and Japanese TNCs. One notable example is the automotive sector, where Japanese brands – Toyota, Honda, and others – continue to dominate. In 2023, Japanese automakers accounted for approximately 68% of passenger car sales in Southeast Asia, a testament to consumer trust in their high-quality products, reliable after-sales service, and strong resale value.[3] These strengths have been developed over decades, during which period more established Western automotive brands fell behind in the region.

Could Chinese electric vehicle (EV) manufacturers, such as BYD, challenge Japan's dominance? Perhaps, but thus far their progress has been hampered by factors such as limited charging infrastructure, high import duties, and Southeast Asian loyalty toward Japanese automotive brands. Barring a significant market disruption, it will be difficult for the Chinese EV makers to dominate the market in the same way that the Japanese have.

Some Macrolevel Statistics

FDI is one of the most critical metrics for assessing economic influence in Southeast Asia. Figure 1 demonstrates that US firms have generally outinvested their contemporaries from the EU27, China, and Japan between 2012 and 2023. Although there was a sharp drop-off in 2018, US firms have rebounded strongly in the subsequent years. In 2023, US FDI even surpassed the combined investment of the EU27, China, and Japan. For Chinese FDI, it has definitely grown from a rather low base, but this pace of growth is modest, at least compared

[1] The 12 'original' TPP members include four Southeast Asian states.

[2] Mireya Solís, 'The Containment Fallacy: China and the TPP,' *Brookings*, 24 May 2013 https://www.brookings.edu/articles/the-containment-fallacy-china-and-the-tpp/ (accessed 10 March 2025).

[3] Japan Times, 'China's EV Makers are Facing a Reality Check in Southeast Asia,' *Japan Times*, 4 March 2025 https://www.japantimes.co.jp/business/2025/03/04/tech/china-ev-makers-southeast-asia/ (accessed 10 March 2025).

to those of EU27, Japan, and US. In virtually every year since 2012, Chinese FDI also ranks the lowest in Southeast Asia.

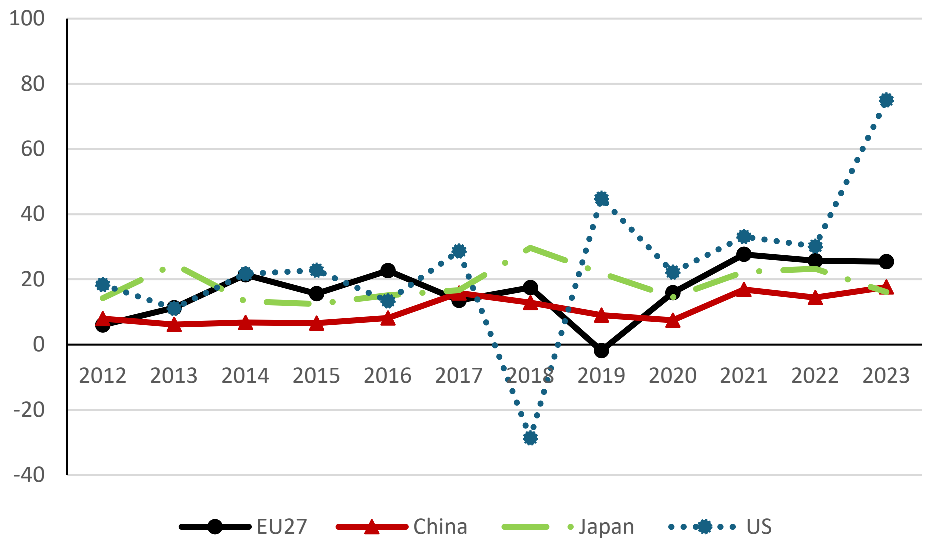

Figure 1: Flows of Inward Foreign Direct Investment into Southeast Asia, 2012-2023 (in Billion USD)

Source: ASEANstats.

What is more relevant here is to analyze the countries where Chinese FDI has exerted the most impact, and the broader relevance to Southeast Asia's economic architecture. To this end, Figures 2 and 3 show that Chinese FDI is a market leader only in two less developed economies of Southeast Asia: Cambodia and Myanmar.[4] These nations, which have relatively underdeveloped economies and only joined the ASEAN bloc in the late 1990s, present opportunities that Chinese firms have been quick to exploit. In these markets, where less-than-mature institutional framework and business climate may deter more established TNCs, Chinese firms have found niches, particularly in labor-intensive industries like real estate and petty trading. However, this expansion has not been without controversy, as some Chinese projects have been linked to thinly-regulated sectors such as gambling, exacerbating governance challenges in these economies.[5]

[4] My prior research, also utilizing data from ASEANstats, notes broad similarities in Cambodia, Myanmar, and Laos. However, there appears to be some statistical reclassification when I attempted to retrieve fresh FDI data on Laos recently. The data inconsistency means that it is best to exclude Laos from the comparison here. See Chengwei Xu and Guanie Lim, 'Chinese Investment in Southeast Asia: (How) Does It Matter?', *Eurasian Geography and Economics*, (2024), pp. 1-18.

[5] Charlie Campbell, 'Is China Really Powerless to Stop the 'Scamdemic'? The Truth Is More Complex,' *Time*, 21 January 2025 https://time.com/7208652/china-pig-butchering-scamdemic-crack-down/ (accessed 14 March 2025).

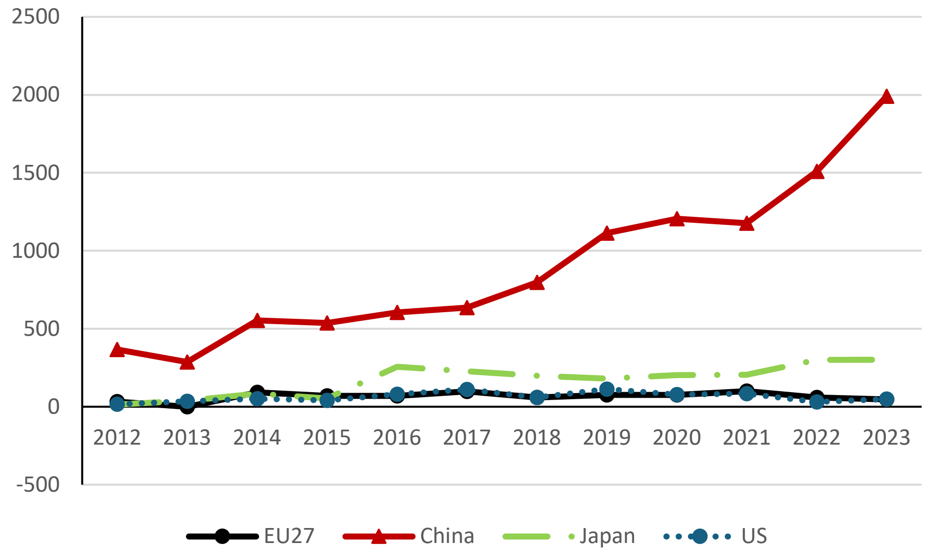

Figure 2: Flows of Inward Foreign Direct Investment into Cambodia, 2012-2023 (in Million USD)

Source: ASEANstats.

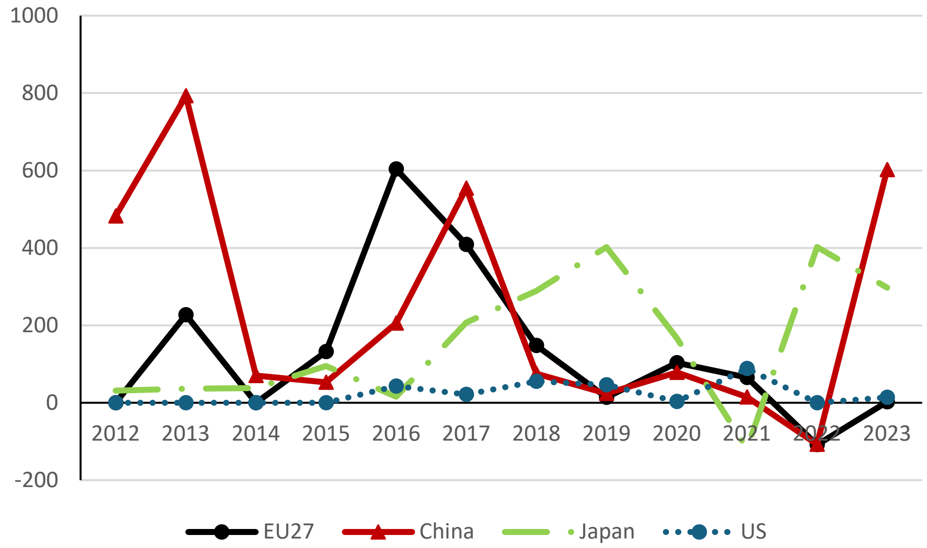

Figure 3: Flows of Inward Foreign Direct Investment into Myanmar, 2012-2023 (in Million USD)

Source: ASEANstats.

Similarly, it is important to stress that the larger and more mature Southeast Asian economies (i.e. Indonesia, Malaysia, Philippines, Singapore, and Thailand) continue to attract substantial capital from EU27, Japan, and the US, notwithstanding China's increasing FDI presence (see Figure 4). Over the period analyzed, there is no clear sign that Chinese FDI has definitively usurped the more 'traditional' investors. The dominance of these traditional investors underscores the resilience of their corporate networks, which extend beyond automotive manufacturing to high-tech industries such as semiconductors, software, and consumer electronics. Iconic brands like Apple, Microsoft, and Coca-Cola enjoy deep-rooted consumer loyalty, reinforcing US economic influence in the region.

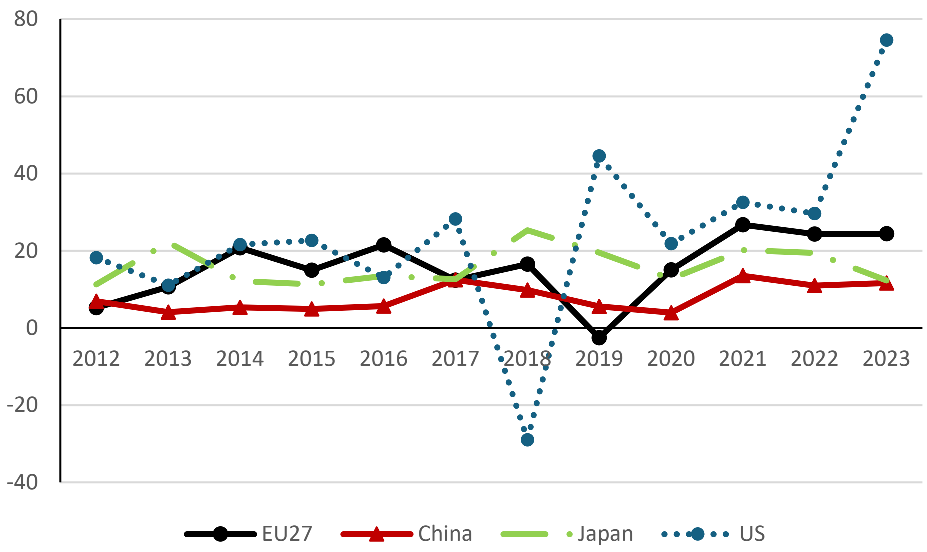

Figure 4: Flows of Inward Foreign Direct Investment into Indonesia, Malaysia, Philippines, Singapore, and Thailand, 2012-2023 (in Billion USD)

Source: ASEANstats.

Structural Issues of Southeast Asian Industrialization

Southeast Asian states have largely adopted a pro-trade and -FDI development model. This approach is especially noticeable in technology- and capital-intensive industries such as precision engineering, semiconductor manufacturing, and petrochemicals. This model has fostered rapid economic integration, but it has also entrenched a reliance on turnkey contractors and modular manufacturing, often at the expense of local capability-building.[6] Consequently, domestic firms in the region often function as junior partners, rather than independent industry leaders capable of driving technological innovation.

With the partial exception of Singapore, virtually none of the Southeast Asian countries have groomed firms with sufficient internal capabilities to compete internationally in high-value segments of manufacturing. If anything, the openness to FDI has indirectly trapped these nations in a 'technology-less' development trajectory, where domestic firms participate in some 'superficial' activities in seemingly high-technology industries.[7] As Western/Japanese TNCs retain proprietary knowledge on critical inputs, factory design, and manufacturing workflow, these Southeast Asian firms are forced to rely on the former in a virtually perpetual basis.

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[6] Kenichi Ohno, *The Middle Income Trap: Implications for Industrialization Strategies in East Asia and Africa* (Tokyo: GRIPS Development Forum, 2009).

[7] Kunio Yoshihara, *The Rise of Ersatz Capitalism in South-East Asia* (New York: Oxford University Press, 1988).

Notably, Chinese firms are increasingly replicating the same business models long employed by Western and Japanese TNCs. While Chinese TNCs may not yet possess the same level of technological sophistication as their Western and Japanese counterparts, their operational strategy in Southeast Asia follows a familiar pattern: maintaining control over key knowledge and processes while limiting technology spillovers to local firms. A case in point is the Alliance Steel integrated steel mill in Malaysia. It is a USD1.5 billion joint venture involving Guangxi Beibu Group and Guangxi Shenglong Metallurgical. It is also one of the biggest projects in Malaysia ever since the Belt and Road Initiative (BRI) was announced in 2013. Operational since 2018, the facility produces high-speed wire rods, bar rods, and H-beam steel – long steel products primarily used in construction. However, studies show that the facility has generated only minimal spillover, with expertise largely retained within the Chinese firms and their affiliates.[8] Furthermore, Malaysian steel players have complained that Alliance Steel is dumping certain specifications of steel in the local market, leading to financial losses.[9]

At first glance, it may appear that Southeast Asian countries have been effective in attracting Chinese investment, particularly as TNCs seek to diversify beyond China. However, merely offering pro-business policies is not enough to ensure long-term industrial competitiveness. Without deliberate efforts to deepen global-local linkages and facilitate technological upgrading, Southeast Asian firms risk being locked into low-value added activities. The real challenge lies in positioning domestic companies strategically within global value chains – enabling them to transition from low-margin activities to higher-value functions such as product design and branding. This challenge has become even more urgent as rising business costs in the region erode the competitiveness of traditional low-cost production models.

Implications and Recommendations

Virtually all Chinese investors, much like their Western and Japanese counterparts, operate in Southeast Asia with a clear business rationale: maximizing efficiency while retaining control over critical know-how. By the same token, the dynamics of FDI-driven growth in the region are not fundamentally different today than in previous decades. Consequently, the priority should be fostering deeper and more generous forms of cooperation with host economies, helping their firms hone human capital and institutional capacity. To achieve this, US policymakers must ensure that human capital development is directly tied to the long-term upgrading imperative of US firms and local stakeholders. US companies are well-positioned to lead this effort, provided there is sufficient policy encouragement. After all, the know-how of some of the world's most technology-intensive industries – ranging from aerospace to semiconductors – remain firmly in US hands. Furthermore, US soft power in Southeast Asia remains unmatched, offering a strategic advantage over other global players.

Japan offers a compelling model in this regard. In late 2023, Tokyo launched the ASEAN-Japan Co-Creation Initiative for the Next Generation Automotive Industry, backed by a USD1 billion fund to build a stronger EV production and sales ecosystem in the region.[10] This joint strategy

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[8] Alvin Camba, Guanie Lim, and Kevin Gallagher, 'Leading Sector and Dual Economy: How Indonesia and Malaysia Mobilised Chinese Capital in Mineral Processing', *Third World Quarterly* 43(10), (2022), pp. 2375-2395.

[9] Jose Barrock and Liew Jia Teng, 'Long Steel Players Urge Close Scrutiny of Alliance Steel,' *The Edge*, 16 January 2024 https://theedgemalaysia.com/node/696725 (accessed 14 March 2025).

[10] Jayanty Nada Shofa, 'Japan to Provide $1b for ASEAN's Regional EV Ecosystem,' *Jakarta Globe*, 18 December 2023 https://jakartaglobe.id/news/japan-to-provide-1b-for-aseans-regional-ev-ecosystem (accessed 14 March 2025).

encompasses workforce training, decarbonized manufacturing, mineral resource procurement, and investments in emerging fields such as biofuels.[11] The broader implication is clear: a more dynamic Southeast Asian automotive industry will also push Chinese EV players to raise their standards. This, in turn, boosts the entire economic pie – creating a win-win scenario for all stakeholders.

Biodata

Guanie Lim is Associate Professor at the National Graduate Institute for Policy Studies (GRIPS), Japan. His main research interests are comparative political economy, value chain analysis, and the Belt and Road Initiative in Southeast Asia. He is also interested in broader development issues within Asia, especially those of China, Vietnam, and Malaysia. He has published his findings in key academic journals such as *World Development*, *Third World Quarterly*, and *Journal of Contemporary China*. His latest monograph – *The Political Economy of Growth in Vietnam: Between States and Markets* (published by Routledge) – details the catching-up experience of Vietnam since its 1986 *doi moi* (renovation) reforms. He received a PhD from the National University of Singapore, an MSc from Nanyang Technological University, Singapore, and a BEng (Hons) from the University of Bath, United Kingdom.

[11] Reuters, 'Japan and ASEAN Plan Joint Strategy on Auto Production, Nikkei Reports,' *Reuters*, 20 May 2024 https://www.reuters.com/business/autos-transportation/japan-asean-plan-joint-strategy-auto-production-nikkei-reports-2024-05-19/#:~:text=May%2020%20(Reuters)%20%2D%20Japan,Nikkei%20newspaper%20reported%20on%20Monday (accessed 14 March 2025).