

**THE NEW REGIONAL CONTEXT OF POST COLD WAR SOUTH ASIA AND ITS
IMPLICATION FOR BHUTAN**

By

Karma Tshering Wangchuk

THESIS

Submitted to

KDI School of Public Policy and Management

in partial fulfillment of the requirements

for the degree of

MASTER OF PUBLIC POLICY

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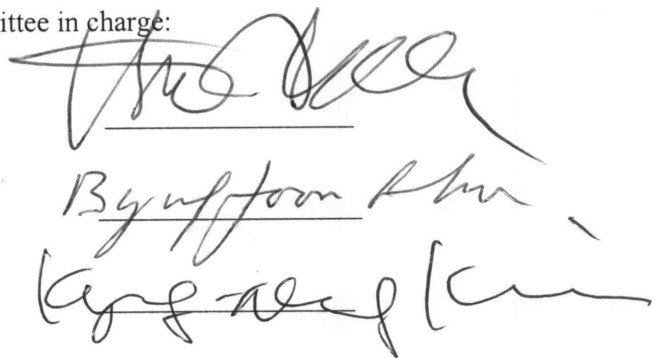
MASTER OF PUBLIC POLICY

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The image shows three handwritten signatures in black ink. The first signature is the most prominent and appears to be 'Hun Joo Park'. Below it are two other signatures, one of which appears to be 'Byung Joon Ahn' and the other 'Kyong Dong Kim'. Each signature is written over a horizontal line.

Approval as of October , 2009

**Dedicated to loving memory of my late parents – Chhoni Dorji and Dechen Pelzom,
and the gratitude which I can never repay in many cycles of lives and who are
missed dearly every single day of my life.**

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ABSTRACT

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South Asian countries experienced epoch making experience subsequent to the end of Cold War and emergence of China and India as economic giants on the Asian subcontinent. Given the quick rise of both countries and the impact of their rise, it would be beneficial for Asian countries to engage into regional cooperation. By doing so, they may take advantage of China's economic rise and at the same time avoid possible conflicts with China, which may result in disastrous consequences for the whole region and smaller countries. On the other hand, a policy of isolation or containment only worsens the situation and unnecessarily provokes tough reaction from China. But within that context, it is important that regional countries adjust their policies in order to benefit from the new opportunities and minimize challenges. The significance is the pursuance of a regional South Asian nations' foreign policy based on diversification and multilateralism with a view to foster further understanding and cooperation in the region.

TABLE OF CONTENTS

INTRODUCTION	1
Part I : THEORICTICAL PERSPECTIVES OF INTERNATIONAL REALTIONS	3
I. Realism	3
II. Neoliberalism	6
III. Constructivism	7
IV. Towards a comprehensive view on South Asia	11
Chapter II .THE NEW STRUCTURE OF INTERNATIONAL POLICTICS IN POST COLD WAR SOUTH ASIA	13
I. South Asia during Cold War	13
Politics	13
Economic relations	16
II. The new features of international relations in East Asia and their implications	18
1. Increased economic interdependence	18
2. <i>The co-existence of cooperation and conflict</i>	19
3. Democratization of international relations in South Asia	22
4. The rise of China as a regional power in Asia	23
5. The India in the new regional context	28

III. South Asian countries in the regional context	31
CHAPTER III : BHUTAN IN THE REGIONAL CONTEXT	33
1. Overview of economic reform and opening up	33
2. Foreign Direct Investment Attraction	35
3. Trade Development	36
4. Challenges Ahead	37
Bhutan's Foreign Policy –Diversification and Multilateralism	39
I .Overview of Bhutan's Foreign Policy since 1960s	41
II .Relations with Regional countries	42
1. Relations with India	42
2. Relations with China	43
3. Relations with Nepal	50
4. Relations with Bangladesh	52
5. Relations with other regional SAARC countries	54
CONCLUSION: TOWARDS GREATER COOPERATION IN SOUTH ASIA IN THE 21 ST	
CENTURY	55
REFERENCES cited	59

ABBREVIATION

Association of South East Asian Nations	ASEAN
Bangladesh-Bhutan-India-Nepal Quadrilateral Growth Initiative	BBIN-QGI
Bengal –India-Myanmar-Sri Lanka-Thailand Economic Cooperation	BIMST-EC
Bengal Initiative for Multi Sectoral Technical and Economic Cooperation	BIMSTEC
Bhutan Chamber of Commerce and Industry	BCCI
Central Treaty Organization	CENTO
Chinese Communist Party	CCP
China’s People’s Liberation Army	CPLA
Federation of Nepalese Chamber of Commerce and Industry	FNCCI
Free Trade Agreement	FTA
Foreign Direct Investment	FDI
Gross Domestic Product	GDP
Gross National Happiness	GNH
International Relations	IR
Joint Working Group	JWG

Least Developed Countries	LDC
Most Favored Nation	MFN
Non Proliferation Treaty	NPT
Organization for Security Cooperation in Europe	OSEC
People Liberation Army	PLA
People's Republic of China	PRC
South Asian Association of Regional Cooperation	SAARC
South Asian Free Trade Area	SAFTA
South Asia Regional Cooperation	SARC
Southeast Asian Treaty Organization	SEATO
Tamil United Liberation Front	TULF
Technical Barriers to Trade	TBT
Trade Related Intellectual Property rights	TRIPs
World Trade Organization	WTO

INTRODUCTION

The ending of the Cold War has brought about mixed results in interstate relations within the South Asian region. On the one hand, economic cooperation has progressed, with the establishment of regional cooperation mechanism like the South Asian Association of Regional Cooperation (SAARC) - India and other regional neighbours, thawing of the Indo-China Relations and some sort of development and reopening of one of old Silk Routes through Nathula Pass, Sikkim, an Indian state to China. Regional countries are also now discussing the importance of a South Asian Free Trade Area (SAFTA) and more and recently the establishment of the Bengal Initiative for Multilateral Sectoral Technical and Economic Cooperation (BIMSTEC).

On other hand, in contrast with economic cooperation, political cooperation amongst regional countries has been fraught with numerous challenges. Unlike Europe where a formal security mechanism – the Organization for Security Cooperation in Europe (OSCE) – exists, South Asia states are yet to institutionalize a security cooperation pact. The SAARC, which has no binding mandate on its members, therefore remains the only forum in South Asia for exchange of views on security issues.

What are the major changes in international relations in South Asian countries in the post–Cold War era that fosters those above mentioned developments? What would be the role of regional countries to play in the new context and how does that would affect regional economics and politics? What will be the policies to ensure regional peace and cooperation? These are the major questions this thesis deals with. The most important argument is that the new regional context of

South Asia, characterized by augmented independence, ambiguity and the democratization of international relations, requires regional countries to adjust their policies towards integrations and multilateralism in order to foster regional cooperation and cope with new challenges. The pursuance of unilateralism or bandwagoning is thus against the will of the majority of nations in South Asia risking undermining the scope and environment for economic development and cooperation. The thesis presents the case of Bhutan to show how a country can foster economic growth and regional cooperation on the basis of a multilateral approach to economic reform and regional integration.

With that objective, this thesis is structured as follows:

Chapter I discusses the major theoretical perspective prevailing among studies on international politics in South Asia. These include realism, neoliberalism, and almost recently constructivism. As the complexity of South Asian politics makes it difficult to look at the region through just one perspective, there needs to be a mixture of paradigms in order to understand regional developments.

Chapter II analyzes briefly the foreign policy of Bhutan and the emergence of China and its rising impact in the regional economies and other SAARC countries, which constitute the new regional context of South Asia. It starts by examining the situation during the Cold War then proceed to discuss the broad trends of international relations in the region today, which can be generalized as a mixture of cooperation and conflict, increased interdependence, and democratization of interstate relations. In this new context, it is important that regional countries adjust their policy and regional strategy.

Chapter III discusses the conclusions and implications of the new regional context in South Asia for Bhutan since the start of economic development and opening of country in 1960s. It explains how Bhutan has adjusted its development strategy in order to adapt with the new regional trends, of which the most important are the adoption of a regional integration and foreign policy based on multilateralism and diversification.

Part I : THEORITICAL PERSPECTIVES OF INTERNATIONAL REALTIONS

I. Realism

Realism is the mainstream theory and subject of international relations after the end of the Second World War. Despite having significant differences, classical realist and neorealist scholars from Hans Morgenthau to Kenneth Waltz and Henry Kissinger share basic features in their theories and assumption which constitute the foundation of realism.

Foremost is the lack of overarching authority within the system of international relations while applying the theory of anarchy and its paramount existence. Instead of the system of domestic politics, which is governed by the state bureaucracy, there is no legitimacy for protection of state's interest and no power beyond states. International politics for realists, therefore, is very conflictual in nature , a constant struggle for power in which countries rely on their own capabilities for survival. A state of anarchy is paramount feature forcing for self help.¹ Under this anarchy, international cooperation is particularly difficult to achieve. Therefore, they avoid

¹ Kenneth Waltz, *The Anarchic Structure of World Politics*, in Robert Art and Robert Jervis, ed., *International Politics*, Longman 1999, p.64

each other if one gains more from alliance and cooperation through relationship. Nations are also constantly nagged by the idea of getting cheated by other nations.²

Second, most realists also favour the idea of balance of power in their theory. In their analysis, states are seen as goaded by the pursuit of their national interests and states are conditioned by the prevailing theory on balance of power. For example, in 1970s, Henry Kissinger was the architect of the détente between China in Asia and USA with the aim of balancing against Soviet power.³

Third, realist writers generally tend to separate domestic and international politics. In the neorealist theory of Waltz, states' actions are governed by the material structural and their position in the international system further calculates states' strategies and interests. State's particular location in the anarchical world enables Neorealists to forecast the likelihood of state's action. Thus, realists adopt the assumption that state interests are given, a priori and exogenously, which can be defined as the pursuit of power.

According to McDougall (1997), from the viewpoint of realism a certain power-balancing logic at work is seen in the Asia Pacific region like China on the one side and USA, supported by Japan on the other side. Starting in the late 1950s, there was also a hostile relationship between the two countries of China and the USSR. In the 1970s, the situation changed once again when

² Stephen Krasner, *Structural causes and regime consequences: regimes as intervening variables*, in Stephen Krasner, ed., *International Regimes* (Ithaca: Cornell University Press, 1983, p.79)

³ For reading of Kissinger's thoughts on the balance of power principle, see Henry Kissinger, *Diplomacy* (New York: Simon and Schuster, 1994)

China and the United States reached a rapprochement.⁴ At the current stage, there is the possibility that weaker states such as Russia and China will co-operate to balance against the US.

Realist scholars also point out adjustments in the policy of South Asian countries to wider changes in the international system and the outer challenges facing countries within a region.⁵

The recent developmental changes and increasing openness of SAARC economies are supportive of stand for creating more opportunity. The establishment of the SAARC in 1985 was an attempt to bring about that change. Just like the Treaty of Rome was preceded by strong opinions for solidarity in the region given the emergence of two superpowers of the US and the Soviet in Post World War II.⁶ The same initial conditions prevail at the time of founding the ASEAN in East Asia too like in South Asia.

In the analysis following the history of ASEAN provides several clear examples of the importance of external development. The creation of the SAARC Regional Forum was in response of the perceived risks in the emergence of a regional power vacuum following the end of the Cold War era. In economic realm, the commitment in early 1990s was the establishment of a South Asian Free Trade Area (SAFTA) prompted by fears that foreign investment would be lost to China. Similarly, the demise of Cold War leading to the relative power changes of the US

⁴ Derek McDougall, *The International Politics of the New Asia-Pacific*, Lynnee Publishers, 1997, p.10

⁵ Hurrell, A, *Regionalism in theoretical perspective*, in Fawcett and Hurrell, ed., *Regionalism in the World Politics : Regional Organization and International Order*, Oxford, Oxford University Press, pp.37-73

⁶ Aparna Sawhney and Rajiv Kumar, *Rejuvenating SAARC: The Strategic Payoffs for India*, Published by The Berkeley Electronics Press, 2008

have created a new context in South Asia, which significantly affect the foreign policy choice of regional states.⁷

II. Neoliberalism

Neoliberalist theory has surfaced in the late 1970s with the works of founding authors like Joseph Nye and Robert O. Keohane who views Neoliberalism or the idea of neoliberal-institutionalism as an alternative choice to realism and neorealism.⁸ As a matter of fact, Neoliberalism and neorealism share basic features and assumptions.⁹ The main difference is that Neoliberalism stresses on the economic dimension of power. Neorealism emphasizes on conflictual nature of international politics and is cynical of peaceful change. But neoliberalist scholars also argue about the possibility of cooperation in anarchic position of international regimes which authorize governments to enter into agreements that would benefit each other.¹⁰ The main problem with prevailing states from cooperation with one another is a fear of deceitful and defection. International regimes can provide the solutions as they help to create a sense of legal liability, reduce transaction costs and provide transparency.¹¹ Neoliberalist authors also believe that as information technology and modern communications make the world smaller, states become more economically interdependent leading to cooperation and to their mutual benefit.

⁷ John Ravenhall, *The Growth of intergovernmental collaboration in the Asia-Pacific Region*, in Anthony McGrew and Christopher Brook, ed., *Asia-Pacific in the New World Order*, Routledge, 1998, pp.254-258

⁸ Robert O.Keohane and Joseph Nye, *Power and Independence*, Glenview, Ill ;Scott, Foresman and Company , 1989

⁹ The three assumptions shared by neorealism and Neoliberalism are : 1-the international system is anarchic; 2 – states are the main actors of international politics and 3- states are rational

¹⁰ See Robert O. Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy*, Princeton University Press, 1984.

¹¹ Ibid

Furthermore, the establishment of multilateral institutions in the region such as SAARC and BIMSTEC (Bengal Initiative for Multi Sectoral Technical and Economic Cooperation) are positive developments that will contribute towards peace and stability. There is the growing democratization of South Asian countries like democratization of Bhutan in March 2008¹² and other neighbouring nations like Nepal.

Compared to realism, neoliberalism puts importance on the economic dimension and interdependence as key to understanding the dynamics of international politics. Indeed, Keohane (1984) uses the market failure approach in elucidating the function of regimes. However, this approach ignores other functions of international regimes such as guaranteeing or at least enhancing security for its members. For many states, the *raison d'être* for participating in international regimes is political and not necessarily economical. This is particularly true in the case of small states as they hope that by joining in regimes led by powerful nation states, their security is more ensured under their protection. This is to a large extent true in case of Bhutan shedding its self imposed isolation and joining comity of nations particularly with India.

Although limited in scope, neoliberalism must be look into as a useful for studying South Asian politics in the context of economic globalization in post Cold War scenario.

III. Constructivism

The theory of neorealism and its subsequent failure of international relations although at one time considered as the important theory in forecasting the Cold War's end and bi-polar order rejuvenated interests in searching for alternative paradigms. Within that context, constructivism has emerged as the new focus of IR theory into the 21st century.

¹² Kuensel, Bhutan Newspaper , March 2008

According to Alexander Wendt, the leading constructivist researcher, constructivism is one of the theories in international relations making the following claims: (1) nation-states are the principal units of analysis in international politics, (2) the key structures in the states system are intersubjectives and not that of materials in constructive theory and (3) national identities and national interests are important part of constructive structures and not an external component of the system as rendered by human nature or domestic politics.¹³

As compared with neorealist and neoliberalists, the theory of constructivist authors has some basic differences. First, they argue that despite the anarchic feature of international system, it means nothing by itself. The varieties of social structures are what that matters under anarchy.¹⁴

Second, while neoliberalism and neorealism take state interests as given, constructivism holds that states define their national interests and in the process define other social conditions as they are the key players.¹⁵ States' identities and interests are thus socially constructed. The social identities of actors defined characteristics of state as well as national interest. Such interests and identities are in continuous fluctuation and are termed as intersubjectives systemic structures, and Wendt also terms these as "shared understandings, expectations and social knowledge".¹⁶ Therefore, to understand the behavior of state is to understand the evolving social context of the system.¹⁷

¹³ Alexander Wendt, *Collective identity formation and the international state*, American Political Science Review 88, June 1994.

¹⁴ Alexander Wendt, *Anarchy is what states make of it: the social construction of power politics*, International Organization 46, No.2, pp 391-425.

¹⁵ Alexander Wendt, *Constructing International Politics*, International Security 20, No. 1. 1995, p. 77.

¹⁶ James E. Dougherty and Robert L. Pfaltzgraff, Jr., *Contending Theories of International Relations*, Longman 2001, p, 169

¹⁷ Shaun Narine, *Economics and Security in the Asia Pacific: A constructivist Analysis*, International Studies Association, March 2000.

Third, constructivist authors have clear focus on the transformative impact of norms. They also regulate nation's behavior as argued by neoliberalist arguments and define national interests that constitute state identities, and other collective identities development. Thus, institution and states are mutually-constituting entities. Institutions affect states' preference and their basic self-identities. The activities of the state are always changing affecting the institutions.¹⁸

Fourth, constructivism looks far ahead of the material forces' impact in developing international politics. Neorealism and liberal theories also believe that material forces like wealth and power derived from them help shape the interests of state. According to constructivist, these forces are important intersubjectives factors playing a decisive part in formulating foreign policy interactions.¹⁹

Narine (2000) opines that the emphasis put upon by the constructivism on the state's action in relation to norms and social structures of state has made it feasible to ask a completely different set of questions which the rationalists have taken on dissecting events after the Cold War ended in East Asia. This is true of South Asian countries. What are the characteristic features which define region's social strata and their relationships vis-à-vis neighbours? What are the criteria used by the states to distinguish their identities with those of their neighbours? What are the interests generated or ensued thereafter from these perception?

Narine also applies this constructivist approach to analyze the situation of Asia Pacific region's security environment focusing on the US and China's relationship. The US defines the economic partnership of China and is unsure about China's position as a threat to its security. As such, the

¹⁸ Shaun Narine, *Ibid*, p.7

¹⁹ Amitav Acharya, *Constructing a Security Community in Southeast Asia*, Routledge 2001, pp 3-4

US is not clear of its own interest and national identity in Asia Pacific region. Meanwhile, China possesses a “dual identity” dragging it in many conflicting directions. Both the US and the Chinese have different perception of security and economics in the regional situation. The differences have added to the ambiguity and uncertainty of the regional environment.

An important application of constructivism in the study of post Cold War East Asian politics is the work on security community. One of the leading scholars and authors, Amitav Acharya , defines its application on the concept of security community with regard to the Association of Southeast Asian Nations (ASEAN).²⁰ In his book “Constructing a security community in Southeast Asia”, Acharya defines and maintains that the expectation of people of sovereign states are peaceful changes from security communities. Two features of security community are important and well defined by him. The first one is about the absence of war and the second on the absence of significantly organized preparations for war (such as arms race) vis-à-vis any other members. He also differentiates security communities from other types of regional security systems, such as security regimes, collective security arrangement and alliance.²¹ According to Acharya, ASEAN regionalism is conceptualized as the process of building a security in which nation states develop a reliable blueprint of peaceful interaction, pursue shared interests and strive for a common regional identity.

²⁰ For Acharya’s work on Security Community, see *Constructing a Security Community in South east Asia*, Routledge 2001, *Association of Southeast Asian Nations: Security Community or Defence Community?*, *Pacific Affairs* Vol, 64, No. 2, 1991, *A Regional Security Community in south East Asia?*. *Journal of Strategic Studies*, Vol.18, No,3, Sept 1995.

²¹ Amitav Acharya, *Constructing a security community in Southeast Asia*, Routledge, 2001

IV. Towards a comprehensive view on South Asia

Given the complexity of international relations in South Asia, it would be difficult to use just one approach in examining the regional trends. Each of the above theories gives important vista to look at South Asia on international relation post-cold War era. Realism and neoliberalism can be useful in understanding the policy of regional states, especially the US whose policies are a mixture of realist and liberalist doctrines. However, when used alone, they could be misleading as realism stresses the inevitability of conflicts while neoliberalism overoptimistically emphasizes cooperation. Constructivism is important to the study of security community, which can be critical to maintaining peace and security in South Asia. For this reason, in examining the new regional context of South Asia after Cold War and its implications for regional countries, this paper tries to follow a comprehensive approach by combining these perspectives. Moreover, given the distinguished characteristics of South Asia, the following factors receive special attention.

First is the new role played by the regional countries. Studies of international politics in South Asia tend to focus on the role of major powers, which have had a dominant influence in South and East Asian politics.²² At the height of Cold War, the tripartite nations of USA, USSR and China have dominated regional affairs through their alliances and sphere of influence. Now with the USSR no longer in existence, China becomes a new focus of regional politics and is viewed as a potential hegemon.

Second is the focus on the distinctive socio –political context of East Asian states. McDougall (1997, pp.9-13) has termed this as the culturalistic approach. According to him, the culturalistic

²² McDougall (1997) assumes that regional powers such as the US, China and Japan play a decisive role to international relations in East Asia.

approach has drawn attention to the way whereby factors endemic to states exerting influence on their behavior and bringing about some general character of international politics. Not like realism and liberalism which share the common belief that the general processes underlying international politics are the same irrespective of the part of the globe or world in which one is examining. The culturalistic perception, on the contrary, argues that there are variations in the general processes because the cultural influences at work in different regions often vary. By applying this approach, it is able to understand why countries behave in certain manners and then using other perspective like realism and neoliberalism, one can get rich insights into regional development. This way of looking at East Asia is similar to the strategic culture approach used by J.N Mak in “The Asia –Pacific security order”.²³

This culturalistic perspective is different from the cultural approach used by Samuel Huntington in “The Clash of Civilization and the Remaking of the World Order”. He argues that “the clash of civilization” gives the dynamics underlying of international politics after the Cold War.²⁴ In his view, Asia is a place of conflicting ideology based on “Confucian”, “Japanese”, “Islamic” or ideas of western hemisphere . In fact, there can be very significant ideology differences like the North and South Korea has demonstrated. It would be oversimplified to attribute the political difference of Japan and China and Japan or between USA and Japan solely to underlying civilizational differences.

²³ According to Mak, different approach to war, war-making and the conduct if war can be linked to culture and the mind –sets which national culture and history engender. Based on this approach, he explains why Northeast Asian states adopt a neorealist behavior while ASEAN members behave in a more neoliberalist –institutionalist manner. (see J.N Mak, *Ibid*) . This approach is basically similar to the culturalistic one used by McDougall.

²⁴ Samuel Huntington, *The Clash of Civilization and the Remaking of World Order*, New York: Simon and Schuster, 1999.

As such, much focus will be on the Rise of China and its impact on Indo- Bhutan Relations in South Asia. On prima facie judgment, there seem to suggest that South Asia is a region of peace and development without instability and unrest. However, the fact is that South Asian countries have yet to reach the level of cooperation matching that of western world or that of Asian miracle countries where their economies are thriving and growing always. One reason has been unsettled disputes among regional countries of China, India, Pakistan and ethnic problems in Sri Lanka. Moreover, there still exist potential conflicts of which the most serious is concerned between two nuclearised countries like India and Pakistan.

The first type of uncertainties concerns the policy of regional powers. Is China, with its rising economic and political power, seeking hegemony? If so, what should be the policy choice of regional countries? How will India react to it or act for the regional balance of power as it is also growing economic power in South Asia. China has always viewed India as a country trying to undermine its rule in the region (p. 89)²⁵. What will, therefore, be the future in South Asia with these two upcoming countries? These are crucial issues that can have decisive impact on the prospects of peace and security in South Asia.

Chapter II .THE NEW SRTRUCTURE OF INTERNATIONA POLICTICS IN POST COLD WAR SOUTH ASIA

I. South Asia during Cold War

Politics

²⁵ Alastair Iain Johnson and Robert S Ross(eds), *New Directions in the Study of China's Foreign Policy*, Standard University Press, 2006 – *China's Decision for War with India in 1962* by John W Garver, p. 86-125

The international relations during the Cold War in South Asia were confrontational mainly due to the rivalry between two giants of the world. When the World War II ended, a long drawn out rivalry and power struggle remain between two super powers , led by US and the other one led by the Soviet Union. But unlike in Europe and many other war zones, South Asia also became a strategic region for India and China where both nations tried to flex their muscles for increasing their areas of influence. This even led to famous 1962 war between them where India lost the war and substantial land areas in Arunachal Pradesh. Ultimately Tibet was annexed by China and the relations between India and China never remained the same like before the 1962 war.

For South Asian nations whether big, medium or small, the only choice remained was to bandwagon with one of the superpowers which resulted in the formations of alliances such as the Treaty of Peace, Friendship and Cooperation between India and Soviet Union in August 1971 for a clear mutual military cooperation which is a big departure from India's former stand on Non-alignment movement.²⁶ Another significant development was the increasing Sino-American allies and prelude to the Bangladesh war of liberation.

The diplomatic relations between Soviet Union and India after its independence from British was ambivalent as India was very active in the Commonwealth of Nations while remaining committed to Non Alignment. It was during the American President Dwight D. Eisenhower's announcement and decision to supply sophisticated arms to Pakistan that alarmed India in 1954. Subsequently Pakistan also joined the two organizations, namely, Southeast Asian Treaty Organization (SEATO) and Central Treaty Organization (CENTO). Another contributing factor was also because of Pakistan's shared border with Afghanistan and through it with the Soviet

²⁶ Wikipedia

Union which provided Moscow with the good reason to find an ally in India. Besides, India's leadership in Non-aligned Movement would bolster its policy in the Third world. Therefore, India and Soviet Union followed policies perceived out of common security threat of American interests in Pakistan. The two nations exchanged military attaches but investment of military aid to India started only after the deterioration of Sino-Indian and Sino-Soviet relations. After the Indo-China war in 1962, the Sino –Pakistan relations was added impetus for the growing cooperation between India and the USSR.

It is also said that US's increasing military power and influence in South Asia has a number of benefits for Chinese national interests in South Asia. It has reduced the Chinese resource drain by supporting economy of Pakistani government while successful in toppling the terrorist protecting government of Taliban regime in Afghanistan and promoting Pakistani policies away from extremists who threatened Chinese interests and stability in Central and South Asia. Expanding US influence in both Pakistan and India has also aided in keeping peace in the subcontinent and averted nuclear war despite tension over the Kashmir. China also viewed the USA influence in the region with so much suspicion. For many years, China tried to expand its influence throughout Chinese periphery and weaken the USA influence bringing about multipolar world.²⁷ Despite so much ideological differences, China sometimes saw common ground with India which resisted USA dominance. China saw US influence and power shift in the overall strategic balance in South Asia in favour of USA. It is apparent that USA's

²⁷ Robert G. Sutter (2005), *China's Rise in Asia – Promises and Perils*, Rowman & Littlefield Publishers, Inc, p. 231-246

dominance and presence in the subcontinent bolstered by closer strategic ties with both Pakistan and India would remain for some years to come.²⁸

Economic relations

Tensions between India and Pakistan strongly influenced the growing economic relations and cast dark shadows. Although the setting up of SAARC was not a new idea, it was a desirous attempt to reestablish the economic cooperation which was already operational even before India's freedom in August 1947 from the British on the subcontinent. The division of India into two nations by the British remained a struggle of political tension and mistrust in South Asia and thus a major hurdle for the economic progress. However, it is widely perceived that SAARC will become confidence building forum and economic union in South Asia.²⁹

Despite geographic proximity not much economic benefits could be reaped. Therefore, the main aim and objective was to work for the economic alliances and socio economic development among the member countries in South Asia. The following is the chronological events of the efforts for the economic regionalization in South Asia:

1949 – Economic cooperation between India and Pakistan came under strain

1983 – South Asia Regional Cooperation (SARC) Declaration Adopted

1985 – South Asian Association for Regional Cooperation (SAARC) established

1987 - SAARC Secretariat established

²⁸ Ibid –Robert G. Sutter

²⁹ Saleem M. Khan, *Journal of Asian Economics* 10 (1999), p. 489-495

1995- Operationalization of SAARC Preferential Trading Agreement (SAPTA)

2001-Setting of target date for realization of a treaty regime on South Asian Free Trade Area (SAFTA)

The rationality for supporting economic union was in keeping with the changing scenario of the world global economy after the Second World War. This has further help to formulate a doctrine on strategy for formation of economic union for both developing countries as well as industrialized nations. Economic union and zoning as seen by many development economists was a formula for solution for larger international and economic problems of our time.³⁰

Unlike in South East Asian nations where billions of dollars were injected into the economies during the height of Cold War thus bringing out ultimate Asian miracle economies, it was not the case in South Asia. The most important contributing factor in the economic success of these “miracle economies ” was special international relations generated by the Cold War.³¹

To sum up, regionalism was immature in South Asia throughout the Cold War period. There was no multilateral economic or security mechanism that helped bring regional countries together. Dominated by the Cold War structure and the Sino-Indo war, Bangladesh Liberation war and overall international relations in South Asia were largely confrontational and uncooperative.

³⁰ Ibid Saleem

³¹ See Satya J. Gabriel, The end of the Cold War and the crisis in East Asia, Excerpt from talk prepared for the Silk Road Conference, Xiamen, China, October 1997.

II. The new features of international relations in South Asia and their implications

Realist scholars believe that the bi-polar structure of the Cold War was more peaceful and stable in comparison with a multi-polar order that came into being after 1991.³² For South Asia, however, it does not mean that the situation is getting worse as regional countries enter the new era after Cold War period. The end of Cold War, while creating new challenges and potential conflicts, has promoted new opportunities of regional cooperation. Driven by new dynamics, South Asia is currently undergoing the transitional period to a new regional structure, some features of which have started to materialize as stated above in the economic relations.

1. Increased economic interdependence

During the period of Cold War, a great rivalry between the US and the USSR dominated South and South East Asia politics and prevented economic exchanges on a region-wide scale. However, together with reforms and opening up of China and India in the 1980s, end of Cold War has fostered economic interdependence in South Asia. As economic development becomes the main priority, regional countries have expanded trade and investment linkages to take advantages of complementarities and economies of scale. Furthermore, economic development requires a peaceful and stable regional environment, which in turn promotes and enhances the level of interdependence among Asian countries.

³² For an example see Kenneth Waltz, Emerging Structure of International Politics, International Security, Vol.18, No.2, (Fall 1993)

Since the 1950s, relationship between India and China has been of tension and confrontational one. However, the two nations have recently enjoyed marked improvement in bilateral relations leading to commercial interdependence and economic cooperation.³³

Combined with the on-going process of globalization and regionalization, this new trend of interdependence in South Asia has forced all regional countries to adopt open economic policy. Even least developed countries like Bhutan and Maldives now view the attraction of foreign investment and the expansion of foreign trade as key to their economic development. In other words, enhancing foreign economic relations and strengthening regional integration has become the choice of South Asian countries after the end of Cold War period. Bhutan sees this important objective in its foreign policy as to develop close friendship and cooperation with its neighbours for peace and economic stability. Therefore, Bhutan has taken up SAARC as a good platform to initiate the process of facilitating on realization of this aim and fulfillment of hope and aspiration of its citizens.³⁴

2. The co-existence of cooperation and conflict

A major trend of international politics in South Asia has been cooperation. After the end of Cold War, the regional countries have been forming and stressing the need for the economic development. Otherwise there is a danger of exposure of the countries to the vulnerabilities like the 1997 -98 Asian financial crises.

³³ Christopher J. Rusko and Karthika Sasikumar, *India and China: From Trade to Peace?*, Asian Perspective, Vol. 31, No. 4. 2007, p. 99-123

³⁴ Shashi Upadhyay, *Bhutan and SAARC*, Bhutan: Society and Polity edited by Ramakant and R.C. Misra (1996), South Asia Studies Centre, University of Rajasthan, Jaipur, p. 321-327

In an era of globalization, lack of cooperation among the regional countries is a zero sum game. The ideological differences no longer hold ground for cooperation. Therefore, SAARC forum and the formation of SAFTA is a strong reason for celebration and optimism.

The World Bank Report released in 2007 said South Asia remained the “least integrated” region in the world. Commercial trading between member countries make up less than 2% of their nations’ combined Gross Domestic Product (GDP) whereas in East Asia, it is 20%.

However, there is a promise of growth from this small base start. A free trade in the region came into effect in July 2006 although it is shamefully slow in growth. The bilateral free trade agreement signed between Sri Lanka and India in 1999 is growing fast. Besides the bilateral relationship between India and China is also growing which is more important from \$4.8 billion in 2002 to \$38 billion in 2007.

But that is still modest compared to China’s trade with South Korea which is worth four times more. However, that is heartening signal between two giant countries that went to war in 1962 and continue to claim a portion of each other’s country. These still haunt and rankle, and Chinese have reiterated its claims of India’s northeastern state of Arunachal Pradesh. Therefore, strategic thinkers are of the opinion that this could still drive a wedge in the relationship of two countries leading to conflict and war again.³⁵

³⁵ “An elephant, not a tiger,” *The Economist*, December 13th -19th 2008.

Therefore, India is carefully writing its foreign policy to meet its economic need and mainly to get access to natural resources and overseas markets for its goods. This is main reason of the US's fear of rising China and helping India against it leading to nuclear détente.

The road to fast growth of the regional economies will be by following economic agenda of SAARC and SAFTA. SAFTA is considered as a supportive tool for promoting regional trade and investment among the SAARC members. Despite sluggish progress, recent push for trade reforms in the field of reduction in tariff rates and liberalization of investment are encouraging signals and development.

Besides regional programs have earned credibility among South Asian leaders. An efficient and proactive usage of this forum is to motivate and inspire economic progress based on solving issues of politics. The creation of South Asian Development Bank and a Council of Economic Advisors is another important landmark achievement. A very crucial role is played by all these institutions in solving the regional differences on areas of geopolitics and territorial disputes while pushing forward the regional development goals.

To achieve a friendly political climate will make conducive atmosphere for economic development hubs and centre of activities to become an equal partner in the global economy. By creating demanding agenda for SAARC and SAFTA, the regional leaders have set the tone for pushing the regional countries for fast growth industrialization, creating import and export zones and learning institutions for human capacity building.

On *prima facie* judgment of the South Asian regional cooperation, one may tend to conclude that so much has been achieved in the field of cooperation. Yet the fact remains that regional South Asian nations have to achieve or attain cooperative level that of western countries.

One strong reason has been unsettled disputes among regional countries such as India and China, the nagging tension between India and Pakistan and political instability in neighbouring countries like Bangladesh and Nepal.

The end of Cold War also created many new challenges for regional and international politics. As compared with the Cold War period, many uncertainties seemed to have accompanied the transformation process in South Asia, which might lead to asking the following questions:

The foremost question again is the rising power of China. What is China aiming at? Is it trying to exert and flex its economic and political power thus leading up to hegemony? If this is the case scenario, then what is the policy choices left for the South Asian countries and India in particular in its relations with neighbouring countries? What and how will India keep the relation as it is also a rising power in South Asia and which has gone nuclear besides Chinese ally Pakistan? These are very important issues which will have decisive impact on the regional stability.

3. Democratization of international relations in South Asia

The democratization of international politics implying equality among regional nations is another feature of the new regional association. At the height of Cold War era, regional nations were allied with one of the superpowers, US and USSR and even China to some extent. Despite China's proximity to the South Asian subcontinent, it could not exercise much influence like in East Asia due to the 1962 Indo China conflict.

The collapse of the Cold War ended this hierarchical relationship in South Asia. In their quest for economic development and alleviation of poverty, the formation of SAARC was important. Besides exercising leadership in SAARC, India is becoming a member of the ASEAN. India has

been an exponent of Bengal Initiative for Multisectoral Technical and Economic Cooperation (BIMSTEC) allowing regional nations to play more important role in region. Therefore, if this trend continues, it is believed that no single power, not even the remaining sole superpower US or for that matter even China can dominate relations in South Asia.

The modernization and international relations also mean a need for multilateral approach to regional affairs. A one sided policy based on power does not serve any country's interest irrespective of superpower status country like US in the world or for that again China. Henry Kissinger says in his book *Diplomacy*, "a policy of confrontation with China risks America's isolation in Asia. No Asian country would want to be – or could afford to be – supportive of American in any political conflict with China which it considered to be the result of misguided United States policy".³⁶ Thus, while supporting the traditional balance-of –power approach to China, Kissinger also warns the US against using policies that go counter the interest of the majority of East Asian countries.

4. The rise of China as a regional power in Asia

China's meteoric rise economically and politically in the region has raised some controversies. The literatures on China's rise are of the views that China is trying to become a new hegemon in Asia.³⁷ The 1979-2000 years saw very fast economic development in China with an annual growth rate of 9.5 in GDP percent as compared to 2.5 percent for developed countries and 5 percent for developing countries.³⁸

³⁶ Henry Kissinger, *Diplomacy*, Simon and Schuster: 1994, p.830

³⁷ Scholars belonging to this group include Richard Bernstein and Ross H. Munro (*The coming conflict with China*, New York : Knopf 1997) , Samuel Huntington (*The Clash of Civilization and the remaking of world order*), Bill Gertz (*The China Threat*).

³⁸ Xinhua News Agency, 26 Nov 2001

There is growing uneasiness that China's booming economy will put much pressure on the neighbouring countries, driving their exports away from their markets and outdoing in foreign investment inducement. This has become a reality with China joining the membership of World Trade Organization (WTO). It would be difficult to rule out economic benefits from China's rise. China is serving as the engine of economic growth not in Asia but globally. In 2002, China accounted for only one-twenty fifth of world output, contributed to one-sixth of global expansion which in absolute terms was more than 10 times that of Japan.³⁹ China's large markets and expanding activities have been providing business opportunities to entire Asian neighbours.

In the words of Victor D. Cha (p.109)⁴⁰, "Asia will be the fastest growing and most dynamic region of the world for generations to come." US wants China to be a "responsible stakeholder" – a term invented by former Dy. Secretary of State, Robert Zoellick meaning to be more responsible player on global and regional issues. China seems to have liked the idea which is acceptance of its place in the world by the American polity given its economic growth which might lead to many issues through cooperation.

While China emerges powerful and rises economically, the satellite countries around China remain fearful and wary of its rise. Prosperous China and economically engaged China would be peaceful and stability driven is an open question. Lack of evidence suggest that Chinese economic and military power are any less threat to other countries (Hun Joo Park, 2007,) p. 179)⁴¹

³⁹ Nicolas Lardy, *The Economic Rise of China: Threat or Opportunities?* ECON Paper, 2003

⁴⁰ Victor D. Cha (2007), *A Vision of Asia*, *The International Journal of Korean Unification Studies* Vol.16, No.2

⁴¹ Park, H. J. , " *Paradigms and Fallacies: Rethinking Northeast Asian Security and Its Implications for the Korean Peninsula*, " *The International Journal of Korean Unification Studies*, 16.1, (2007)

Out of seven SAARC countries, four countries (Bhutan, India, Nepal and Pakistan) share borders with China and in China's foreign policy, South Asia comes third in importance ranking after the Northeast and Southeast Asia. The rest of the SAARC countries form an important part of South Asia. China's military security concerns vis-à-vis its powerful neighbour, India combined with border disputes and willingness to protect its 'soft strategic underbelly' i.e. Tibet, lend a very clear perception of China's South Asia policy. (Malik, 2001, p.74)⁴²

China's approach towards South Asia policy has been mostly 'India-centric', which has seen military links dominating the policy agenda with other neighbours of India. China's main policy objective is to prevent the rise of a competitor of equal stature, a real rival to challenge China's status as the 'Middle Kingdom' in Asia. There is an old Chinese adage which says, 'one mountain cannot accommodate two tigers'. China knows that India, "if it ever gets its economic and strategic acts together, alone has the size, might, numbers and, above all, the intention to match China." Meanwhile, taking India as weak and indecisive China keeps India under pressure by supplying arms and arsenal to its neighbours and supporting insurgency movements. Many of Indian neighbours are obtaining their military arsenal from China. Beijing justifies its military relations with other South Asian countries as legitimate in keeping within the Five Principles of Peaceful Coexistence. (Malik, p.74)⁴³

China's relations with South Asian nations are based on border disputes. Beijing has protracted territorial disputes of India and Bhutan while it has resolved disputed boundaries with Nepal and Pakistan. As in China, many countries of South Asia are polyglot, polychrome and

⁴² Malik, J.M. (February 2001). *South Asia in China's Foreign Relation*. Pacific Review, Vol.13, No.1

⁴³ Ibid Malik

polyconfessional and they share borders with India. Geopolitical landscape during post colonial time has created a number of overlapping multi ethno religious and linguistic problems in the subcontinent. An internal security issue of one country has direct bearing on external security ramifications. Broadly speaking, India's relations with other South Asian states have been guided by two paramount factors: Firstly, its aspiration to shield the Subcontinent from undesirable external forces that might like to 'fish in troubled waters' and destabilizing India's security environment. Secondly, a need to ensure that physical proximity and ethno religious affinities do not lead to instability on or near its borders affecting India's political relation giving rise to secessionist demands within India.

Towards this goal, India resorted to measures like combination of diplomatic, economic and military means in order to establish security in South Asia. During 1949–1950, India signed treaties with Himalayan Kingdoms of Bhutan, Nepal and the small protectorate of Sikkim to strengthen its close links besides taking the responsibility of ensuring security in their northern frontiers with China. (Malik, 2001, p.74)⁴⁴ However, South Asian states have always resented India's dominating role in the region. They have tried to resist the imposition of the Indian version of the **Monroe Doctrine** by seeking to build security links with extra regional powers of USA and China as a counterweight to India's hegemonic ambition. This has led to India's continuing conflict with its smaller neighbours. China has insisted that political problems and border disputes must be handled according to the Five Principles of Peaceful Coexistence without resorting to force or other means.

China continues to grumble about India's 'big brotherly' attitude and hegemonic ambition. China has been critical of the use of coercive strategies by India with its neighbours and

⁴⁴ Ibid

maintenance of equal treatment irrespective of the political size of countries. Due to different sizes and might, India is regularly drawn into the big-brother syndrome or small state versus big state as in the biblical story of David versus Goliath in its relation with other smaller neighbouring countries. Whenever neighboring countries have tried to play **‘the China card’** in their relations with India, political problems have arisen between two big neighbours as well as between other South Asian neighbours. Thirdly, China’s relations with Pakistan outweighs any other bilateral relationship. No other country has armed another country in such a way like China has done with Pakistan. It is China’s grand strategy to shape the South Asian security environment with ramifications spreading to other smaller countries like Nepal and Bhutan. (Malik, 2001, p.74-75)⁴⁵

In the coming years China’s position in the international relations will remain unquestioned if it can resolve the Tibetan issue and Taiwan case. However, the risk will continue to remain so for the quest to exercise leadership among the US, China and India in the South Asian subcontinent. As mentioned above of the China’s rise and its impact, it would be a prudent move for the South Asian nations to forge into regional cooperation. In doing so, it will be for the beneficial cooperation and wellbeing of all the South Asian countries. The policy of distance and isolation will only incite a tough reaction from China.

As such, there is a strong wish for a peaceful environment for economic development and common aspirations and national interests for the rest of South Asian nations. China also thwarted isolation and launched a diplomatic offensive after the Tiananmen incident against the

⁴⁵ Ibid

diplomatic quarantine sought by US.⁴⁶ For the South and South East countries, vibrant and stable China will contribute for regional cooperation. It is also observed by Shuja that economic development leads to bigger interdependence between nations which sometimes cause diplomatic problems but in the end always promote good relations and understanding.⁴⁷

In conclusion, as stated by Robert Art, a realist approach to deal with rising China will be counterproductive.⁴⁸ Therefore, it is through the interdependence, multilateral economic and security cooperation that will engage China to bring economic development and benefits among the neighbouring countries.⁴⁹

5. The India in the new regional context

India got freedom from the British in 1947 prior to the Chinese Communist Party (CCP) which came to power in 1949. Like China, India too has a big population. According to World Bank report, some 456 million Indians or 42 % of the Indian population lived below poverty line in 2005. India has 60 million chronically malnourished children which roughly about 40% of the world's total. To make a serious impact or dent in poverty, India needs to grow its economy by 8% per annum.⁵⁰

⁴⁶ Godwin. Paul. H.B, *Force and Diplomacy: China prepares for the Twenty-First Century*, in *China and the World (Chinese Foreign policy Faces the New millennium* edited by Samuel S. Kim , Fourth Edition , Columbia University (1998),p.171-191

⁴⁷ Sharif M Shuja, *China after Deng Xiaoping: Implications for Japan*, *East Asia: An International Quarterly*, Vol.17, Spring 1999.

⁴⁸ Robert Art opines that military power will remain as the most important measure to solve conflicts among states in the future (see Robert Art, *The four functions of force*, in Robert Art and Robert Jervis, *International Politics*, Longman 1999).

⁴⁹ Robinson, Thomas W. *Interdependence in China's Post-Cold War Foreign Relations*, in *China and the World (Chinese Foreign Policy Faces the New millennium* edited by Samuel S. Kim , Fourth Edition , Columbia University (1998),p.195-213

⁵⁰ " China and India – A tale of two vulnerable economies," *The Economist* December 13-19th, 2008

India's first prime minister, Pandit Nehru envisioned a synergistic relationship with China. India also formally recognized the People's Republic of China (PRC) which also resulted the signing of Panchsheel Agreement in 1954 during premier Zhou Enlai and Indian government. However, strains of diplomatic relation showed in 1956 when China promulgated official map of China encompassing Indian territories rejecting the McMohan line demarcated by the British colonial rulers in 1914. China also constructed a network of covert roads along the disputed border in response to which India also posted construction of military outpost along the McMohan line. This proved the straw that broke the camel's back in the diplomatic relation. China's People's Liberation Army (PLA) attacked India and badly defeated unprepared Indian armies in October 1962. India lost 38,000 square kilometers of unsettled border areas. Diplomacy was called off and bilateral trade between two countries remained all time low for more than three decades.⁵¹

India also lent support in the Bangladesh's Liberation war in 1971 from Pakistan, a close ally of China. Again India went ahead in detonating an underground atomic device, proving its nuclear power capabilities in 1974. However, India under Indira Gandhi's premiership also pursued a renewal of diplomatic relations with China and met even her counterpart and indicated her aspiration for economic cooperation. Both the countries granted one another Most Favored Nation (MFN) trading status in August 1984. Nevertheless, bilateral trade amounted to \$ 190 million even in the 1990.⁵²

⁵¹ Christopher J. Rusko and Karthika Sasikumar, *India and China: From Trade to Peace?*, Asian Perspective, Vol. 31, No. 4. 2007, p. 99-123

⁵² Ibid, p.99-123

Rajiv Gandhi did his best to reconcile diplomatic relationship with China and even visited Beijing in 1988 leading to Joint Working Group (JWG). Narasimha Rao followed his predecessor's diplomatic efforts. The Sino-Indian diplomacy, however, suffered a setback during Vajpayee's government when India conducted its nuclear test in 1998. But then by 2006, a Memorandum of Understanding on Defence Cooperation was signed and increased the number of military exchanges between them.⁵³

Now India and China are moving from autarky to cautious globalization. For many years the borders were closed for trade and commerce. As the tension have deescalated, both the governments have realized that there is much to be gained from the cross border activity. Hence the Nathula Pass in Sikkim which was closed since 1962 war was reopened in 2003 which some analyst predict will lead to millions of dollars' worth trade. This old Silk Route will also open doors to link Sikkim and Tibet and there will be boom in tourism. The next proposal is the establishment of what they call a "growth quadrangle" including Northeastern India, Southwestern China, Northern Myanmar and Bangladesh.⁵⁴

In summary, India is a nuclear state in the South Asian subcontinent. Its national security reflects the country's foreign policy as well as its military policy. India's first Prime Minister realizing the need to establish the newly born independent nation as a strong and unified and as a sovereign democratic state based India's foreign and national security policies on principles of idealist nationalism. As a follower of Mahatma Gandhi and strong believer in the idea of nonviolence (Ahimsa), Nehru's firm commitment to idealist nationalism was understandable.

⁵³ Ibid .p.103

⁵⁴ Ibid, p. 114

India's unfailing faith in the policies of the United Nations and Nonalignment, Five Principles of Panchsheel (peaceful coexistence) and decolonization were all reflections of such ideals⁵⁵

If any country wanted to buy reactors, it was mandatory to sign the nuclear Non-Proliferation Treaty (NPT) along with a promise not to make bombs and open their site for inspection. If they don't they are branded outlaws like North Korea and Iran. 183 signatories kept their word. However, the Indo-US nuclear deal exempted India from the NPT's restriction and allows to 50-120 more nuclear bombs while still selling sensitive nuclear technology. With this grant of approval from the western power, "India got the privileges of a nuclear-weapons state without the responsibilities".⁵⁶ However, its immediate neighbour, Pakistan will demand the same treatment. India's constant foreign worry as the Mumbai terrorist bombing has shown is still in its neighbours like Pakistan, and Bangladesh with its semi hostile country with 153 million living on the deltas.⁵⁷

III. South Asian countries in the regional context

In the foregoing chapter and arguments I have been talking about the transformation on the South Asian subcontinent from the era of Cold War to resulting in the thawing of relationship between India and China. After the Second World War ended, the race for the superpower has escalated throughout the world between the US and USSR. Each and every country was willy-nilly drawn into the bandwagoning with the superpowers and seen how it has enhanced the

⁵⁵ Runa Das, *Explaining India's Nuclearization: Engaging Realism and Social Constructivism*, Asian Perspective , Vol.32, No.1, 2008, p. 33-70

⁵⁶ Joseph Cirincione, *Bush's Very Dangerous Deal* , Newsweek ,Special edition /issues 2009, December 2008-February 2009

⁵⁷ "India elsewhere," *The Economist* December 13-19th, 2008

importance of the regional role in the context of world affairs. The end of Cold War has demonstrated that no nation can remain an autarky and that globalization has become the order of the day through the revolution in the information technology and financial services. The international relation has grown in scope and complexity in South Asia. The East Asian tigers' financial crisis experience has also shown how interconnected and regional economies will suffer if there is no proper cooperative mechanism in place.

There is little doubt that unilateral policy of any country in the regional countries in the South will be to the national interest of that country. Landlocked countries of Bhutan and Nepal can export with shipping arrangement through other SAARC neighbouring country like Bangladesh and their ports in Chittagong which is closer than the harbor in Kolkata in India. It is argued that ports of Male and Chittagong are well suited for exporting to serve the Far East markets. Likewise it is said that from Karachi port, South Asian exports could be made to the Gulf Region and from Bombay to the markets in North America and Colombo to the European continent.

The strengthening of SAARC is important for the economic cooperation. The no end in sight of misunderstanding between Pakistan and India's relationship is a stumbling block to regional peace and stability of the subcontinent. Both the nations have to take tough diplomatic measures to break through in the relations to get anywhere.

Another important issue is that both the nations have to deal with the Chinese rising power. It is a positive sign that India is also joining as a member of ASEAN where China is also one of the members. It is through such association that China will remain engaged and further economic and diplomatic ties and pursue other cooperative regional relationships.

CHAPTER III : BHUTAN IN THE REGIONAL CONTEXT

Druk Yul, the land of Thunder Dragon better known to the outside world as Bhutan, with an area of 18,000 square miles in eastern Himalayas remained in self-imposed isolation for many centuries. The long period of isolation was given up during the reign of third monarch, King Jigme Dorji Wangchuk who was alarmed by the Chinese invasion of Tibet in 1958 and its subsequent annexation, and the 1962 war between India and China. Since then Bhutan has embarked upon an economic development plan from its barter system and has never looked back. With the exposure to the outside world after 1960 the monarchy was forced to begin a process which might be called “defensive modernization”.

1. Overview of economic reform and opening up

Bhutan is one of the smallest developing countries in the world based on forestry and agriculture which provide the main livelihood for more than 60% of the population. The harsh terrain and mountainous features create development activities difficult. The economy is closely tied up with the Indian economy. The industrial sector is still under development and backward. Most production is of cottage type. Many development projects rely on Indian migrant labor. Hydropower potential and its tourism industry are key resources. Bhutan has made some progress in increasing the country's productive base and improving social welfare. Well model education system, social and environment protection programs in Bhutan are in progress with the help of multilateral development organizations. Each economic development plan and program has taken into account the country's desire to protect the country's environment and cultural traditions. The Royal Government as part of its careful measure to protect its cultural identity encourages environmentally conscientious tourists only. Detailed and strict industrial licensing

system on trade, finance and labor with unclear policies fail to attract foreign investment.⁵⁸ SAFTA came into effect from 1 January 2006. The idea of free trade was proposed in 1995 and SAFTA was signed in January during the 12th SAARC Summit during which India promised to cut down customs tariff to 5% for items imported from other SAARC countries. Accordingly, Pakistan, India and Sri Lanka were to slash down customs duties between 0% and 5% within a period of seven years, and to be followed by Bangladesh, Bhutan, Nepal and Maldives in 10 years period.⁵⁹

Although Bhutan is considered and clubbed with one of the lowest per capita income countries in the world, Bhutanese live a more decent life than the figure implies. Unlike many of Bhutan's neighbours in South Asia, Bhutan still has plenty of land frontier left to be developed. Over 60% of the country's area is undeveloped forests, and the average landholding ceiling per family is 25 acres (Perry, p.259). In a span of 30 years, what Bhutan achieved in its economic development from the primitive barter system is remarkable considering its sparse population of 600,000. Bhutan achieved in 30 years what other nations took hundreds of years to do. Bhutan's economic development and modernization actually started in 1960 with the introduction of First Five Year Plan almost completely financed by India (Perry, p.261).⁶⁰

⁵⁸ <http://en.wikipedia.org/wiki/Economy-of-Bhutan> retrieved on 15/7/08

⁵⁹ <http://news.bbc.co.uk/2/hi/southasia/4566818.stm> retrieved on 15/7/08

⁶⁰ Perry, Stephen David. "The Promised: 'Uncaptured' Peasantry, the State and Development in Bhutan." *Canadian Journal of Development Studies* Vol.10, N.2, (1989), 257 – 575.

Before the visit of then Indian Prime Minister, Jawaharlal Nehru in 1958, many economic reforms were not initiated. The first motorable road was opened in 1960 to the capital, Thimphu from Phuntsholing, a small town near the Indian border. Today, Bhutan has more than 1,750 km of blacked topped road and 500 Km of gravel road connecting all the bustling towns in Bhutan. Although many developed countries offered to help Bhutan in its economic development projects, Bhutan could not accept them because of certain treaties with India. The 1910 Anglo Bhutanese Treaty and the 1949 Indo-Bhutan Treaty of Friendship gave the Indian government the right to 'advise' on Bhutan's external affairs. Therefore, whatever economic reforms that has been undertaken till late 1970s was almost completely through Indian financial and technical aid. The deal struck between Bhutan and India, inter alia, was a guarantee of internal stability by Bhutan in return for massive development help from India (Perry, p.261). Prime Minister Nehru stated at Paro during his visit to Bhutan in 1958:

“it is therefore essential that I make it clear to you that our only wish is that you remain an independent country, choosing your own way of life and taking the path of progress according to your will. At the same time, we two should live with mutual goodwill. We are members of the same Himalayan family and should live as friendly neighbours helping each other. Freedom of both Bhutan and India should be safeguarded so that none from the outside can do harm to it ”

2. Foreign Direct Investment Attraction

Foreign Direct Investment (FDI) has contributed in increasing the living standard of many countries and economic growth which has help to open up investment policies. Recent

International Investment Agreements (IIAs) have helped to address bilateral, multilateral and regional issues on investment policies and creating investment rules.

Bhutan is yet to measure the impact of FDI on the country's economic growth. FDI policy rules framed in 2002 still failed to attract investors into the country so far. The Royal Government has approved 13 FDI projects in Bhutan out of which only four are actively operational like high end resorts and specialty fat manufacturing units in Pasakha.⁶¹

Bhutan is in need of developing and reviewing FDI policy to gain from FDI and to take full advantage of it. If the FDI could be widen properly in Bhutanese context and situation many say it could reduce the country's heavy dependence on foreign aid.

3. Trade Development

The basic framework of India and Bhutan bilateral relations is the 1949 Treaty of Friendship and Cooperation which is characterized by close trust, understanding with extensive cooperation in the field of economic development.

Free trade relations existed between India and Bhutan. In March 1995, Indo-Bhutan Trade and Commerce Agreement was renewed for a period of 10 years and ending in March 2005. The main export products from Bhutan to India were electricity (from Chukha and Kurichhu Hydroelectric Project), forest products, agricultural produce and alcoholic beverages. Major imports exports from India are mainly petroleum products, rice, machineries, automobiles and other spares, and fabric products.

⁶¹ Kuensel, 11 December 2008, "First FDI impact study"

4. Challenges Ahead

Timed honoured traditional relationship existed between India and Bhutan and with the desire to further strengthen them. Free Trade Agreement (FTA) was entered into to reap the benefits from the free trade and commerce. Bhutan stand to gain from this FTA since Bhutan has to import everything from India and whatever Bhutan has for sale , India alone is sufficient a big market for its products. India has been exceptionally over friendly with Bhutan in comparison to other SAARC countries. As per Article –VIII, the medium of transaction in Indo Bhutan trade will continue in Indian Rupees and Bhutanese Ngultrums. In this regard, since Bhutan’s exports are mainly edible items which are tax exempted, Bhutan stands to gain by way of excise refund on whatever imports that is made from India. Excise refund also make up about almost 10% of the national revenue income of Bhutan.⁶²

As of 7 June, 2008, Bhutan was still not the member of World Trade Organization (WTO). With its hopeful membership by 2009, Bhutan will be opening up 54 of 155 services and 5,820 goods with maximum duty rates fixed inclusive of all agricultural items which might undergo few changes in final stages. Bhutan will have 152 countries as potential trading partners. A WTO negotiation team of Bhutan are in touch with WTO headquarters doing preliminary study and it is expected that Bhutan will become a WTO member after the fifth working party meeting in 2009. However, opening up of services will not be uniform. All foreign companies will have a maximum equity limited to 70 percent to a minimum of 49 percent. As such, it will be all Bhutanese registered companies governed by Bhutan’s trade laws.

⁶² <http://en.wikipedia.org/wiki/Economy-of-Bhutan> retrieved on 15/7/08)

Only a small portion in financial sector might be opened up. In non agricultural and agricultural goods, Bhutan will impose a maximum duty 100 to 150 percent on sensitive products and not beyond that if applied once. Average duty applied so far is 48.7 percent on agriculture, with red rice having a protective 100 percent maximum duty. The average duty rate is 26.3 percent on non agricultural products. Both duty rates were originally higher which was brought down to accommodate other countries' wishes.

USA has expressed interest in finance and energy sector in Bhutan. China is interested in exporting some goods while Japan in establishing car showrooms and workshops. Other western nations have shown interests too. European Union in goods and services, and extending business visa by Canada. Joining membership of WTO will open up opportunities to all other countries as well. A WTO tag will make possible for attracting foreign investment, transfer of technology and other skills to Bhutan. Bhutanese products will find ready markets abroad with favourable tariff rates. However, there will be trade imbalance if unlimited imports are made from other countries affecting foreign exchange reserves. This could force weaker competitors to shut down. Further, laws cannot be changed easily once implemented on access to duties on goods and services. Bhutanese agriculture might suffer as it is supported by poor technology. The best part of becoming a member will be a set of strong transparent domestic trade laws based on international trade laws to promote good governances.⁶³

On the issue of some Bhutanese industries suffering, "Market forces will determine the best and most competitive are left, so that consumers benefit in the end." The pros and cons side of joining WTO membership will be the advantage of disputes settlement. Bhutan will be able to

⁶³ <http://news.bbc.co.uk/2/hi/southasia/4566818.stm> retrieved on 15/708)

take big countries to court for unfair trade practices. Likewise it can also be taken to task for barring anyone against WTO trade laws.

The process started in 1999 for Bhutan when it applied for WTO membership. Since then, some legislative changes have been made in conformity with WTO norms. Agreements on sanitary and phyto-sanitary products are made and it means that sanitation and health issues will not be used to bar trade. Trade Related Intellectual Properties Rights (TRIPS) agreement also means to protect intellectual property rights. Technical Barriers to Trade (TBT) make sure that duties on products are applied in a transparent manner while ensuring the quality standards. The National Assembly will take the decision in parliament sitting of both the Houses on joining WTO membership.

Bhutan's Foreign Policy –Diversification and Multilateralism

The Indo-Bhutan Treaty of 1949 is still misinterpreted to mean that India controls Bhutan's foreign affairs which are no longer true. Bhutan handles all of its international affairs itself like border demarcation issue with China which is sensitive to India since 1962 wars. The new Treaty signed with India in 2007 clarifies that Bhutan is master of its own foreign relations. Bhutan has established diplomatic relations with 21 countries, the European Union, and has embassies in India, Bangladesh, Thailand, and Kuwait. It has UN mission offices in New York and Geneva. India and Bangladesh have residential embassies in Bhutan. Thailand has a consulate office only in Bhutan. Citizens of India and Bhutan may travel to each other's countries without a passport or visa using their national identity cards as per long standing Treaty. Bhutanese citizens may also work in India without any legal restrictions. There is no formal diplomatic relation with its northern neighbour, the People's Republic of China. However, exchanges of visits at various

levels have significantly increased in recent times between the two countries. In 1988, the first bilateral agreement between China (PRC) and Bhutan was signed while establishing consulates in Macau and Hong Kong at the same time. Bhutan's border with China is largely undemarcated and disputed in some parts.

On 8 February 2007, the Indo-Bhutan Friendship Treaty was significantly rewritten. Whereas in the Treaty of 1949, Article 2 read as ‘ “The Government of India undertakes to exercise no interference in the internal administration of Bhutan. On its part the Government of Bhutan agrees to be guided by the advice of the Government of India in regard to its external relations.” ’

In the revised version it reads now as ‘ “In keeping with the abiding ties of close friendship and cooperation between Bhutan and India, the Government of the Kingdom of Bhutan and the Government of the Republic of India shall cooperate closely with each other on issues relating to their national interests. Neither government shall allow the use of its territory for activities harmful to the national security and interest of the other” ’. The preamble is also included in the revised treaty which says that ‘ “Reaffirming their respect for each other's independence, sovereignty and territorial integrity” ’, an element which was not there in the earlier treaty. Bhutan's status as an independent and sovereign nation is strengthened by the Indo-Bhutan Friendship Treaty of 2007.

Bhutan has no diplomatic relations with all powerful nations like the United States, Russia, China, the United Kingdom or France. However, informal contacts are made through embassy in New Delhi with them.

I. Overview of Bhutan's foreign policy since 1960s

Bhutan saw the danger of China becoming more menacing in the 1950s and suspected its intention. To this was added by the Indo-Pak war and uncovered the threats of small countries to the danger of territorial integration, disestablishing and other political crisis. When India annexed a small neighbouring kingdom of Sikkim into one of the Indian states, Bhutan's aspiration to protect its sovereignty and independent status as Buddhist Kingdom has been intensified. Therefore, Bhutan's joining as a member of SAARC was a direction in that to avert outside threats and to improve its relations with other South Asian nations. Constrained by its low economic development, Bhutan saw huge scope to expand its trade within the regional South Asian nations.⁶⁴

The intervention of Afghan problems by the Soviet Union in 1979 coinciding with Mrs. Indira Gandhi's victory in Indian election in 1980 caused anxiety and concern in the subcontinent. USA reacted by sending more envoys to convince their leaders in India and Pakistan to initiate regional approach to the new emerging political situation in the region. At this juncture, the president of Bangladesh, Mr. Zia-ur Raman took the initiative of addressing through official correspondences to all the leaders of the seven regional countries seeking immediate regional cooperation to deal with the prevailing tense situation in 1980. Being a small landlocked country with limited military and economic capacity, Bhutan welcomed the idea with great enthusiasm. It is also said that the concept of SAARC was originated from the third King of Bhutan before the 1971 Indo Pak war. He envisaged of 3 nations of India, Bangladesh and Bhutan forming regional cooperation as a start and then to further extend into other countries.

⁶⁴ Kyoko Inoe, Mayumi Murayama et al (2004), Sub-Regional Relations in The Eastern South Asia with special Focus on Bangladesh and Bhutan , Institute of Developing Economies, Chiba 261-8545, Tokyo, Japan

Despite Pakistan and India's hesitation, Bhutan endorsed the proposal of forming regional organization.

II .Relations with Regional countries

After shedding its many years of self imposed isolation in the early 1960s, Bhutan is now fast catching up with all its other neighbouring nations. Therefore, Bhutan continues to develop and keep good diplomatic relations with all neighbouring countries in the region and beyond. It is also responsible as member of the international community to play an active part and role.. The overall foreign policy objective is to fulfill by keeping Bhutan's friends and development partners informed regularly of the development activities in the country through diplomatic missions and other channels of communications. The following passages sumps up the various stages of relations shared with other nations.

1. Relations with India

Bhutan and India has a very unique relationship. A small and a big nation can stay side by side and develop together if the country is bestowed with enlightened leaderships and stable government. India has helped to finance most of the development projects in Bhutan especially hydropower and they have bought much of the power generated from the project. When the British left India, Bhutan felt the need to look India from a different perspective with regard to the Treaty of Punakha signed in 1910 which did not define the status of Bhutan well. The British did not find Bhutan's external relation necessary as long as it was inward looking and isolated which actually happened for many years. With the signing of **Treaty of 1949**, Bhutan got back

32 square kilometer of Dewangiri or Deothang ceded by the Treaty of Sinchula signed in 1865 so as to remove any fear from Bhutan on its independence status. (Penjore, 2004, p.119)⁶⁵

For a long time, India has been Bhutan's economic development partner. Over the years, Bhutan has gained some sort of confidence in its relation with India. In the most recent visit of Indian Prime Minister to Bhutan, Dr. Manmohan Singh promised the nation that India would commit 100 billion Rupees for the 10th Five Year Plan He has reiterated to buy electricity in the future too. (Kuensel, 17 May 2008)⁶⁶

2. Relations with China

The emergence of People's Republic of China (PRC) in 19649 intensified its suzerainty claim on Bhutan marking the beginning of an acrimonious relation with new China.⁶⁷ (Penjore,2004 p.113) Despite sharing common border, Bhutan and China are the only countries with no diplomatic relation. People Liberation Army (PLA)'s incursion into border areas which is not demarcated properly has been a threat to its integrity and national security during the last many decades. Chinese authorities are putting subtle pressure on Bhutan to start a diplomatic relation. Establishing diplomatic relation with China is made an unnecessary condition to solve the border problems and dispute. What can be deduced from this diplomatic relations with China on Indo-Bhutan relation?

⁶⁵ Penjor, D. (2004). "*Security of Bhutan : Walking between the Giants*" Journal of Bhutan Studies, Vol.10, Summer 2004

⁶⁶ Dorji, K. "*A meeting of Minds.*" Retrieved on 28 May 2008 from <http://www.kuenselonline.com>.

⁶⁷ Penjor, D. (2004). "*Security of Bhutan : Walking between the Giants*" Journal of Bhutan Studies, Vol.10, Summer 2004

Historically, Bhutan has closer ties with Tibet than India. However, geo-political and historical factors have led to seal the relation in 1960 after Tibet's annexation by China. Beijing's unwelcome claim on Bhutan completely tilted the balance in favour of Indian relation. What interest did China has in Bhutan? Most historians point out that it was nothing more than to bring Bhutan under its area of influence and to stop the British expansionism in Asian political arena. Beijing always used its old ambiguous tool of "middle kingdom" suzerainty in its relation with neighbours. However, it backfired in its relation with Bhutan. Hardly there is any evidence of two having relation until the Ching dynasty kept its residents in Lhasa in 1720. Chinese made great efforts to exercise its 'historic' rights of claim over Bhutan between 1865 when the Treaty of Sinchula was signed and the Treaty of Punakha in 1910. The signing of 1949 Treaty of Indo-Bhutan Friendship brought Bhutan under Indian influence. Even in the early 1930, the PRC was interested in forming the 'Himalayan Federation 'made up of neighboring state of Tibet, Nepal, Ladakh, Sikkim to extend its political ideology and influence to south. Chinese have always wanted to extend its suzerainty over Bhutan as early as 1731 based on their historian Tiehtsung. The history is based on a certain Tibet's ruler called Polhanas who misinformed the overlord of Ching dynasty that Bhutan was under him.

a) Border Problem

Sino-Bhutan border dispute is not so much a contest over territory as it is of Beijing's desire to penalize Bhutan for being over friendly with its arch rival, India. Border problem of two countries is only a tip of an iceberg. The border had never been demarcated (Mathou, p.396)⁶⁸ Until the Chinese annexation of Tibet in 1959, a 470-kilometer long unmarked border along Tibetan plateau and Bhutan was much of a trouble between the peoples of both countries. China takes that disputes on the border as a source of differences and warned that only a small incident will incite confrontation between two nations. Both Tibetan yak herders and even PLA, cross over into what Bhutan considers as its territory while Bhutanese highland herders too stray into what China considers as its land. The herdsmen of both countries have been asserting traditional pasturelands rights leading to claims and counterclaims on disputed border. It became a serious security threat after Chinese's incursion into Bhutanese territory in September 1979. When Bhutan protested, Beijing expressed its desire to solve the problem bilaterally following which Bhutan's Tshogdu (National Assembly) deliberated on normalizing relation with China and initiating direct talks to solve the problem. This incident led to a direct Sino-Bhutan border talk. Up till then Bhutan's border issues with China has been incorporated with the Sino-Indian border discussion.

The formal discussion was held in 1984 in Beijing while the initial talks has started in 1981.(Mathou , p.400)⁶⁹ Since then the talks was held alternatively in two capitals. China always asserts that 1949 Treaty of Indo-Bhutan Treaty is an 'unequal' treaty and regards it as a symbol of Indian hegemony. Although the progress has been slow on the border disputes, lots of differences seemed to have narrowed.

⁶⁸ Mathou, T.(2006) *Bhutan – China Relations: Towards a new step in Himalayan Politics*. Retrieved on 20 June 2008 from <http://www.bhutanstudies.org.bt/admin/pubFile/19-Spdr&pglt.pdf>

⁶⁹ Ibid

b) Border Resolution for Diplomatic Relation

As stated earlier by J Malik, Bhutan is the only neighboring state in SAARC region that has maintain any diplomatic relation with its immediate northern neighbour, China. It became clear from the second round of talks in 1985 of Chinese interest of expanding contact. In 1996 the Chinese started logging and road construction activities in the disputed border areas making issues to be brought up in the 11th round of talks. China then proposed for signing an interim agreement for maintenance of peace and security along the borders. This agreement signed on 8 December 1998 in the 12th round represents the first legal document that is signed between two countries. Till then, China has never recognized Bhutan's sovereignty and always asserted its suzerainty over Bhutan as part of Chinese territory. China's approach in settling border issue is through a 'package deal' rather than sector wise issue. China also suggested exchanging 495 square kilometers area with an area of 269 square kilometers in north-western Bhutan during the 11th round of talks held in Beijing. A small strip of border land at Sinchulumba in North West is very close to Chumbi valley and shares border with an Indian state of Sikkim. However, this particular swapping of border areas will have seriously undermined India's security by shifting the Sino-Bhutan border to the south. Nonetheless, both sides agreed to discuss at technical level, and later to decide on territories on the maps of both the countries. In 2004, Thimphu hosted the 18th round of talks.(Penjor, 2004,117)⁷⁰ Thimphu and Beijing have increased their contacts through yearly consultation on border disputes. Cultural visits followed by participation in regional security issues, hydropower development and tourism.

One China policy has always been maintained by Bhutan in international arena. Bhutan has voted for restoring China's United Nations' seat in 1971. During its 55th UN General

⁷⁰ Ibid Penjor

Assembly's Vice-Chairmanship, Bhutan rejected Taiwan's bid to participate in UN and WHO and opposed Taiwan's proposal to host 2002 Asian Games. Although there is no diplomatic mission between two countries, the Chinese ambassador in New Delhi has visited Bhutan since 1994 on regular basis. Bhutan's ambassador to India visited China in 2000 as a reciprocal gesture. These exchanges of visits have opened avenues for exploring views on different issues and border disputes.

An unresolved border dispute with China has been a concern for Bhutan's national security and territorial sovereignty which need to be solved soon. However, if diplomatic relation is a precondition for resolving border problem with China, how it is going to affect Indo-Bhutan relation is a big question. For Bhutan, it is the last thing to antagonize relation with India who has been mainstay and benefactor since the 1960s in its efforts on development and economic policies apart from addressing security support. (Penjore,p.117)⁷¹

Thus, China's economic and political rise has provoked controversies on its role in the region. Among the vast literature on China, two major schools of thought can be identified. The first views China as potential threat to the US and neighboring countries as it attempts to become a new hegemon in East Asia.⁷² The second school regards China as merely a developing country with numerous challenges and problems ahead. The period from 1979-2000 has seen the fastest economic development in China with an annual Gross Domestic Product (GDP) growth rate of 9.5 percent as compared to with 2.5 percent in other developed countries and 5 percent for developing countries.⁷³ Sustained economic development and, subsequently, increased military

⁷¹ Ibid Penjor

⁷² Scholars belonging to this group include Richard Bernstein and Ross H. Munro (The coming conflict with China, New York : Knopf 1997) , Samuel Huntington (The Clash of Civilization and the remaking of world order), Bill Gertz (The China Threat).

⁷³ Xinhua News Agency, 26 Nov 2001

strength have allowed China to gradually enhance its status as big power in East Asia and for that matter in whole South Asia. The main question here is how China's rise has influenced economic and political development in Asia as a whole.

There has been a widespread fear that China's booming economy will put strong pressure on Asian nation states, driving their exports away from third markets and outdoing them in foreign investment inducement. This has been occurring in reality, particularly since China's accession into the WTO. However, it would be a social gaffe to rule out positive effect of China's economic rise. Concurrently China is serving as an engine of growth in Asia as well as globally. In 2002, China alone accounted for one-twenty fifth of world output and contributed to one-sixth of global expansion. ; its economic expansion in absolute terms was more than 10 times that of Japan.⁷⁴ China's large market and expanding activities has also been providing new business opportunities to other Asian neighbours.

On the other hand, there remain unresolved issues between China and neighbouring countries. In all major disputes in East Asia linking Taiwan, Korean peninsula issues and South China Sea, China is involved directly in all this quagmires. While Beijing has been willing to cooperate on various areas with other countries, its position remains tough regarding territorial issues.

In the coming years, if China succeeds in sustaining economic growth and resolving domestic problems such as Tibet, it may become a superpower in East and in the world. Thus, the possibility that the quest for regional leadership among the US, China and also Japan will then risk undermining the peaceful environment in East Asia.

⁷⁴ Nicolas Lardy, *The Economic Rise of China: Threat or Opportunities?* ECON Paper, 2003

Given the above mentioned impact of China's rise, it would be beneficial for Asian countries to engage into regional cooperation. By so doing, they may take advantage of China's economic rise and at the same avoid possible conflicts with China, which may result in disastrous consequences for the whole region. Whatsoever, a policy of isolation or containment only worsens the situation and unnecessarily provokes tough reaction from China.

There are common interests between China and the rest of the region. All need a peaceful environment for economic development. For Asian countries, stable and developed China is more conducive for regional cooperation. In the past, China has always turned aggressive when it has faced domestic trouble or unrest. As observed by Shuja (1999), economic development and prosperity entail greater interdependence with other countries. In the short term, interdependence can cause difficulties in the relationship but it will foster understanding in the long term.⁷⁵

There is also a realist approach to deal with the security challenge posed by China which will not work well.⁷⁶ East Asia need multilateral security cooperation, not forces, to engage China. So does in South Asia. The main argument for multilateral security cooperation is that it will benefit members through the provision of stable and predictable environment. It would also bind China into a common framework with rules and norms that would be hard to break. It is, therefore, important that all regional SAARC member countries namely India, Pakistan, Sri Lanka and others to participate in this framework.

⁷⁵ Sharif M Shuja, *China after Deng Xiaoping: Implications for Japan, East Asia: An International Quarterly*, Vol.17, Spring 1999.

⁷⁶ Robert Art opines that military power will remain as the most important measure to solve conflicts among states in the future (see Robert Art, *The four functions of force*, in Robert Art and Robert Jervis, *International Politics*, Longman 1999).

3. Relations with Nepal

Nepal and Bhutan are in the same Himalayan range. The formidable mountainous terrains of Bhutan are the biggest hurdle in promoting socio economic development and contacts with outside world thereby nurturing a sense of solidarity and interdependence within closed settlements. Solidarity as confirmed by various researchers has reduced the community's ability to cooperate with outsiders. In this connection, social capital flourishes within a narrow circle of families and personal friends (Fukuyama, 1991).⁷⁷

Bhutan and Nepal are in many ways similar in social and political structure too. Both the countries are ruled by kings. Besides being neighbours, both the nations are facing challenges in the current political scenarios, while Bhutan King has started to hand over the authority of power to the elected leaders, Nepal King asserted his authority with much vigour, to the chagrin of the Maoist rebels. (Hutt, 2005, p.83).⁷⁸ The year 2006 saw the downfall of Nepal King's attempt to re-establish monarchical rule. (Gellner, 2007, p.80)⁷⁹ On the other hand, Bhutan king enjoyed much popularity among the masses of his people and Bhutanese subjects will always remain grateful for divesting his power and remaining fountain head of wisdom in this stage of turmoil in all over the world. The Nepalese minority in Bhutan tried to bring about turmoil in a small and peaceful society in the country on the grounds of ethnic cleansing by Thimphu government. Despite the merits of social capital, this is one of the dark aspects and sides of the social capital.

⁷⁷ Fukuyama, F. (1991) '*Social Capital and Development: The Coming Agenda*', *SAIS Review Vol. XXII No.1*.

⁷⁸ Michael Hutt, (Jan/Feb 2005). *Nepal and Bhutan in 2004: Two Kings, Two Futures*. *Asian Survey*, Vol XIV, No.1, p.83-87

⁷⁹ Gellner, D.N. (2006), *Nepal and Bhutan (A Year of Revolution)*, *Asian Survey Vol.XL VII. No.1*

Bhutan has recently ushered in Druk Phuesum Tshogpa (Bhutan Prosperity Party) into the new parliament by landslide victory. The party is very popular among the people as it was a pro royalist and enjoyed social capital support like people. (Thibodeaux (2008, 25 March)⁸⁰. The country and new parliament also accepted and passed the Constitution intact. (Palden, 2008).⁸¹ While neighbouring country like in Nepal, the system of rule is “Panchayat System” adopted in 1960 and lasted till people were unhappy and started the “People’s Movement” (Jan Andolan) in 1990. (Gellner, 2007, p.80) Nepal has become a republic recently ending 240 years of monarchy and hoping to change the social capital scenario of the country. (Karmali, 30 June 2008)⁸² In this light, Thimphu hopes to settle the Bhutan’s Nepali refugees problems in Nepal very urgently bringing about social capital development and economic prosperity in the region.

As recent as 9th Plan, although macroeconomic conditions are favorable, Thimphu could not make headway in improving the private sector. Besides that, Nepal and Bhutan still have to make headway in the settlement of thousands of Bhutanese refugees in eastern Nepal.(Thierry, 2002, p. 192) ⁸³ Today Nepal is politically disturbed country too. Strikes and all forms of street protests are the order of the day. If bad politics are continued for a long time, development of social capital that bind people together will no longer be there. (Upadyaya, 2008)⁸⁴ This is the status of

⁸⁰ Thibodeaux, R. (2008). *Monarchy loyalist party wins Bhutan election*. Retrieved on 28/6/08 from <http://www.voanews.com/english/archive/2008-03/2008-03-25-voa12.cfm?CFD5990231&CFTOKEN=14443789>

⁸¹ Palden, T. (2008). *Constitution accepted intact*. Retrieved on 31 May 2008 from <http://www.kuenselonline.com>

⁸² Karmali, N. (30 June 2008). *Himalayan Vistas*. Forbes Asia

⁸³ Mathou, T. (Jan/Feb 2002). *Bhutan in 2001: At the Crossword*. Asian Survey, Vol.XII, No.1, p192-197

⁸⁴ Upadhyaya, N.P.(2008). Social Capital and Political Culture. Retrieved on 26/6/08 from <http://www.telegraphnepal.com/news-detl.php?news-id=3375>

relations between Bhutanese and Nepali .In the context of social development of Bhutan, one cannot help but to draw upon more inspiration from the experiences of other countries and apply them to achieve further goals in its relations with Nepal.

The commercial relations between two countries are not large. However, efforts have been made to increase within the framework of SAARC. There is no framework to conduct trade except for the one Trade and Transit Agreements that both the countries have signed with India. The Bhutan Chamber of Commerce and Industry (BCCI) and the Federation of Nepalese Chamber of Commerce and Industry (FNCCI) signed in 2003 a Memorandum of Understanding for increasing economic cooperation and mutually beneficial trade.

Many sacred Buddhist sites such Buodhanath Stupa and Lord Buddha's birthplace in Lumbini are destination centres for Bhutanese pilgrimages. Both has great potential to enhance bilateral relation through cultural cooperation given continued flourishing of Buddhism in Nepal where as it permeates all aspects of life in Bhutan.

4. Relations with Bangladesh

Bangladesh is second most important country as a neighbour after India. We have diplomatic relations since 1973 and residential ambassadorial posts in both the countries since 1979. Even from ancient times, caravan loaded with trade goods has travelled there and the saints from Bengal like Tilopa and Naropa are part of Bhutan's inspiration even today. The relations between two countries strengthened when Bhutan showed sympathy for its liberation movement and recognition of its independence.

A bilateral trade agreement was signed in September 1980 between 2 countries with the usage of transit trade routes like road and rail through India. The volume of trade increased when Bhutan started to export its surplus products to Bangladesh and other third countries following the liberal trade agreement with India in 1988. The important trade exit points include Chittagong port in Bangladesh providing a link for Bhutan's overseas trade.

Bangladesh is an alternative destination and market for Bhutanese traders for hard currency.

The primary products of Bhutan are the main exports which are worth US\$ 5 million annually. The main imports from Bangladesh consist of readymade garments and auto machineries. Dhaka also granted and 50% concession on handling charges and Fifth Freedom Rights to the Druk Air, Royal Bhutan Airlines. Like in India, Bhutan has also benefitted from the scholarships in the field of medicine and engineering in Bangladesh.

The two countries have signed an agreement to co-operate in identifying flood control measures to implement during summer months which is a constant threat to Bangladesh.

In summing up, the bilateral agreements signed between the two countries include the (1) 1980 Trade Agreement and Protocol to the Trade Agreement signed in 1984; (2) 1984 Agreement signed on Economic and Technical Co-operation; (3) Air Services Agreement; (4) Cultural Co-operation Agreement. Besides formal diplomatic ties, both the countries' wholehearted response to Bangladesh's former President Zia's proposal in the formation of SAARC resulted in mutual benefits. Bhutan also lent cooperation to Bangladesh joining other international organizations.

Besides, this relationship has also helped Bhutan diversify its trade and reduce complete dependence on India. The total value of Bhutan's exports in 2001 was Nu. 222.4 million.⁸⁵

5. Relations with other regional SAARC countries

Among the SAARC regional countries, Bhutan is pursuing the diplomatic relations with the following countries and trying its best to work within the framework of SAARC and to enrich the quality of lives among the people in the respective countries.

Maldives

Bhutan's diplomatic relations with the coral island of Maldives in the Indian Ocean started in 1984 with an accreditation of Bhutan's Bangladesh ambassador to Maldives. So was the role of Maldivian ambassador to Sri Lanka to Bhutan. Cooperation between the two countries resulted in exchanges to take place in the field of health sectors and notes on visa free travel between two countries to be concluded. A steady stream of high officials' visits has been increased since 1987 to enhance the relationship.

Pakistan

Pakistan is the last country in SAARC region with whom Bhutan established its diplomat relations in 1988. A bilateral relation between them is unique one in the context of multilateral relations in South Asia as well as international levels. As members of SAARC, United Nations, and the Non-aligned Nations Groups, the two nations will be interacting at the forums. In fact, Bhutan's relations with Pakistan are limited by its special close friendship with India and because of geographical reality and therefore, nothing to offer to each other. The relations will

⁸⁵ Kyoko Inoe, Mayumi Murayama et al (2004), Sub-Regional Relations in The Eastern South Asia with special Focus on Bangladesh and Bhutan , Institute of Developing Economies, Chiba 261-8545, Tokyo, Japan

never reach the status of cordiality like that of India unless some cataclysmic event takes place in South Asia.⁸⁶

Sri Lanka

The two countries established diplomatic relations since 1987 and both the countries are rich in Buddhist tradition. There has been enough interaction after Sri Lankan Government and Tamil United Liberation Front (TULF) chose Thimphu as a venue for holding talks in 1985. Bhutan has availed Sri Lankan universities to availed training for the Bhutanese in the field of medicine and other fields like social sciences like planning, management and statistics.

Under SAPTA, Sri Lanka granted a special tariff import rate which is 15 % of the 20 % SAARC rate as an LDC for Bhutan on apples and concessions for oranges, processed fruits, and wood products. Likewise, Bhutan has granted concessions on the import of tires, chocolates and semi-precious stones from Sri Lanka.

CONCLUSION: TOWARDS GREATER COOPERATION IN SOUTH ASIA IN THE 21ST CENTURY

The paper so far has analyzed the regional association of countries in South Asia and its impact on regional countries focusing on Bhutan. In conclusion, one can confidently say that Bhutan has come a long way into the international arena in its own way setting its own way of life and economic growth path. Bhutan also expects the two powerful neighboring giants to exercise their political wisdom for the regional cooperation for the coming future. Although given the existing animosity and mistrust between Indo-China relationship after 1962 wars and Indo-Pakistan's

⁸⁶ Bholia, P.L, Bhutan-Pakistan Relations, in Ramakant and R. C. Misra (eds) 1998, Bhutan – Society and Polity , South Asia Studies Centre, University of Rajasthan, Jaipur, India, p.308-320

volatile relationship, peaceful relations are open questions. Nonetheless, it is expected that wisdom will prevail in the end and bring about many meaningful multilateral cooperation in the regions

Immediately following the end of the Cold War, there was a mood of triumph and excitement throughout the capitals of western world. Communism ideology had failed. The Western capitalist philosophy had won. Mankind had realized “ the end of history ”. Therefore, all societies all around the globe, irrespective of their stage of social and economic development, would become replicas of liberal democratic societies found in the West. The export of democracy from the West to the Rest was seen as unmitigated good.(Mahbubani, 2004,p.12)⁸⁷ In Bhutan, Fourth King Wangchuck abdicated in favour of his son and ushered in democracy in March 2008. In stark contrast, Nepal King Gyanendra tried to reverse the democratic process and reintroduce royal rule. (Gellner, 2006, p.86)⁸⁸

It is hoped that India and Pakistan will rise above the issues that have dragged them to constant conflict of national interest and finally wisdom will prevail among them. In the 21st century South Asia has great opportunities to foster closer economic and political cooperation . In the prevailing context of the South Asian cooperation and conflicts coexist and uncertainties abound, by strengthening domestic economic fundamentals and maintaining a multilateral and balanced approach to regional issues, regional countries can take advantage of new opportunities for economic development and contribute to sustained peace and stability.

⁸⁷ Mahbubani, K. (2004), *Can Asians Think?* , Utopia Press Pvt Ltd, Singapore

⁸⁸ Gellner, D.N. (2006), *Nepal and Bhutan (A Year of Revolution)* , Asian Survey Vol.XL VII. NO.1

On the other hand, it is not an exaggeration when we say, out of 1.3 billion population, one out of every five people on the planet live in China. The economy is roughly half the size of that of the United States now and it is expected that the two will be equal in three decades. What the Chinese do in their everyday lives, will have a bearing on the availability of natural resources, prices of energy, environmental impact on the planet and the prosperity of mankind.⁸⁹

The two important sub-regional level initiatives taken are further positive signs: 1) Bangladesh-Bhutan-India-Nepal Quadrilateral Growth Initiative (BBIN-QGI) and (2), Bangladesh-India-Myanmar-Sri Lanka-Thailand Economic Cooperation (BIMST-EC). The first one is pursued under SAARC region whereas the other involves two countries belonging to the ASEAN.

Therefore, it is a positive sign that such Growth Zone Approach to economic development goals can help achieve higher levels of regional integration providing flexibilities to exploit existing economic complementarities.

The Gross National Happiness (GNH) policy is built on four pillars: 1) preservation of environment preservation, 2) promotion of cultural heritage, 3) equal socio economic development, and 4) good governance. While this concept is the guiding principle for Bhutan's vision 2020, less is written on its practical application for achievement (Allison, 2003, p.1162; Thinley, 2005, p.3)⁹⁰. Therefore, the concept of GNH should not just remain a slogan but work

⁸⁹ Richard N. Haass, *Bringing China into the Fold*, Newsweek ,Special edition /issues 2009, December 2008-February 2009

⁹⁰ Allison, E. (2003). 'Gross National Happiness and Biodiversity Conservation in Bhutan.' www.bhutanstudies.org.bt/seminar/0402-gnh/GHN-papers-3rd_49-57.pdf (26/6/2008)

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towards achieving long term sustainable development for social well being of our society. Social capital to promote trust, develop networks, cooperation and other norms of reciprocity seems appropriate in the society at this stage. The reforms for governance started even before the National Assembly was started in 1953 and putting importance on the role of civil society and social capital. (Gnaur, 2006, p.2,3)⁹¹

In final analysis, we must not waste our resources and energies funneling into regional conflict but rather take the opportunities to bring about economic prosperity as the following sayings go.

“Don’t let the urgent crowd out the important”

Jian wang zhi lai, “Know the Future in the Mirror of the Past” - Chinese saying

⁹¹ Gnaur, Jens (2006), ‘Good Governance and Public Administration Reform in Bhutan’ at <http://www.danidaderforum.um./NR/rdonlyre/4BC2D2C2-CA84-475D-92BD-147953> BB21CD/0/Bhutan-Pdf

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