

WHAT HAS CHANGED AFTER THE WORLD TRADE ORGANIZATION MEMBERSHIP OF CHINA: OPPORTUNITIES AND CHALLENGES

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August 2007

ABSTRACT

The year 2007 marks the sixth year of China's accession to the World Trade Organization (WTO). China's entry into WTO brought one of the world's largest economies under global trade liberalising rules. It is apparent that this development would have some inevitable results. In the six years, the country has changed in many positive ways. The ideas of market economy and trade and investment liberalizations have been integrated into popular thinking. Since its WTO entry, China's economic relations with the rest of the world has changed, China's imports have soared. Both China and the global community benefit from international investment and trade, and the country now has a higher stake in keeping the multilateral trading system open. China's WTO accession has also changed the global economic landscape. The Chinese economy has grown rapidly over the last six years and surpassed the United Kingdom to become the world's fourth-largest economy. China has also become the world's third-largest trading country after the United States and European Union. The country has also become one of the most popular destinations for foreign direct investment. Though consumers around the world benefit from the lower prices of products made in China, the country's rapidly rising exports have become the frequent target of antidumping suits. While some warn that the real challenges facing the country are further market openings, others are looking forward to more market opportunities and progress on issues such as the protection of intellectual property rights (IPR). The aim of the paper is to analyse all aspects of China's entry into WTO.

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1. Introduction

China has a tradition of trade in the history. The famous Silk Road opened the trade between China and the West. China's accession to the World Trade Organization (WTO) on December 11, 2001, following fifteen years of difficult negotiations was a turning point both for the WTO and its members and for China.

With its accession to the WTO, China became one of the last major trading nations to join that organization. China is prepared to become an important player in the global economy. WTO membership generated tremendous benefits for China; expanding trade, further economic reform, attracting even higher levels of foreign investment and fostering the rule of law.

WTO membership pushed significant responsibilities and challenges on China. Besides, it fundamentally redefined China's relations with other countries, like its neighbours in the Asian region and especially with the United States (U.S.), its most significant export market.

Chinese government officials and those who followed the progress of the negotiations over the years knew that accession would bring with it the necessity of a large number of reforms in domestic economic policies. It would be also difficult to implement some of the accession-related changes in a way that met the expectations of China's trading partners.

WTO membership also brought with it the opportunity to take advantage of new market access opportunities and new protections now available to China under the rules-based system of the WTO.

As a non-member of the WTO, China found that its exports were often the subject of discriminatory treatment in overseas markets. In addition, as a country that was making the transition from a centrally planned economy to market economy, China often saw its exporting enterprises subjected to anti-dumping actions that treated Chinese exporters unfairly -often because of China's designation as a 'non-market economy'.¹ However China still is a socialist market economy.

¹ Gong Baihua , Managing The Challenges of WTO Participation: Case Study 11, Shanghai's WTO Affairs Consultation Center: Working Together to Take Advantage of WTO Membership
http://www.wto.org/english/res_e/booksp_e/casestudies_e/case11_e.htm

When China and the European Union (EU) reached bilateral agreement on the terms of China's WTO accession and signed an accord to this effect in May 2000, it became clear that China's WTO accession process was being accelerated. However, EU and China relations will not be examined in this paper.

The year 2007 marks the sixth year of China's accession to the WTO. The country entered the "post-WTO transition period" by the end of 2006. But governments and businesses inside and outside China have different expectations for the future. Some warn that the real challenges facing the country are further market openings and the ability of the PRC leadership and economy to withstand such tests. Others, however are looking forward to more market opportunities and progress on issues such as the protection of intellectual property rights (IPR).²

2. Opportunities of Joining WTO

The central argument in favour of accession was that China should pursue modernization and take its rightful place among the leading world powers in the global institutions and WTO accession was the vehicle for this.³

The November 15th, 1999 U.S.-Sino agreement on the terms for China to join the WTO was the most significant deal between the two countries since diplomatic relations were established three decades ago.

The major economic benefits China derived from its WTO membership include stability in external economic relationships; firmer and speedier economic reform; long-term growth based on efficiency and innovation.⁴

²Wang Yong, China in the WTO: A Chinese View, How is China assessing its first five years with the WTO, and what does the future hold?

<http://www.chinabusinessreview.com/public/0609/yong.html>

³ Glenda Mallon, John Whalley, China's Post Accession WTO Stance, NBER Working Paper Series, 10649, August 2004, p.6.

<http://www.nber.org/papers/w10649>

⁴ Leonard K. Cheng, China's Economic Benefits from Its WTO Membership, Center for Economic Development, December 1999.

<http://www.bm.ust.hk/~ced/wto.htm>

Membership created winners and losers on both sides. After entering the WTO, China enjoys the most favoured nation (MFN) status as a member country. This enables China to enjoy the advantages offered by other countries and regions opening their markets and it also cause the main trading countries to gradually abolish their discriminatory practices, thereby promoting China's export trade.

MFN status gave China the same trading privileges enjoyed without annual review by almost every other U.S. trading partner.⁵ China was important enough to receive MFN treatment from almost all countries even prior to joining, and some suggested that by joining under such demanding terms, it was opening itself up to challenges that could have actually reduced its market access.⁶

China has enjoyed MFN since 1980 but only by an annual vote of Congress. Joining the WTO does not give China any trading advantage with the U.S. that it did not enjoy but China anticipated that securing MFN status will remove the Congress' annual examination of its human rights, labour and environmental record.

For the U.S., the agreement granted access to the Chinese market for both U.S. exports and investments, including in politically sensitive sectors like banking, insurance, and telecommunications. As it was expected, it improved the chances for relations to develop peacefully on the basis of mutual interest.⁷ U.S. benefits from greater export opportunities in China, more job creation at home and more diverse options for overseas investment.

2.1. The Society and the social issues

In the six years since China joined the WTO, the country has changed in many positive ways. The ideas of market economy and trade and investment liberalizations have been integrated

⁵ Martin and Kathleen Feldstein, China gambles on WTO entry, Originally published in The Boston Globe, February 1, 2000

<http://www.nber.org/feldstein/bg020100.html>

⁶ Robert Z. Lawrence, China and the Multilateral Trading System, NBER Working Paper Series, 12759, December 2006, p.15.

<http://www.nber.org/papers/w12759>

⁷ China in the WTO: The Debate, Volume 4, Number 38, December 1999, Written by James H. Nolt, World Policy Institute, Editors: Tom Barry (IRC) and Martha Honey (IPS)

<http://www.fpif.org/briefs/vol4/v4n38china.html>

into popular thinking. More important, the Chinese public now widely accepts core WTO concepts such as transparency, accountable governance, and national treatment.

In 2004, the PRC Constitution was revised to include concepts of property rights and human rights. The public has become more involved in policymaking than in the past in part because the media frequently publishes commentary on government policy that stimulates public discussion. In addition, government bodies release draft laws and regulations for public comment and often host public hearings to which companies and private citizens are invited. That these developments have happened in the first six years of China's WTO accession seems to support the argument that economic liberalization helps foster greater openness.

WTO membership is likely to improve workers' rights in China over the long term. Foreign employers in China today typically pay wages many times higher than those paid by domestic firms. Opening the way for more U.S. investment in China will improve wages and spread information among Chinese workers about the superior rights of workers abroad.

Isolating China from the world community is not an effective way to encourage either democratization or human rights. Joining the WTO did not resolve the many deep social, political and economic problems of China. However, expanded foreign commercial relations have contributed to a significant increase in the standard of living and life alternatives of most Chinese.

China's WTO accession has also changed the global economic landscape. The Chinese economy has grown rapidly over the last six years and recently surpassed the United Kingdom to become the world's fourth-largest economy. China has also become the world's third-largest trading country after the U.S. and the E.U.; its total trade volume hit a record \$1.4 trillion in 2005. The country has also become one of the most popular destinations for foreign direct investment, attracting nearly \$230 billion between 2002 and 2005.⁸

⁸Wang Yong, China in the WTO: A Chinese View, How is China assessing its first five years with the WTO, and what does the future hold?
<http://www.chinabusinessreview.com/public/0609/yong.html>

2.2. Trade, Labour and Growth

Since its WTO entry, China's imports have increased. For example, from 2001 to 2005, imports from the U.S. rose more than 21 percent each year on average, while overall imports grew 28.6 percent annually on average. China has also actively participated in regional and global economic integration. Indeed, it signed the landmark free-trade agreement (FTA) with the Association of Southeast Asian Nations in 2002 and also inked an FTA with Chile in 2005. China is currently negotiating FTAs with more than 20 countries. Both China and the global community benefit from international investment and trade and the country now has a higher stake in keeping the multilateral trading system open.⁹

China become in a better position to attract foreign investors who use China as their export platform. In addition, it also attracted foreign investors who feel more secure about developing China's domestic market. Regardless of whether it is export-oriented or attracted by the huge domestic market, FDI not only brings in additional capital but more importantly management, technology, market information and global production and distribution networks that link China more tightly to the other economies.

Growth has been spread over the last two and half decades with high average annual real GDP growth rates of nearly 10% per decade.

China: Real Growth Rates of GDP and Exports¹⁰

	1970-1980	1980-1990	1990-2000	2000-2006	1980-2006
GDP	6.2	9.3	10.4	9.7 ^b	9.8 ^b
Exports	n.a.	5.7	14.1	23.3 ^c	12.4 ^c

Notes:^b GDP 2006 calculated with the GDP growth rate for 2006.

^c Excluding 2006.

Exports are a major driver of economic growth in China, amounting to 35 per cent of GDP in 2005. This figure relates to exports from Mainland China, excluding exports from Hong Kong.

⁹ Wang Yong, China in the WTO: A Chinese View, How is China assessing its first five years with the WTO, and what does the future hold?

<http://www.chinabusinessreview.com/public/0609/yong.html>

¹⁰ World Bank, World Development Online Indicators, February 2007.

Note, however, that some of Mainland China's exports are shipped through Hong Kong; therefore adding Hong Kong exports to mainland exports would mean double counting.

WTO membership has improved China's export conditions by securing access to foreign markets. It also reinforced international investors' confidence and made China a favourable destination for foreign investment. The country, however, has to respect and implement WTO-consistent institutional arrangements in intellectual property rights, safeguards procedures and standards. This may affect some of its export- and import-competing sectors negatively.¹¹

In the process of economic growth, China underwent stark changes in the structure of the production side of its GDP. Agriculture declined from a 28.4 % share of GDP in 1985 to 13.1 % in 2004.¹² . Industry expanded its share of 43.1 % in GDP in 1985 to 46.2 % in 2004. The share of the service sector increased from 28.5 % in 1985 to 40.7 % in 2004. In terms of employment, agriculture sector declined from 68.7 % of total employment in 1980 to 50 % in 2002, whereas industry sector increased from 18.2 % to 21.4 % and the service sector from 13.1 % to 28.6 % in the same period.¹³

Growth tends to be unbalanced among the regions. High dynamics prevail in the urban centres, especially those of the coastal regions, whereas the west and north are not growing as strongly. There is a stark divide between the urban centres and the countryside as well as between coastal regions and the interior. Regional difference is the key cause of labour migration. The coastal growth areas offer higher wages that attract workers from the interior of the country. It is estimated that the number of rural labour migrants rose to around 60 million in 2000, 94 million in 2002, and 114 million in 2003.¹⁴

¹¹ Horst Siebert, China: Coming to Grips with the New Global Player, *The World Economy*, 2007, doi: 10.1111/j.1467-9701.2007.01037.x , p.896.

¹² World Bank, *China at a Glance, Country Fact Sheet*, Washington, DC. , August 2006

¹³ E.S.Prasad, *China's Growth and Integration into the World Economy: Prospects and Challenges*, IMF Occasional Paper-232, 2004, Washington, DC, p.55.

¹⁴ Huang, P. and S. Zhan, *Internal Migration in China: Linking it to Development*, Regional Conference on Migration and Development in Asia, 14–16 March 2005

http://www.iom.int/chinaconference/.les/documents/bg_papers/China.pdf

2.3. China's attitude toward its WTO commitments

The PRC government is serious about meeting its WTO obligations and has reviewed and revised thousands of laws and regulations to ensure their consistency with WTO rules. Opening its economy to foreign competition by the WTO membership compelled China to change its current commercial laws and practices. Trade disputes would be resolved through the WTO adjudication procedures rather than through bilateral bargaining.

Though there is still a gap between China's current policies and its WTO commitments, its record of WTO implementation has generally been good, as recognized by the WTO itself and most countries. Forty-nine percent of U.S. companies surveyed in 2006 by the U.S.-China Business Council gave China a grade of "excellent" or "good" in the implementation of WTO obligations, while another 38 percent said it has done a "fair" job. 54 percent said their profits from China increased in 2005 and nearly two-fifths said their China operations earned profits higher than their global average.

At the same time, according to a survey by the American Chamber of Commerce in China, most U.S. companies are satisfied with market access in China. In 1999, only 24 percent of respondents said they had successfully entered the PRC market, but in 2005, 72 percent said they had increased the number of their products and services available in China.¹⁵

China's concessions benefited many major U.S. industries. Among those likely to gain the most are farmers, financial companies and high-tech industries. U.S. law and accounting firms are also granted expanded access under the agreement. China's concessions in the financial sector are the most intense because they benefit not only U.S. banks and insurance companies but also other U.S. exporters and investors who will be able to do business more easily than U.S. financial service companies can assist them and their Chinese customers. U.S. firms are also free to distribute their products throughout China without going through a Chinese intermediary. These market-opening concessions phased in over five years to give Chinese firms a chance to adjust to the prospect of foreign competition.

¹⁵ Wang Yong, China in the WTO: A Chinese View, How is China assessing its first five years with the WTO, and what does the future hold?
<http://www.chinabusinessreview.com/public/0609/yong.html>

As the U.S. is a WTO member and granted China MFN before the membership, China's entry imposed few adjustments on the U.S. compared to the intense changes required of China. To calm U.S. firms that face Chinese competition, China has accepted 12-15 years of special protection against any rapid surge in Chinese imports on the presumption that such a surge might result from dumping, which is illegal under WTO rules. A U.S. firm can also gain temporary protection against alleged dumping.¹⁶

Openness to foreign trade and investment favours democratization in the long run because more Chinese will be educated abroad, work with foreigners and gain greater access to sources of information and ideas beyond Chinese government control. China benefits from the creation of jobs, the training of its workers and greater knowledge of international markets.

China's banking sector commitments did not require the government to allow foreign acquisitions of PRC banks. However, U.S. banking industry and the U.S. government are pressing China to go beyond its WTO commitments to allow foreign-majority ownership in banking.

China's banking system is fragile. Asset quality is poor and capitalisation of banks is low. Government intervention in the banking system is massive. Banks are not competitive by international standards.¹⁷ Liquidity of the banking system is high due to monetary policy, banks hold excessive reserves, inter-bank interest rates are low and credits are expanding strongly. Chinese savers seem confident in state-owned banks. If the depositors lost their confidence, a severe risk for a stable growth process in China would arise. Thus it is essential that bank failures leading to a bank run be prevented.¹⁸

As of 2007, China admits foreign banks in accordance with its WTO commitment. In principle, Chinese banks must be competitive by then or at least the majority of them. However, foreign banks are limited in many ways. They are only allowed to open one branch

¹⁶ China in the WTO: The Debate, Volume 4, Number 38, December 1999, Written by James H. Nolt, World Policy Institute, Editors: Tom Barry (IRC) and Martha Honey (IPS)
<http://www.fpi.org/briefs/vol4/v4n38china.html>

¹⁷ For more detailed discussion, See; John Whalley, Liberalization in China's Key Service Sectors Following WTO Accession: Some Scenarios and Issues of Measurement, NBER Working Paper Series, 10143, December 2003, p.10-14.

<http://www.nber.org/papers/w10143>

¹⁸ Horst Siebert, China: Coming to Grips with the New Global Player, The World Economy, 2007, doi: 10.1111/j.1467-9701.2007.01037.x , p.901.

per year. State-owned firms are given preference on credits from state-owned banks, and this implies unproductive use. Even if banks were advised by the central government to learn to make money, the local Party leader is likely to continue to pressure the banker into providing credit to the state-owned enterprises.¹⁹

3. Foreign Direct Investment

Apart from growth in trade, China's WTO entry has sparked a boom in foreign direct investment (FDI). FDIs are the largest drivers and beneficiaries of China's booming exports. According to the PRC Ministry of Commerce, FDIs accounted for more than 60 percent of Chinese exports in 2005.

Before China's accession to WTO, less than 60% of inward FDI went to the manufacturing sector. But after China joined the WTO, more inward FDI went to the manufacturing sector and its share reached over 70% as the share of FDI going to the real estate sector decreased sharply. In agriculture, before China joined the WTO, only 1% of accumulated FDI went to this sector, but in recent years the agricultural share of new FDI increased to 2%.²⁰

China's rich, low-cost labour resource and the vast market provide much scope for profit and make foreign investors more confident in investing in China. By China's WTO entry, the private sector which has been discriminated against for many years, gained rapid growth.²¹

¹⁹ Ibid., p.902.

²⁰ John Whalley, Xian Xin, China's FDI And Non-FDI Economies and The Sustainability of Future High Chinese Growth, NBER Working Paper Series, 12249, May 2006, p.4
<http://www.nber.org/papers/w12249>

²¹ China Daily, November 18, 2002, WTO Entry Boosts China's Economy,
<http://www.china.org.cn/english/49058.htm>

Foreign Direct Investment in China, 2001-2005²²

	2001	2002	2003	2004	2005	% change
Total FDI						
No.of contracts	26,139	34,171	41,081	43,664	44,001	68.3
Amount utilised (\$ billion)	46.9	52.7	53.5	60.6	60.3	28.6
U.S. FDI						
No.of contracts	2,594	3,363	4,060	3,925	3,741	44.2
Amount utilised (\$ billion)	4.9	5.4	4.2	3.9	3.1	-36.7

Source: September-October 2006 chinabusinessreview.com

WTO membership makes China more attractive to foreign investors. More money invested in China means more high-paying jobs, more government tax receipts and more technology transfers. China's WTO commitments facilitate increased competition in every sector of the economy. Competition will foster gains in efficiency and productivity, which will strengthen China's economy over time and enhance the ability of Chinese firms to compete with the best multinationals in any market. In the long-run, increased competition benefit efficient and innovative firms, regardless of whether they are local or foreign, private or public. At the same time increased competition removes inefficient firms and technological laggards

In industries that China's WTO commitments seem to open completely to foreign-invested firms, companies sometimes find that China's laws and regulations meet the technical requirements of its WTO agreement but keep foreign-invested companies at a significant disadvantage to their domestic competitors. For example, foreign companies and trade officials point to China's use of technical standards, food-safety regulations, licensing requirements and professional qualifications among other non-tariff barriers as evidence of China's efforts to limit foreign access to the PRC market.

Although the benefits that foreign firms bring to China in terms of technical and managerial expertise are widely acknowledged, many PRC officials view market openings as one-sided concessions to trading partners and not as mutually beneficial.²³ As in many countries, PRC

²² September-October 2006, chinabusinessreview.com

²³ Michael Overmyer, WTO: Year Five, With China's WTO entry requirements winding down, will 2006 become China's "Year of the Bank"?

<http://www.chinabusinessreview.com/public/0601/overmyer.html>

trade officials also face pressure from domestic companies to limit the market access of foreign competitors which sometimes results in policies that undermine WTO principles.²⁴

4. Assessing the impact of trade and investment on the China Economy

Official PRC media and leaders tend to focus on the positive impact of China's WTO accession and its efforts to open its economy. But some scholars, journalists and other critics within China have more negative assessments of China's trade and investment policies.

4.1. Challenges faced and the outcomes

China's entry into the WTO has not just created winners. Reduced tariffs on agricultural produce have threatened the livelihoods of hundreds of millions of farmers. The modernisation of China's economy and the opening of its markets have brought wealth but at the cost of unemployment for many.²⁵ China's unemployment rate increased substantially during the period of economic restructuring. This experience is typical of transition economies. From January 1996 to September 2002, the unemployment rate of urban permanent residents increased from 6.1 % to 11.1 % and that of all urban residents, including temporary residents increased from 4.0 to 7.3 percent.²⁶

China's total trade volume has surged in recent years and critics say that China's economic growth is overly dependent on foreign trade. The warning is that the ratio of trade to GDP, the foreign trade dependence ratio, is too high. China's dependence on trade reached 80 percent in 2005, higher than many other countries, including the U.S., Japan, and India, according to a study by the Chinese Academy of Social Sciences.²⁷ Those on the other side of the domestic debate have questioned the calculation of the ratio: The size of China's GDP has largely been

²⁴ Washington continues to violate WTO rulings by distributing funds collected through antidumping duties to domestic companies and an EU sugar subsidy was also found to violate WTO rules.

²⁵ Duncan Hewitt, China's unemployment challenge, 19 March 2002

<http://news.bbc.co.uk/2/hi/business/1881153.stm>

²⁶ For more see, John GILES, Albert PARK, Juwei ZHANG, What is China's True Unemployment Rate?, China Economic Review, October 2004 and John Knight, How High Is Urban Unemployment in China?

²⁷ Quoted from "China in the WTO: The Debate, Volume 4, Number 38, December 1999, Written by James H. Nolt, World Policy Institute, Editors: Tom Barry (IRC) and Martha Honey (IPS)"

<http://www.fpif.org/briefs/vol4/v4n38china.html>

underestimated because it has only recently begun to take into account the service sector. Thus, China's dependence on trade is probably smaller than what critics suggest.²⁸

Critics also argue that Chinese companies have not obtained the profits or gained the technologies that they had hoped from the WTO accession. China's industrial policies aimed at strengthening domestic firms are largely useless because WTO rules prohibit restrictions on local content and forced technology transfers. Moreover, the critics claim that foreign investors have given up local partners in existing joint ventures (JVs) in favour of wholly foreign-owned enterprises. Critics worry that multinational corporations are thus tightening control over their technologies to the disadvantage of Chinese domestic enterprises.

Critics cite the auto industry as an example of Chinese companies not benefiting from partnering with foreign investors. For instance, soon after partnering with Nissan Motor Co. Ltd., Dongfeng Motor Corp. increasingly neglected independent R&D as it received product models from foreign partners. This eventually led to the departure of many engineers from Dongfeng.²⁹

Some observers argue that Chinese companies can grow by working with foreign investors, especially by learning how to develop a global sales network. Along with the expansion in market access, the reduction of tariffs and the abolition of non-tariff measures, more foreign products, services and investments entered Chinese markets. However, further opening the market causes some domestic products, enterprises and industries to face more intense competition.³⁰

Many journalists, scholars and officials do not believe that western countries treat Chinese exporters fairly and cite research to support the view that China deserves to have market economy status. The critics argue that it is unfair for the U.S., Japan and E.U. to withhold market economy status from China. On the other side, the U.S. and EU. granted Russia such

²⁸ Wang Yong, China in the WTO: A Chinese View, How is China assessing its first five years with the WTO, and what does the future hold?

<http://www.chinabusinessreview.com/public/0609/yong.html>

²⁹ Ibid.

³⁰ <http://www.wto.org>

status in 2002, even though Russia and China received comparable scores in the 2006 Index of Economic Freedom compiled by the Heritage Foundation and the Wall Street Journal.³¹

Complaints about China's policies are concentrated in several areas. First, many criticize the widespread violations of IPR and the weak enforcement of China's IPR laws and regulations, particularly with respect to movies and software. For example, the Motion Picture Association estimates that 93 percent of films sold in China in 2005 were pirated.³² Recognizing these problems, the PRC government has made great efforts to take measures against IPR violations. China has made progress in educating the general public about the importance of IPR, but it will take more time to promote adequate understanding across China's huge population.

The second area of controversy concerns technical barriers to trade. For example, in 2001 China issued rules on biotechnology safety, testing and labelling that slowed exports of genetically modified crops to China. China has also begun to set standards, some of which differ markedly from those that are widely accepted internationally.

The third controversial issue concerns China's industrial policies, especially subsidies to domestic enterprises. These include different forms of preferential tariff and value-added tax treatments that help reduce the costs of local products competing against imports.

The inflow of international capital has deepened China's integration with the global economy. First, the country has become a major global manufacturing centre. Though consumers around the world benefit from the lower prices of products made in China, the country's rapidly rising exports have become the frequent target of antidumping suits.

In addition, when its foreign exchange reserves hit \$875 billion at the end of March 2006, China surpassed Japan as the world's largest holder of foreign exchange. At the end of 2005, roughly \$257 billion of this foreign exchange was held in U.S. Treasury bills, raising concern in the U.S.³³

³¹ Wang Yong, *Ibid.*

³² *Ibid.*

³³ *Ibid.*

Though China's economic expansion has brought certain pressures to bear on the rest of the world, the Chinese economy, along with the US economy, is one of the world's greatest engines of economic growth.

As new sectors of the Chinese economy are opened, U.S. export opportunities increased work for Americans in industries such as aerospace, chemicals, entertainment, computers, waste treatment, biotechnology, telecommunications equipment, medical equipment and other high-tech products. Some industries such as textiles and clothing that are already losing jobs due to Chinese competition are little affected by this agreement because Washington agreed to no significant new trade concessions. However, there are some losses of U.S. jobs as firms relocate labour-intensive manufacturing from the U.S. to China as conditions there become more favourable to foreign investment.³⁴ On the other side, WTO entry increased competition within China and that led to increased job losses in the short run.

4.2. Economic Forces in China

There are three major economic forces in China.³⁵ Internationalists comprise businesses that are internationally competitive. They are China's exporters and they include most of the firms that receive foreign investment. Internationalists also employ most of the foreign-educated Chinese and they are mostly prominent in light industries such as textiles, clothing, toys, food processing, and other simple consumer products. Internationalists are the main economic force that benefit directly from the WTO agreement, but they constitute only a small fraction of the total economy.

Nationalists are the second major economic force in China. They control businesses that are not efficient enough to compete successfully in international trade but dominate the domestic market. These nationalists are prominent in many heavy industries and in some farm sectors in which China is not a competitive producer. They also include wheat farmers and most of China's leading chemical, petroleum, high-tech electrical machinery, aircraft and automobile producers. Occasionally, some of these large firms try to obtain a foreign partner to inject capital and upgrade their technology to make them more competitive but the political

³⁴ China in the WTO: The Debate, Volume 4, Number 38, December 1999, Written by James H. Nolt, World Policy Institute, Editors: Tom Barry (IRC) and Martha Honey (IPS)

<http://www.fpif.org/briefs/vol4/v4n38china.html>

³⁵ Ibid

complexities of such investments often discourage foreigners. Thus most nationalists could not benefit from Chinese WTO membership.

Localists are China's third major economic force. These are producers who are not only less competitive than the world market standard but also less competitive than the leading national producers within China. They are mostly small-scale producers for local markets. Despite their relative inefficiency, they have helped provide political and economic stability through employment and subsidies. The underdevelopment of China's transportation network has insured that in most parts of China, people buy mostly from local businesses funded by local branches of government banks. However, the recent rapid construction of highways provides an alternative to state-run railroads, bringing in new competition. Because China's tariff cuts increased the competition they face, they viewed WTO membership as a threat.³⁶

5. Boosting consumption by domestic demand

China and the international community have changed significantly as a result of China's WTO entry. The business environment has greatly improved and trade and investment have grown. Foreign businesses are pressing for changes beyond those contained in China's WTO commitments but voices within China are cautioning against further market openings.

WTO accession has accelerated China's economic opening and reform. China's 11th Five-Year Plan (2006-2010) offers a new development strategy focused on technological innovation and growth driven by domestic demand.

To boost consumption, the plan sets out key policies such as improving rural infrastructure and strengthening the economy of the interior. PRC leaders believe that accelerating industrialization and urbanization in the interior will create more domestic demand and thus reduce China's dependence on exports.

Technological innovation strategy includes strengthening local research and development (R&D) capabilities and thus creating more competitive and value-added Chinese companies

³⁶ China in the WTO: The Debate, Volume 4, Number 38, December 1999, Written by James H. Nolt, World Policy Institute, Editors: Tom Barry (IRC) and Martha Honey (IPS)
<http://www.fpif.org/briefs/vol4/v4n38china.html>

and brands. To help domestic firms achieve these goals, the government plans to increase financial and other support for R&D.

Competition among local governments for investment has characterized China's dynamic growth and has intensified since China entered the WTO, especially as the central government has transferred more power to local levels to approve foreign investment in their jurisdictions.

6. Why China needs the WTO

Growth rates averaging nearly 10 percent annually have created a vast array of new job and investment opportunities, making China more prosperous. The effect of China's transformation from a planned economy to a market economy, influencing everything from consumer choice to investment flows.

The concern for China has been and will continue to be, to keep the dual momentum of economic growth and structural reform on best going. In many respects, WTO membership is China's best option for sustaining the pace of economic growth and reform. As the world economy has become more complex and interconnected, China's entry in WTO has become more critical for China, as well as for the U.S., Asia and the world. As a WTO member, China is able to participate in the formulation of rules that govern international trade and investment. WTO membership links China to the global economic community, bringing with it more employment and investment opportunities and greater social stability.

Besides, it is able to defend its trade interests using the WTO dispute-settlement system. Chinese exporters benefit from the certainty that their trading partners must obey WTO rules. Thus, WTO members are not able to discriminate against Chinese products in their home markets.

Perhaps most importantly, consumers and companies benefit from an expanded rule of law as China implements its WTO commitments, particularly those designed to foster the highest degree of transparency and trade-related non-discrimination.

7. Overview: Current Situation

Director-General of the WTO Pascal Lamy told an audience in Shanghai on 6 September 2006, *“Since its accession to the WTO, China has been the fastest growing trading nation in the world. Its trade growth has been faster than that of other developing countries. As a result China is today the world's third largest trading economy, behind the European Union and the United States.”*³⁷

The Chinese government has substantially reduced barriers to imports which today stand among the lowest in developing countries. The average of applied import duties dropped to 9.7% in 2005, down from 15.6% in 2001. In the same year, average applied rates in India, Brazil or Mexico were 20%, 11% and 12% respectively.³⁸

Furthermore, China's ratio of imports to GDP which is a criterion to measure an economy's openness is high. This ratio has moved from 5% in 1978 to 30% in 2005, about twice that in the U.S. and more than 3 times the ratio in Japan. It is also higher than other developing countries such as Argentina, Brazil or India.³⁹

The number of imported goods that has been subject to import licenses or quantitative restrictions has dropped substantially. In the late 1980s, China imposed licensing requirements on almost 50% of all imports. By the time China joined the WTO in 2001, this share dropped to around 4%. In 2005, the government eliminated all licensing requirements.

From 2001 to 2005, China imported goods worth nearly 2.2 trillion USD with an annual growth rate of 28%. Throughout the 1990s China was the fastest growing export market for U.S. companies. This trend accelerated from 2000-2005, as U.S. exports to China rose by 160% while exports to the rest of the world rose only 10%. But China has also become a destination for other developing country exports. China is the world's third largest importer

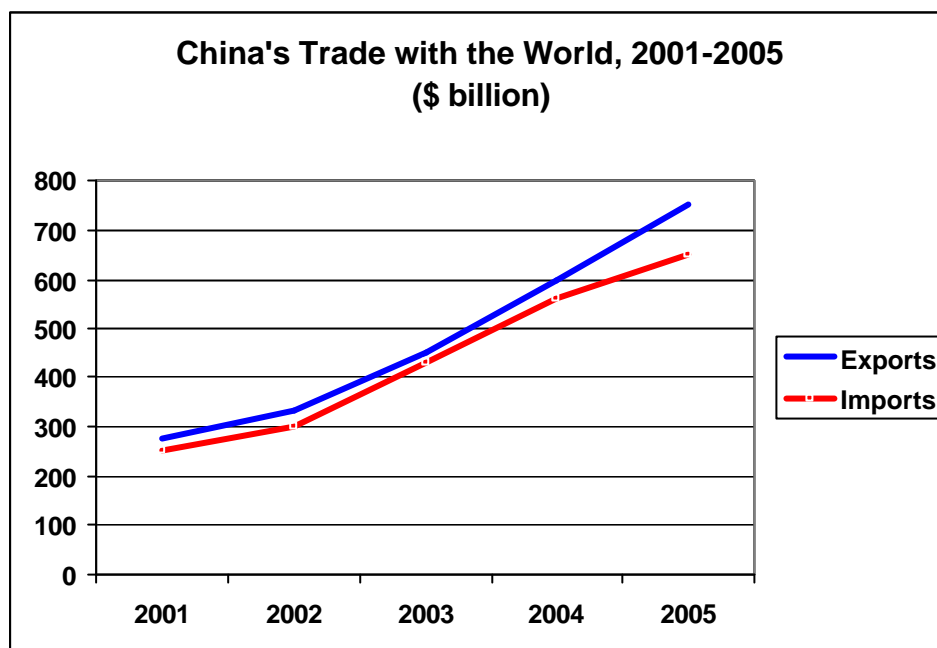
³⁷ “China was strong when it opened to the world”, WTO News: Speeches-DG Pascal Lamy, Shanghai, 6 September 2006

http://www.wto.org/english/news_e/sppl_e/sppl33_e.htm

³⁸ Ibid.

³⁹ Ibid.

from the world poorest countries, after the EU and the U.S., absorbing nearly 40% of their exports.⁴⁰ China's trade in goods has rapidly expanded after the WTO entry.



Source: September-October 2006 chinabusinessreview.com

The United States is China's largest trade partner.

China's Top 10 Trade Partners, 2005

Overall	Imports	Exports
United States	Japan	United States
Japan	South Korea	Hong Kong
Hong Kong	Taiwan	Japan
South Korea	United States	South Korea
Taiwan	Germany	Germany
Germany	Malaysia	The Netherlands
Singapore	Singapore	United Kingdom
Malaysia	Australia	Singapore
Russia	Russia	Taiwan
The Netherlands	Thailand	Russia

Source: September-October 2006 chinabusinessreview.com

⁴⁰ Ibid.

Nearly all of China's top exports and imports have at least doubled since 2001.

China's Top Goods Exports, 2001-2005 (\$ billion)

Commodity	2001	2005	% change
Electrical machinery and equipment	51.3	172.3	235.9
Power generation equipment	33.6	149.7	345.5
Apparel and clothing accessories	32.4	65.9	103.4
Iron and steel	8.2	34.1	315.9
Optical and medical equipment	6.4	25.5	298.4
Furniture and bedding	7.6	22.4	194.7
Toys and games	9.1	19.1	109.9
Inorganic and organic chemicals	7.5	19.1	154.7
Footwear and parts thereof	10.1	19.1	89.1
Plastics and articles thereof	6.7	17.8	165.7

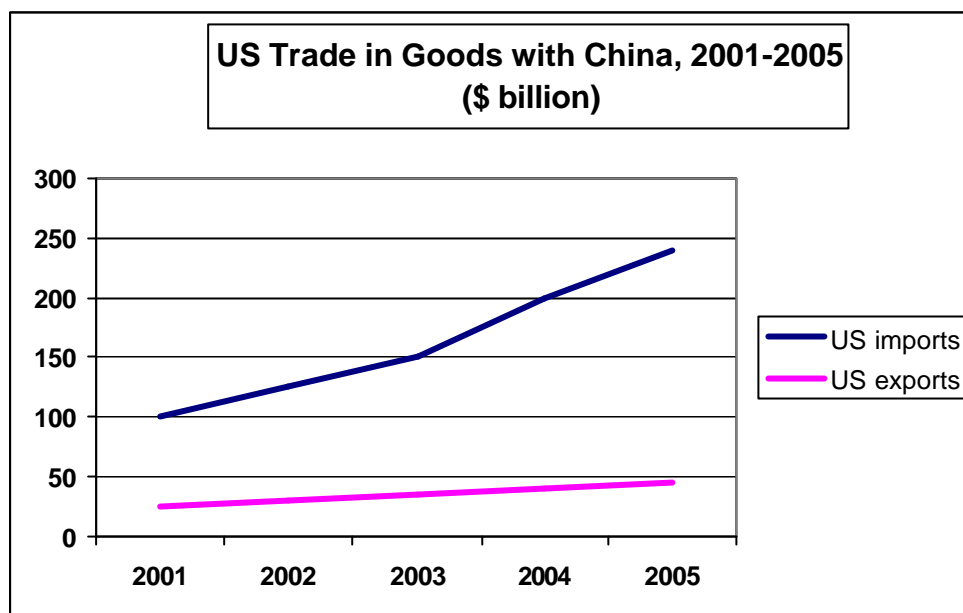
Source: September-October 2006 chinabusinessreview.com

China's Top Goods Imports, 2001-2005 (\$ billion)

Commodity	2001	2005	% change
Electrical machinery and equipment	55.9	174.8	212.7
Power generation equipment	40.6	96.4	137.4
Mineral Fuel and oil	17.5	64.1	266.3
Optical and medical equipment	9.8	50.0	410.2
Plastics and articles thereof	15.3	33.3	117.6
Inorganic and organic chemicals	10.6	32.8	209.4
Iron and steel	13.0	31.9	145.4
Ore, slag and ash	4.2	26.0	519.0
Copper and articles thereof	4.9	12.9	163.3
Vehicles and parts other than rail	4.5	12.3	173.3

Source: September-October 2006 chinabusinessreview.com

U.S. exports and imports with China have both more than doubled since 2001.



Source: September-October 2006 chinabusinessreview.com

Most top U.S. exports to China at least doubled.

U.S. Top Goods Exports to China, 2001-2005 (\$ billion)

Commodity	2001	2005	% change
Electrical machinery and equipment	3.4	6.9	102.9
Power generation equipment	4.1	6.4	56.1
Aircraft, spacecraft and parts	2.4	4.4	83.3
Optical and medical equipment	1.2	2.4	100.0
Oil seeds and oleaginous fruits	1.0	2.3	130.0
Plastics and articles thereof	0.8	2.3	187.5
Inorganic and organic chemicals	0.5	2.0	300.0
Iron and steel	0.5	1.9	280.0
Cotton	0.1	1.4	1,300.0
Pulp and paperboard	0.3	1.0	233.3

Source: September-October 2006 chinabusinessreview.com

China has become a top supplier of consumer goods for U.S.

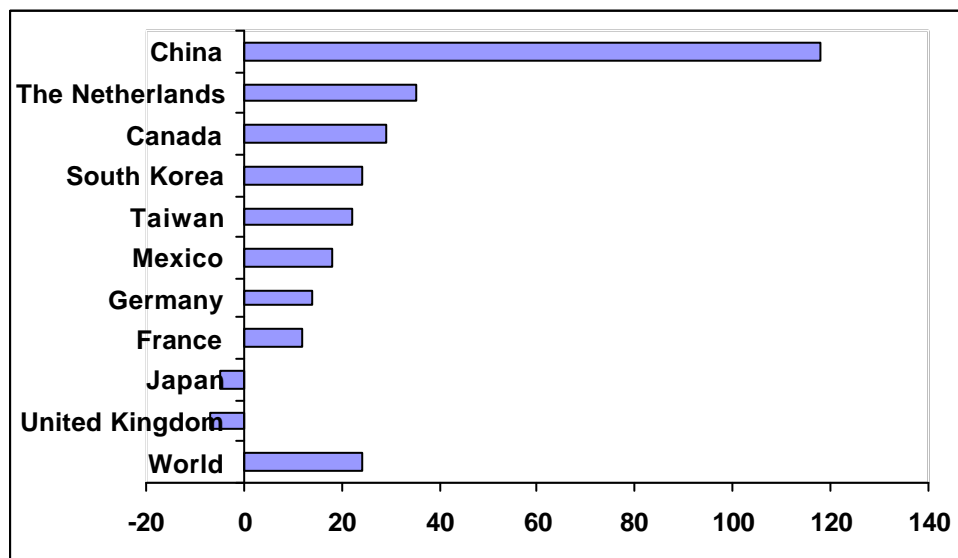
U.S. Top Goods Imports from China, 2001-2005 (\$ billion)

Commodity	2001	2005	% change
Electrical machinery and equipment	19.7	53.1	169.5
Power generation equipment	13.7	52.7	284.7
Toys and games	12.2	19.1	56.6
Furniture and bedding	7.5	17.1	128.0
Apparel and clothing accessories	6.4	16.8	162.5
Footwear and parts thereof	9.8	12.7	29.6
Iron and steel	2.3	7.4	221.7
Plastics and articles thereof	3.2	6.6	106.3
Leather and travel goods	3.9	6.3	61.5
Vehicles and parts other than rail	1.5	4.2	180.0

Source: September-October 2006 chinabusinessreview.com

Meanwhile, China has been the fastest growing major market for the U.S.

US Export Growth to Top Export Markets, 2001-2005



Source: September-October 2006 chinabusinessreview.com

Chinese products that have comparative advantages have been suffering as a result of an increase in anti-dumping allegations and the block of green barriers - import restrictions on the grounds of environmental and food safety.⁴¹

Nearly a fifth of goods made and sold in China have been found to be sub-standard such as canned fruit, dried fish and fruit drinks. China has pledged to take action to improve its food and drug industry after a series of safety scares aroused domestic and global concern.⁴² From pet food to toothpaste, tyres to jewellery and seafood to toys, questions have been raised over the reliability of Chinese-made goods.⁴³

Besides, recently some U.S. firms have recalled Chinese-made toys due to safety risks from magnets and dangerous levels of lead paint.⁴⁴ As it is stated in the media, Beijing had been quick to act after the first recall, revoking the licence to manufacture goods of a firm in Guangdong province. The government recognised that people could lose faith in the “Made in China” label very quickly.⁴⁵

About 85% of the toys produced in China are for export. The U.S. is also China's largest export market. Most of the Chinese toys shipped to the U.S. are for local consumption with a small portion re-exported to Latin America.⁴⁶ China has become toy maker to U.S. and the world since its entry to the WTO in 2001 and promotion to permanent normal trade status with the U.S. in 2002.⁴⁷ Therefore, China has been struggling to convince the world its goods

⁴¹ China Daily, November 18, 2002, WTO Entry Boosts China's Economy,
<http://www.china.org.cn/english/49058.htm>

⁴² Fifth of China goods sub-standard, BBC News, 4 July 2007
<http://news.bbc.co.uk/2/hi/asia-pacific/6269318.stm>

⁴³ Chinese product scares prompt US fears, Laura Smith-Spark, 10 July 2007
BBC News, Washington
<http://news.bbc.co.uk/2/hi/americas/6275758.stm>

⁴⁴ BBC News, New recall of Chinese toys in US, 22 August 2007
<http://news.bbc.co.uk/2/hi/business/6959574.stm>

⁴⁵ Toy woes prompt China checks call, BBC News, 15 August 2007
<http://news.bbc.co.uk/2/hi/business/6947420.stm>

⁴⁶ Toys: Exports to US Enjoy PNTR Status, Issue 11, 2000 (15 November)
<http://www.tdctrade.com/alert/cba-e0011sp6.htm>

⁴⁷ Chinese Toy Terror, Shu-Ching Jean Chen, 02 August 2007
http://www.forbes.com/markets/2007/08/02/mattel-lead-recall-markets-equity-cx_jc_0802markets1.html

are safe after a series of scandals over a string of products.⁴⁸ However, many Chinese toy workers have lost their jobs following Mattel Inc.'s global recall of toys.⁴⁹

The New York Times newspaper reported that a workers' rights group in the U.S. released a report detailing what it called brutal conditions and illegal practices in Chinese toy factories, many of which supply some of the world's biggest brand-name toy makers.⁵⁰ Also, China Labour Watch said that it had investigated eight Chinese factories over the last year and discovered widespread labour violations, including the hiring of under-age workers, mandatory overtime, unsafe working conditions and managers who engaged in verbal abuse and sexual harassment.⁵¹

From the Chinese point of view, recent anti-dumping and anti-subsidy investigations launched by the U.S. against Chinese goods violates rules set by the WTO and show signs of protectionism. The investigations and the measures they might take against Chinese goods will lead to double taxation, which is banned by the WTO. China prefers to resolve issues through consultation and expanded cooperation.⁵²

According to Thurow,⁵³ China decided, "We are the cheapest place to make everything." Foreign firms flooded in, selling equipment to China or making products there and selling them back to the developed world. But there are problems relating intellectual property rights. Chinese companies pirate Western technology and products without punishment and undersell the foreign firms that have invested in them.

Also, Thurow believes that tales of China's phenomenal growth are often just that fictions sold by bureaucrats to rate a promotion. Politicians have an incentive to massage the statistically measured results in their favour. "*China is a great success but it is not growing at*

⁴⁸ Toy official claims Beijing knew of problems, 15 August 2007

<http://www.msnbc.msn.com/id/20275789/>

⁴⁹ China toy group says many workers losing jobs, 17 August 2007

<http://www.msnbc.msn.com/id/20319052/>

⁵⁰ U.S. Group Accuses Chinese Toy Factories of Labor Abuses , David Barboza

Published: August 22, 2007

<http://www.nytimes.com/2007/08/22/business/worldbusiness/22factory.html>

⁵¹ Ibid.

⁵² US Combined Investigations into Chinese Goods Violates WTO Rules, 24 August 2007

<http://english.cri.cn/4026/2007/08/24/1241@265540.htm>

⁵³ Lester Thurow, A Chinese Century? Maybe It's the Next One, New York Times, Published: August 19, 2007

<http://www.nytimes.com/2007/08/19/business/yourmoney/19view.html>

*9 to 10% a year. The G.D.P. in China has been growing somewhere between 4.5 percent to 6 percent a year, not at the 10 percent rate claimed in official statistics. What is clear is that China is unlikely to surpass the United States in GDP in absolute or relative terms anytime soon.*⁵⁴

8. What should be done?

There are several reasons to be optimistic about the future of China's business environment. First, PRC policymakers are sensitive to international pressure and insist that all new policies be consistent with WTO rules. Second, Chinese consumers and businesses have more confidence in the quality of international brands and technologies which will help international exporters and investors maintain their edge over domestic firms for at least the near future. Third, IPR protection will improve as the government and the public both recognize that achieving China's goal of promoting technological innovation requires better IPR enforcement. Fourth, to maintain social and political stability, the country will have to keep attracting foreign capital as labour is still in oversupply and job creation remains a top priority for PRC leaders.

For a country with such a big domestic market and where trade is equivalent to over 60% of GDP, which ranks third in world trade and with the world fastest growth of exports it is easy to understand why trade is so critical for China's growth and development. With China now a major global player, a crisis there would have a severe impact on the Asian countries and on the world economy.

With respect to intellectual property, China accepted the obligation to honour these rights upon its entry into the WTO. Its laws and regulations must be amended to conform to the 'Agreement on Trade-related Aspects of Intellectual Property' (TRIPs). This applies to patents, trademarks and copyrights, including production technologies, fashion and audio and video products. It requires that the Chinese government forcefully combats product piracy.

⁵⁴ For further discussion see, Lester Thurow, A Chinese Century? Maybe It's the Next One, New York Times, Published: August 19, 2007
<http://www.nytimes.com/2007/08/19/business/yourmoney/19view.html>

In the area of IPR protection, important progress made. However, it will take some time to solve and will require the collective efforts of all countries involved. A complete set of laws and regulations are needed in order to meet the world standard of IPR protection. There is the need for additional action for China in other important areas such as industrial policies, trading rights, services, transparency, agriculture and the elimination of government policies that hinder market access for U.S.⁵⁵

As a WTO member, China also has to improve its human right situation, reform its legal system so as to protect contracts and combat corruption and the rule of law should extend to the political and security areas. Divisions between prosperous cities and stagnant rural areas threaten long-term stability in China. Particular attention would be paid to agriculture, rural development and farmers' incomes, balanced regional development, technological innovation, energy conservation and environmental protection.⁵⁶

⁵⁵ See Annual USTR Report to Congress Finds Mixed Record by China in Implementing World Trade Organization Obligations, 12/11/2006
http://www.ustr.gov/Document_Library/Press_Releases/2006/December/Annual_USTR_Report_to_Congress_Finds_Mixed_Record_by_China_in_Implementing_World_Trade_Organization_Obligations.html

⁵⁶ See World Trade Organisation, Trade Policy Review: China, 19- 21 April 2006, Concluding remarks by the Chairperson
http://www.wto.org/english/tratop_e/tpr_e/tp262_crc_e.htm

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