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CHINA'S ACCESSION TO WTO: EXAGGERATED FEARS?

Yuefen Li

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United Nations Conference on Trade and Development

Abstract

The determination of China to accede to the World Trade Organization was driven mostly by its desire to further its economic reform. However, because of the spectacular growth in its international trade in the past two decades, there is the fear that with China's accession to WTO, China would undergo another wave of international trade expansion which might cost job opportunities in both developed and developing worlds. On the other hand, the Chinese are wary of social dislocation to be caused by intensified foreign competition in the post-accession period. A close examination of the structure of China's international trade shows that because of the high import contents of China's exports and the fact that foreign-funded companies account for about half of China's international trade, future growth in China's international trade will benefit to various degrees China's trading partners as well as home countries of transnational corporations. Furthermore, the talk of an imminent export surge from China seems far- fetched, as the conditions of China's accession to WTO as well China's foreign trade potential are unlikely to permit that to take place. On the whole, the challenges posed by China's accession to WTO will, at least in the short run, be greater to China than to its trading partners. However, two decades of fast economic growth and opening-up to the outside world have prepared the country. Therefore, the new set of problems for China is likely to be surmountable.

I. INTRODUCTION

China's accession to the World Trade Organization (WTO) on 11 December 2001 was a monumental event. Never has an accession to the WTO stirred up such intense emotions throughout the world: euphoria, envies, and, above all, fears. Workers on both sides of the Pacific Ocean and beyond have genuine fears of losing their jobs. Governments and entrepreneurs from both developing and developed countries are afraid of a Chinese export surge. Companies in China, on the other hand, are afraid of heightened foreign competition and its resultant factory closures and social sufferings. This is not surprising at all. After all China is the seventh largest trading power in the world, ranking fourth in textile and first in clothing exports. Its foreign trade registered a twelve-fold increase in the past two decades, while China did not have much market access security. However, the economic impact of China's accession has also been blown out of proportion by the attention it has attracted. It has been a major focus of attention for many years, being so politicized that it takes on its own political life with many lobby groups, political supporters and opponents. The issue has been so commercialized that it has become the source of an industry turning out studies, books, reports, experts, consultants, seminars and conferences. When the negotiators were still haggling over the conditions of Chinese accession, which would certainly have great bearing on the magnitude of its economic impact, many books and reports had already been produced and numerous econometric simulations had already been run to estimate the accession-caused job losses and accession-resultant trade expansion. Such analysis which did not take into full consideration the economic realities of the

Chinese foreign trade as well as the legal realities facing China in the WTO framework, contributed to the build-up of emotions.

The economic realities of Chinese foreign trade are that, firstly, Chinese exports, in addition to their reliance on imported technology and equipment, have a high import content of primary and intermediary products. Second, the source of about half of the Chinese merchandise trade is foreign-funded companies. Third, China's foreign trade potential is determined by its economic strength. It is important not to overlook the fact that China is still a developing country with per capita income around US$900. The legal reality is that the WTO is a rule-based trading organization. Members enjoy certain rights yet also have obligations to fulfil. For WTO acceding governments, prior to their accession, they have to conduct bilateral negotiations with WTO members requesting for market access agreements. Then, most of these bilateral deals have to be multilateralized. The overwhelming majority of WTO Members use accession as an opportunity to redress their historical trade complaints against the applicants. When discussing opportunities and challenges of WTO accession for acceding governments, the latest Annual Report by the Director-General of the World Trade Organization[1] pointed out that "Many WTO Members are interested by negotiations with larger potential Members, because they have commercial interests to advance ...". Extracting the best possible terms for domestic interests is the norm for WTO Members in conducting bilateral negotiations. Needless to say, major WTO members are among the first to use their weight to wring concessions from applicants to meet lobby pressure from transnational corporations (TNCs), farmers, politicians and etc. Economies applying to join the WTO, especially large exporters, generally have to pay a high price.

Consideration of both economic and legal realities suggests that the short-to-medium-term prospect of China's post-WTO accession days should look much less dramatic than what it is being painted now. An imminent export surge seems remote. The removal of the uncertainty about China's most-favoured nation (MFN) treatment and the granting of permanent normal trade relations (PNTR) to China does not mean that China can expand its exports to its full capacity. WTO rules and China's accession conditions will not allow this to happen. The assumption of an export explosion could be compared to an analogy of a person who, after taking only one look at a heavy-weight boxer to estimate his size, strength and stamina, estimates the number of people he could knock down, without taking into consideration of the rules of boxing within the boxing ring and the possible rulings of the referee. Even if an export surge were to materialize, it could not happen without an accompanying surge of imports with substantial resulting gains to foreign TNCs. On the other hand, expectations of a gigantic market with 1.3 billion Chinese people also exaggerate the country's import potential.

Another factor leading to the faulty assumptions relating to China's accession to WTO could be traced to data on international trade. The currently prevailing method of collecting and processing of trade data is misleading in various ways, in particular when developing countries and economies are involved. Trade flows in the last part of the 20th century changed tremendously. With greater and faster mobility of capital, goods and information and more open borders, the traditional way of shipping domestic goods from one economy to another is just one of the many modes of international trade. Commercial relations among countries have already entered into a more sophisticated phase owing to the operation of TNCs. In order to maximize profits, TNCs have been searching ways to cut costs (transportation, labor, taxes, tariffs, etc) and jump trading barriers. This has given rise to many new kinds of transaction which have not been correctly or fully reflected in the data on international

[1] WTO, *Overview of Developments in the International Trading Environment,* WT/TPR/OV/7, 10 December 2001.

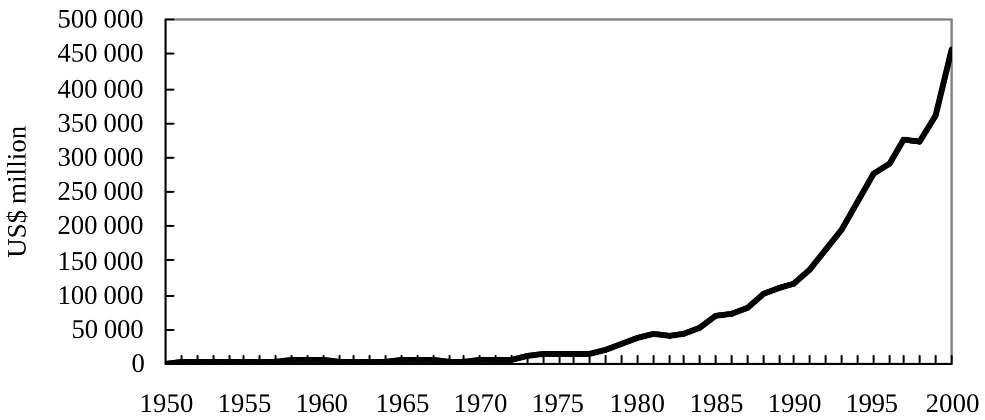
merchandise trade. For instance, TNC affiliate sales in host countries are substitutes of exports, yet they are not captured in the trade data. Production sharing and specialization involves round-tripping, especially for exports from processing zones. Round-tripping exaggerates both import and export values and volumes. When a large amount of international trade is intrafirm trade,[2] failure to take these factors into consideration distorts international trade data, affecting both judgements and policy making at various levels. The outmoded way of compiling data on international trade leads to biases against developing countries, especially those which receive large amount of FDI, but do not yet possess or possess little capacity to set up production facilities and export products in host countries. In some relevant cases, WTO dispute settlements based on data compiled with such methodology could not be said to be very fair.

The first part of this study analyzes the major characteristics of China's foreign trade; the second part looks into Chinese accession conditions which will hinder China from a free expansion of its foreign trade; the third part examines possible impacts of China's accession on its economy.

II. EXPORT PROCESSING ZONE OF THE WORLD

Two figures frequently pop up when people talk about China's foreign trade, i.e. China is the seventh largest exporter and the eighth largest importer in the world.[3] China's foreign trade has indeed grown rapidly in the past two decades. This is largely due to the Chinese policies of opening up its economy and the accelerating pace of globalization.

Figure 1
China's foreign trade, 1950–2000
(Millions of US$)



Source: UNCTAD.
Note: For 2000 imports of China there is a difference respecting to data from WTO. WTO indicates 225 097 billions of US$ while UNCTAD indicates 206 132 billions.

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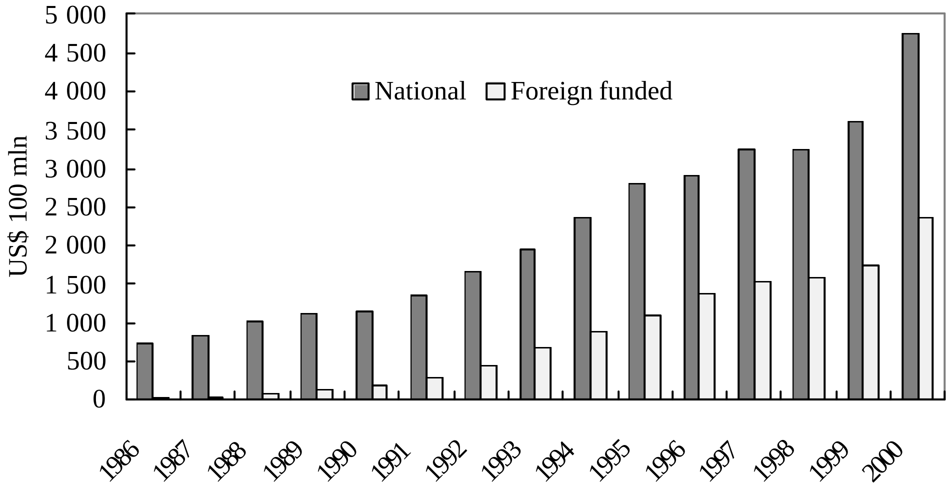
[2] In 1994, intrafirm trade accounted for more than one-third of United States exports of goods and for more than two-fifths of United States imports of goods. (Survey of Current Business, *U.S. Intrafirm Trade in Goods*, by William J. Zeile, February 1997).
[3] Table 1.5 of *International Trade Statistics 2001*, World Trade Organization.

A. Foreign-funded companies[4] account for half of China's merchandise trade

According to data from the Chinese Government, cumulative utilized foreign direct investment in China now amounts to over US$350 billion, almost exclusively in the form of greenfield projects. 400 out of the 500 world largest corporations have invested their money in China. Topping the list are companies from Taiwan Province of China, Hong Kong (China), Japan, Singapore, the United States and Europe. Most of these companies engage in exports. There are many government rules and regulations concerning such matters as export-performance requirements and trade-balancing foreign-exchange requirements. On the other hand, substantial tax and tariff incentives are also a widespread feature of China's foreign trade regime.

Owing to both push and pull factors, China is becoming an attractive export platform for TNCs. Linkages between FDI and trade are substantial in China. The share of foreign trade undertaken by foreign funded companies has been increasing rapidly, amounting to close to half of China's merchandise trade in 2000. Exports by foreign investors have grown from about 2 per cent of the total of Chinese exports in 1986 to about 48 per cent in 2000. Meanwhile, exports by foreign investors have given rise to large imports which have risen about 5.5 per cent of the national total in 1986 to nearly 52 per cent in 1999. Taking out the imports and exports by foreign investors in China, China's foreign trade is on a much smaller scale and the huge trade surplus is also much less impressive.

Figure 2
Foreign-funded and national enterprises in China's foreign trade, 1986–2000



Source: Ministry of Foreign Trade and Economic Cooperation of China.

[4] Foreign-funded companies include equity joint ventures, contractual joint ventures (primarily for low- value-added export processing operations of short duration), wholly foreign-owned enterprises, and joint resource exploration companies (in special extractive industries).

Not all goods produced by foreign-funded companies are exports. To jump trade barriers and thus to enter the Chinese market is also a primary purpose of the country's FDI. Take the United States for an example. "While United States exports to China roughly tripled between 1990 and 1998, affiliate sales soared by more than 21 times over the same period (1998 is last year of available affiliate data). That's from a low base, to be sure – affiliate sales in 1990 totalled just US$639 million. Nevertheless, in 1998, United States exports to China and affiliate sales were roughly equal at US$14.2 billion and US$13.9 billion, respectively".[5] Affiliates sales in China, which are substitutes for exports, nevertheless, were not reflected at all in international trade data. Though lack of data on affiliate sales after 1998 makes it difficult to analyse the trend of the past few years, income from United States FDI in China throws some light on the most recent trends. Income plus reinvested earnings of United States FDI in China increased from US$543 million in 1998 to US$2 billion in 2000.[6] Foreign-funded companies in China also export part of their processed products back to their home countries. "Between 1994 and 1998, exports by United States foreign affiliates in China back to the United States rose more than tenfold (from US$206 million to US$2.1 billion)".[7] This partly reflects the effect of the United States' special tariff provisions which provide duty exemptions for the value of United States exports which has United States inputs. Nevertheless, on the whole, the United States exports more to its foreign affiliates in China than it imports from them. According to Chinese data, about half of Chinese exports to Japan are actually from Japanese-funded companies. For companies funded by Taiwan Province of China, however, not many products processed/produced on the mainland have been sold back to the island province of China. Instead, they go to the United States. The same is true with Hong Kong (China). Of the Chinese exports to the United States, about a quarter is from companies funded by Hong Kong (China) and Taiwan Province. Once again, whether or not international trade data registers this type of exports scientifically is a question. Other destinations of products by foreign firms in China are China's neighbouring countries and other major markets. According to Morgan Stanley, between 1994 and 1998, exports from non-United States foreign affiliates in China to third markets (including the United States) surged by nearly seven times from US$466 million to US$3.2 billion.

China's WTO accession has triggered another wave of FDI into China as major investment opportunities will be available in economic sectors which used to be considered as "pillar industries" and closed to foreign companies. They are mostly lucrative industries like telecommunications, insurance, automobile, etc. China's huge size and abundant supply of cheap labour are also magnets to attract foreign investment. On top of this, the current synchronized global recession exerts additional pressure on companies to cut cost, thus further strengthened the trend of moving into China. Taiwan Province of China, the Republic of Korea as well as Japan are currently undergoing another wave of "hollowing out", as production facilities are being relocated to the mainland. At present, foreign-funded companies from NIEs occupy a third of both exports and imports for the total trade by this kind of companies. It seems that the flying geese model is very much at work in China. The previous wave of the early 1990s increased the presence of newly industrialized economies (NIEs) in China significantly. It is expected that China's WTO accession will give new impetus to regional redistribution of manufacturing capacity in Asia. While NIEs are undergoing further specialization in search of cost saving and better market opportunities, China is at the receiving end of their outsourcing and relocation of the sunset industries as well as some dynamic industries. By doing so, NIEs might have better chances of maintaining reasonable profit margins for their sunset industries, thus

[5] Morgan Stanley 2001, The Latest views of Morgan Stanley Economists, 2 April 2001, *America's Trade Deficit with China – Here to Stay?*
[6] Survey of Current Business, *U.S. Direct Investment Abroad,* Jeffrey H. Lowe, September 2001.
[7] Morgan Stanley Economists, 02 April 2001, *America's Trade Deficit with China – Here to Stay?*

prolonging their life span. On the other hand, China will get employment and tax revenue benefits as well as some value added profit margin. This may also enable China to climb up its own industrialization ladder faster.

This torrent of inflow of capital has turned the Chinese economy into a unique example of globalization. At present, about 10 per cent of the Chinese economy is owned by foreigners. Therefore, one could say that gains of China's accession to WTO will not be enjoyed by China alone, nor will the pain of the post-WTO transition be felt by China itself. The latest trade dispute between China and Japan is a case in point. The restrictions on Chinese exports of vegetables, in particular green onions and mushroom, also hit Japanese firms in China. For instance, KIFA, a Japanese company based in China which exports about 90 per cent of its vegetables back to Japan, suffered tremendously during the Sino-Japanese trade dispute. The rest of the world, especially multinational corporations, will share both the gains and the pain of China's accession.

Table 1

Origin and destination of import and export of foreign-funded companies in China, 1996–2000

	1996		*1997*		*1998*		*1999*		*2000*	
Foreign-funded companies	*US$ million*	*Per cent*	*US$ million*	*Per cent*	*US$ million*	*Per cent*	*US$ million*	*Per cent*	*US$ million*	*Per cent*
IMPORT										
TOTAL	75,603.88	100	77,721.35	100	76,717.49	100	85,883.61	100	117,272.69	100
Including:										
NIEs	27,107.89	36	28,110.74	36	27,652.73	36	29,475.51	34	39,198.76	34
ASEAN[a]	2,981.70	4	3,753.38	5	4,272.71	6	5,172.45	6	8,607.66	7
Japan	19,497.14	26	19,509.06	25	18,774.04	24	21,436.77	25	28,415.89	24
European Union[b]	11,380.85	15	10,615.10	14	11,219.84	15	12,496.66	15	16,623.00	14
United States	7,091.85	9	7,581.64	10	7,713,73	10	8,310.99	10	9,960.08	8
Sub-total		90		90		91		90		88
EXPORT										
TOTAL	61,506.36	100	74,899.86	100	80,961.89	100	88,627.66	100	119,441.21	100
Including:										
NIEs	20,398.29	33	25,026.36	33	24,259.92	30	25,966.52	29	36,004.72	30
ASEAN[a]	1,315.24	2	2,114.24	3	2,044.65	3	2,494.04	3	3,863.87	3
Japan	14,881.83	24	16,008.74	21	15,916.43	20	17,682.00	20	23,340.53	20
European Union[b]	7,030.39	11	9,136.49	12	11,522.51	14	12,660.76	14	17,300.23	14
United States	13,499.19	22	16,874.47	23	20,332.06	25	22,550.07	25	28,798.76	24
Sub-total		93		92		91		92		92

Source: Ministry of Foreign Trade and Economic Cooperation of China.
a Excluding Singapore.
b 15 countries.

B. High import content and worsening terms of trade

According to estimates, over 50 per cent of the total exports from China are processed products. As for foreign-funded companies in China, the importance of processing and final-assembly activities is even more significant. In 1999, about 70 per cent of the trade carried out by foreign-funded companies belonged to the category of processing and assembling. These activities are highly dependent on imports of machinery, equipment, as well as raw and intermediary materials. Out of the imports and exports carried out by foreign companies, the processing of imported materials and components and last-stage assembly occupies a big share. In 1999, for the total processing trade amounting to US$127 billion by foreign-funded companies, US$53 billion worth of material and other inputs were imported, leaving a relatively small margin as valued added for the host country.

Table 2
Export processing by foreign funded companies in China, 1999
(100 million US$)

Foreign-funded companies	*Value*	*Per cent over national total*	*Per cent over previous year*
Total processing value	1272.12	68.95	8.32
Exports	745.39	67.23	7.74
Imports	526.73	71.53	9.15
Including			
Processing of imported materials	1094.44	87.43	4.06
Exports	641.61	85.43	3.56
Imports	452.83	90.42	4.79
Processing of client's imp orted materials	177.68	29.95	44.83
Exports	103.78	29.01	43.68
Imports	73.90	31.37	46.48

Source: China's Customs Authorities.

No official data exist as to how much of these imports and exports were intra-firm trade. According to a survey[8] undertaken by an independent scholar, 30.4 per cent of imports by these companies were intra-firm transactions.

Duty exemptions and reductions have been extended to significant amounts of imports from foreign-funded companies. In special economic zones, foreign enterprises receive total duty exemptions on imports of capital goods and material to be reprocessed in the SEZs. According to China's Customs Authorities, only around 25 per cent of total imports in 1998 entered as ordinary trade, subject to normal customs trade.[9] The remaining 75 per cent, which consisted of primary, intermediate material and other inputs, including capital goods, were mostly imported by foreign-funded companies. Of this total 10 per cent consisted of imports associated with joint ventures' initial investments which entered China duty free. Imports associated with processing trade benefited from a 50 per cent duty exemption.

Being a developing country, China's exports also depend a lot on imports of capital- and technology-intensive goods for the purpose of processing exports. Imports of industrial raw materials have also been increasing fast. For instance, for textile and apparel industries, much of the raw and intermediary material inputs are imported from Taiwan Province of China, Hong Kong (China), the Republic of Korea and the United States. In recent years, terms of trade for many of Chinese manufacture products have been worsening largely because of price increases of the imported goods.

On the whole, the growth dynamics of the exports of foreign-funded companies are stronger than those of domestic companies. They seem to be better able to adapt to the market situation. While for Chinese firms, especially SOEs, exports, particularly of traditional products like textiles, are growing slowly, or not at all.

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[8] A survey undertaken by Long Quoqing.in 2001 and referred to in an UNCTAD Discussion Paper No. 161 "China's terms of trade in manufactures, 1993–2000" by Zheng Zhihai and Zhao Yumin, June 2002.
[9] World Bank, *Assessing the Implications of Merchandise Trade Liberalization in China's Accession to WTO,* Elena Ianchovichina, Will Matin and Emiko Fukase, 23 June 2000.

C. Trade complementarity and trade links with Asian economies

Commercial ties between China and Asian economies have intensified in recent years. Trade volume and value have both been increasing fast. Imports from NIEs, ASEAN and Japan by foreign-funded companies account for around 65 per cent of the total imports of these companies in the years since 1996.

Trade between China and South-East Asia (Indonesia, Malaysia, Philippines and Singapore) more than doubled between 1993 and 2000 reaching US$36 billion. China ran a trade deficit of US$5.9 billion with these countries in 2000. Trade with South Asian countries (India, Pakistan, Bangladesh, Nepal, Sri Lanka, Maldives, Afghanistan and Bhutan) has also been expanding fast. The principal imports into China include iron-ore sand, chromium ore, and leather and textile materials. Sino-Thai trade has also been expanding with China running a trade deficit in the past four years. For some years, China has been importing more from ASEAN countries as a whole than it has been exporting to them. Exports from these countries to China also moved up the value-added ladder. Electronic products and machinery have penetrated Chinese market. With the lowering of tariff rates and the removal of NTB, trade from these countries should be further enhanced.

More than half of China's imports are from newly industrialized economies and Japan. As mentioned before, low production costs have attracted the relocation of less dynamic industries to China. The largest trade deficit of China has been with Taiwan Province of China – more than US$15 billion in 2000. If products sold by Taiwan Province of China enterprises in the mainland were to be included, the figure would be much larger. Japan is China's largest trading partner in Asia. Trade with the Republic of Korea grew fast from very low level in the early 1990s to over US$30 billion in 2000. The Ministry of Finance of the Republic of Korea has forecast that exports to China would increase by up to US$1.5bn every year once trade barriers are reduced or eliminated.[10]

III. LEGAL REALITIES OF CHINA'S ACCESSION TO WTO

The WTO accession obligations are not based on a rule of one size fitting all. As a matter of fact, the hurdle has been raised considerably with the passing of time, especially for those applicants whose economies have potential to develop fast. As a rule of thumb, larger potential Members are forced to accept conditions above the level of existing WTO members. In the latest Annual Report by the Director-General of the World Trade Organization,[11] acknowledgement of this problem was mentioned specifically: "Questions of parity of commitments with existing WTO Members also tend to be present, notably with respect to "developing country status" and market access commitments". Take Taiwan Province of China (named as Chinese Taipei in WTO) for an example. The Oxford Analytical Brief had the following comments: "Taiwan's accession accords are stricter than those of many other WTO members. The island was admitted under the stringent rules applying to developed economies, and the government offered a range of special concessions in areas such as services, agriculture and intellectual property ... Taiwan's 1,500-page admission protocol has shown considerable flexibility in meeting United States demands. In many ways, the final agreement is

[10] Oxford Analytica: South Korea/China: Deepening Ties (A) Nov 20, 2001.

[11] WTO, *Overview of Developments in the International Trading Environment*, WT/TPR/OV/7. 10 December 2001.

shaped by long-standing United States grievances regarding access to Taiwan's markets".[12] Therefore, WTO accession has been used as a way to gain access to the markets of WTO applicants as well as to restrict their exports, especially the most dynamic products – those to the United States being especially important in China's case. Accession is used to, in the words of a former United States Trade Representative, secure "broad-ranging, comprehensive, one-way trade concessions".[13] Most of the members of WTO, in various degrees, have used accession as an opportunity to reduce their market-access difficulties in the applying economies. As stated in the latest Annual Report by the Director-General of the World Trade Organization, "WTO Members are well-placed to ask an applicant to liberalize, …".

In the case of China, they went far in this direction. Market access commitments made by China are sweeping. Tariffs are to be slashed from an average of 15 per cent to 10 per cent upon accession. Non-tariff barriers will be phased out. China's commitments will affect profoundly all protected sectors of economy, including agriculture, service and certain industrial sectors. As some journalists put it, the market opening commitments made by China are not "piecemeal" but "wholesale". On the other hand, the Chinese WTO accession commitments include special clauses which carry the possibility of more frequent and easier utilization of trade defense instruments by members importing Chinese goods. Not understanding fully these special clauses is one reason why people often exaggerate the economic impact of China's WTO accession on the rest of the world.

A. Restrictions on textiles and clothing exports from China

Without looking into China's accession conditions and existing restrictions on Chinese textile exports, many studies have projected that Chinese textile industry will achieve particularly large gains from WTO accession. Some, including Chinese experts, even project that exports could grow by 130 per cent or more within a short period of time. In textile-importing countries, however, so much is the worry about such imports that some people seem to believe that everyone will shortly be wearing shirts made in China. A number of non-governmental organizations have started to line up with textile-importing countries like the United States and European Community and have stepped up their campaign against the phasing out of the Agreement on Textiles and Clothing on the grounds that countries like Bangladesh, Pakistan and Sri Lanka are likely to be hurt by a liberalization which would allow China to achieve greater market shares at the expense of poorer countries.

However, the legal reality is that China's accession conditions would not permit China to benefit from the Agreement on Textiles and Clothing (ATC) to the same extent as other WTO Members.[14] First of all, the transitional special safeguard measures introduced by ATC will be binding for China until 31 December 2008, i.e. four years after its removal for other WTO Members. Secondly, the base for quota expansion for China is much smaller and slower than other WTO Members. For instance, the bilateral textile agreement between the United States and China permits an annual average growth rate of less than 1 per cent, one of the lowest among importing countries. Indeed, because of this low annual permissible growth rate and the low quota bases, some experts in China have even suggested that joining ATC would be detrimental to the Chinese textile and apparel

[12] Oxford Analytica Brief, Taiwan: WTO Benefits, 15 November 2001.
[13] Speech at Economic Strategy Institute Annual Conference, Washington, May 16, 2000, WWW.USTR.gov/
[14] Complaints from importing countries will have to be taken up. Within 30 days of receipt of a WTO Member's request for consultation with China on market disruption complaints, consultations should be held. Meanwhile, China will hold its shipments of the relevant product to a level no greater than 7.5 per cent (6 per cent for wool product categories) above the amount reached during the first 12 months of the most recent 14 months.

exports. On top of this, according to the Report of the Working Party on the Accession of China which has the same legal status as WTO agreements, it is not very clear whether China can receive ATC benefits retroactively from January 1995 when ATC took effect or from the date of Chinese accession to WTO, i.e. December 2001. The wording of the Report is that "To these base levels, the increase in growth rates provided for in Articles 2.13 and 2.14 of the ATC should be applied, as appropriate, from the date of China's accession".[15] During the past seven years of ATC's operation, textile and clothing products were supposed to be progressively integrated into the WTO regime and quotas for the rest of the products were to be increased gradually at specified rates. Though major importing countries have not implemented ATC at the pace indicated by the agreement, there have been some benefits. Under the application of ATC to China, the coverage of its products by quotas is wider and the extent of quota increase will be less than for other WTO members. Under the ATC "growth on growth" provisions, until end-2004, the incremental increase for existing quantitative restrictions maintained by WTO Members on Chinese exports will be no more than 16 per cent, while in the same period other Members will, in principle, enjoy an expansion of a further 25 per cent following the first two stages of implementation of the ATC. These conditions constitute an iron ceiling for Chinese exports and will make the expansion of quotas insignificant for China in some products. In addition, the Chinese utilization of existing quotas is often 100 per cent or close to 100 per cent, while that of countries such as Indonesia, Thailand and Bangladesh has been hovering around 80 per cent. This too limits the potential export expansion for China.

Moreover other WTO Members will be able to expand their exports without the restriction of quotas starting from 1 January 2005 when the ATC is supposed to come to an end, and their trade in textiles and clothing should be fully integrated into WTO's trade liberalization. For China, however, a special transitional safeguard will continue to prohibit China from benefiting from the post-ATC free trading regime in textiles and clothing. The special safeguards will permit importing countries to impose import restraints if market disruption is deemed to be caused by an import surge. Moreover some other countries such as Mexico, Turkey, and some Asian countries will also benefit from the preferential provisions of their respective regional trade agreements.

Restrictions on the expansion of China's textile exports also will come from conditions accepted not connected to ATC. For instance, a number of WTO Members have succeeded in maintaining their prohibitions, quantitative restrictions or other measures inconsistent with the WTO Agreements against textile and clothing imports from China. For example, Argentina, the European Community, Hungary, Poland, Slovakia and Turkey all have signed agreements with China to keep their restrictions till 2005. Anti-dumping practices inconsistent with WTO rules will be maintained by Mexico against China's exports until 2007.

As a result of all these considerations the potential expansion of Chinese textile exports is relatively limited. Domestically, China's textile industry, after years of fast growth, has also been entering a period of less rapid growth which is likely to require structural adjustments. Chinese and foreign manufacturers will need to tailor their investments to realistic forecasts of future market expansion if they are not to be confronted with excess capacity.

At present the United States is the major destination of China's exports. The United States International Trade Commission[16] did a comparison of existing quotas with import levels implied by

[15] World Trade Organization, WT/MIN(01)3, 10 November 2001.

[16] United States International Trade commission, August 1999, *Assessment of the Economic Effects on the United States of China's Accession to the WTO*.

permissible growth rates under the ATC on men's woven shirts from China (a major export item) with those for imports from South Asia, Hong Kong (China) and the Republic of Korea, WTO members designated as small suppliers, and all other affected WTO suppliers. According to these calculations, between 1998 to 2004, permissible Chinese imports would increase by 6 per cent, but those of South Asia (India, Bangladesh, Sri Lanka and Pakistan) would increase by 78 per cent, those of small suppliers like Egypt, Guatemala, Costa Rica, Kenya etc, by 73 per cent; and those of all other suppliers such as Turkey, Indonesia, Malaysia, Philippines, Singapore and Thailand, by 47 per cent. One point worth noting is that this comparison was done on the basis that China could benefit from ATC retroactively from 1995, which means the permissible increases in Chinese could be overestimated. The conclusion of the United States International Trading Commission was none the less as follows: "All these figures demonstrate, during the next five and a half years when quotas are being phased out, China's access to the U.S. market for textiles and apparel will increase only slightly as a result of its WTO accession".[17] Furthermore the National Retail Federation wrote that Chinese WTO accession would not "significantly expand China's access to the U.S. market" or cause "disadvantage to U.S. producers or other foreign suppliers" because China's average quota-weighted base growth rate for apparel is only 1.33 per cent, based on growth rates established in the bilateral agreement in 1997. The Federation concluded that increasing these annual growth rates according to the growth rate provisions of the ATC would result in growth rates that "hardly permit massive increases in United States apparel and textile made-up imports from China".

B. Transitional Product-Specific Safeguard Mechanism[18]

Up to 2013, WTO Members importing Chinese products will be able to use special safeguards to address rapid increases in imports from China that cause or threaten market disruption. Imports could be considered as undergoing rapid increase as measured by volume or value relative to the previous levels, so long as evidence is produced to show "material injury, or threat of material injury to the domestic industry". These specific mechanisms permit importing countries to apply restraints unilaterally based on criteria lower than those stipulated in WTO Safeguards Agreements. Ordinary WTO safeguards apply when imports from all sources "cause or threaten to cause serious injury to the domestic industry that produces like or directly competitive products"[19] but under the transitional product-specific safeguard mechanism importing countries will be able to evoke safeguard measures that target imports from China. Arguably, a decision to resort to trade defense mechanism could be made much more easily when the exports of only one country are affected.

C. Anti-dumping

Up to 2016, a special methodology for a non-market economy relating to price comparability will be used to determine the existence of subsidies and dumping for imports from China. If a WTO Member feels that the importation of a particular product of Chinese origin constitutes dumping, or is taking place at a price "less than its normal value",[20] the importing country has the option of using as a benchmark the price level of a like product from a third which may have higher production costs than those of China. The likelihood of this eventuality is increased by the scarcity of countries with costs of production as low as those in China. Similar rules apply to subsidies. These two provisions could be a major source of litigation. It should also be noted that the accession conditions allow China to request

[17] Ibid pp. 8–18.
[18] These safeguards are additional to those applying to textiles (described above).
[19] Article 2, Agreement on Safeguards.
[20] Terminology used in Agreement on Implementation of Article VI of GATT.

the WTO to review specific sectors or even the Chinese economy as a whole to determine the degree of market orientation and the applicability of the special non-market methodology. But such a review could be expected to be lengthy. Already, anti-dumping charges against China are the highest for any WTO members. According to the latest report from China more than 30 countries have started 477 anti-dumping, anti-subsidy and protective measures investigations against more than 4,000 categories of Chinese products.[21] For exporters experienced in handling trade disputes, such kind of investigations may not lead to loosing of export markets, thus they would not be much negatively affected. Most of the Chinese exporters are lack of knowledge and experience in dealing with anti-dumping investigations. As a matter of fact, many Chinese exporters cannot understand why a third-party production cost level was used and have chosen not to respond to litigation, thus resulting in losing of export markets. According to WTO, China is already having the highest number of affected exporters among WTO Members for anti-dumping investigations.[22]

IV. CHINESE FEARS

More than two decades of reform has led to some remarkable achievements in China, and the country is increasingly deemed as a success story for the entire developing world. However, the easier part of the reform has come to an end and the remaining tasks are daunting. Moreover, Chinese economy has recently been facing deflationary pressure. Postponement of further reform could be costly. With a huge population and low per capita income, China cannot afford a period of low growth. However, the government has found it hard to push through critical measures like SOE and financial reform. Joining the WTO is a massive top-down commitment. The Chinese leadership considers the WTO accession to be a historical necessity to complete the reform of the past two decades. The determination is based on the calculation that WTO accession could serve as an irreversible driving force for the next wave of market reforms, and that China will emerge stronger and more integrated in the world economy. However, as major WTO Members have used the desire of China to join the WTO as a good opportunity "to advance their commercial interest" and to open the Chinese market, it is natural to expect that the Chinese entry into WTO will have much greater impact on China itself than on its trading partners. The social dislocation resulting from WTO accession will be intense and the short-term economic cost caused by foreign competition will be significant. Though it is true that the efficiency gains resulting from trade liberalization will take time to manifest and trade balance will deteriorate, the scenario of a post-WTO China destabilized by a massive increase in imports seems alarmist. Consideration of the economic impact of WTO accession on China should take into account the following circumstances.

- Two decades of economic reform have prepared the country and the population economically and mentally for sweeping market opening. With an across-the-board improvement of living standards, human dislocation should be easier to bear than before. The build-up of foreign exchange reserves, improvements made in institutional and physical infrastructure, etc, will all help to absorb forthcoming shocks. The economic sectors to be affected have mostly already undergone less drastic reforms. Take SOEs as an example. Their importance in the Chinese economy has declined by a wide margin over the years. In the 1990s, they accounted for 55 per cent of the country's

[21] *China Daily* (a Chinese newspaper in the English language) 13 December 2001.
[22] WT/TPR/OV/7, Table AII.4.

gross industrial output but currently, their share is only around 28 per cent. Employment by SOEs has also fallen sharply, from a peak of 112.6 million in 1996 to an estimated 81.2 million 1999. Some of the laid-off workers from SOEs have re-entered the workforce in the private sector.

- To join WTO at a time of synchronized world economic recession has its good and bad side. On the bad side is the effect of low demand in the world on China's exports, though China has not been affected by the current global slowdown as much as some of its Asian neighbours, whose major exports items are IT products. In 2002, with weakening consumer confidence, China's huge exposure to exports of consumer nondurables is likely to be a major weakness. On the good side global deflation is forcing TNCs to shift production to China to benefit from its low labour costs and from the potential of its gigantic internal market. Manufacturing relocation to China is accelerating. On the other hand, the much talked-about foreign competition pressure on SOEs will reduce effective demand as fears about job security will result in increased precautionary saving. This will be reflected in downward pressure on imports.

- FDI will rise not only in manufacturing, but also in newly opened up sectors. To exploit their new opportunities commercial presence will be needed for foreign financial service providers. Though expectations should not be exaggerated, they will create some new employment opportunities and increased local consumption will result.

- Assumptions as to sharply increased imports are based on the magnitude of tariff and non-tariff reductions. But there are offsetting factors. For example, the imports by foreign companies in China already enter with low or zero tariffs as a result of China's preferential treatment to foreign-funded enterprises. With a big share of imports already entering China with tariffs even lower than the average tariff level in the developed countries the "non-pillar" industries, which are not much protected by tariff and NTBs, should not be greatly affected by tariff cuts. Market access and tariff reduction will be mostly felt by automobiles, agriculture, telecommunications and the service sectors. For the rest, the impact will largely come from the removal of non-tariff barriers and special government support such as policy loans. The high costs of economic reform already incurred in these activities were one of the reasons for the government's decision to accede to WTO. Moreover imports will be subject to vigorous competition from domestic producers since the price level in China is low. Generally speaking, except for products protected by the government, other countries will find it difficult to compete with China on price. Should there be a flood of cheap foreign products, like its trading partners China could resort to WTO trade defense instruments such as safeguard measures. Finally the effects in China of the opening-up on WTO accession will be alleviated by the vigorous policy of macroeconomic expansion pursued by the government.

V. CONCLUSIONS

The challenges posed by Chinese accession to WTO will, at least in the short run, be greater to China than for its trading partners. The fears of an imminent surge of exports from China take insufficient account of the legal and economic realities. The high import content of China's exports and the important role played by foreign-funded companies in China's foreign trade mean that increased exports will be associated with corresponding increases in imports and that export restrictions on Chinese exports are difficult to apply without hurting foreign-funded companies. Complying with WTO accession conditions will be a source of difficulties to many Chinese industries, in particular the “pillar” industries, and the social and economic dislocation will be significant. However, two decades of economic reform and opening-up to the outside world have prepared the country for economic shocks. Thus the new set of problems for China are likely to be surmountable.

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