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CHINA'S ACCESSION TO WTO: EXAGGERATED FEARS?

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DISCUSSION PAPERS

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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

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

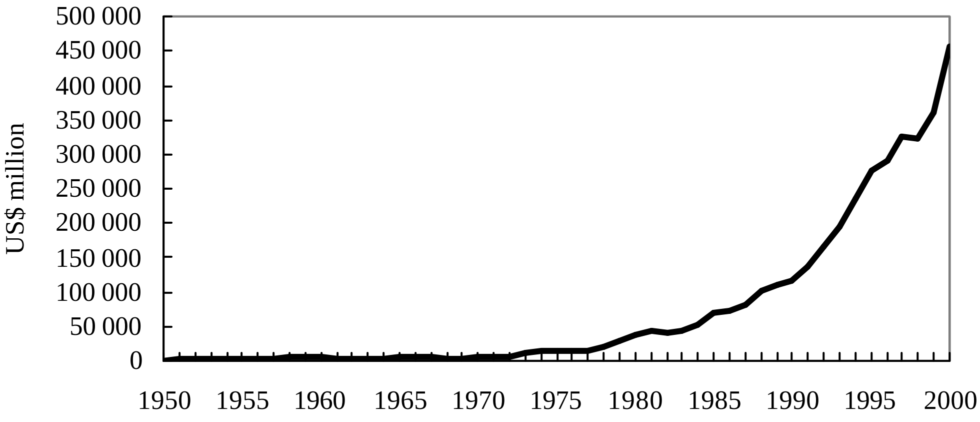
merchandise trade. For instance, TNC affiliate sales in host countries are substitutes of exports, yet they are not captured in the trade data. Production sharing and specialization involves round-tripping, especially for exports from processing zones. Round-tripping exaggerates both import and export 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.

[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