



China's trade policy. The hegemon in waiting

Hanns Günther Hilpert is Deputy Head of the Asia Research Division at the Stiftung Wissenschaft und Politik (German Institute for International and Security Affairs - SWP)

China's epochal economic rise is manifested most of all in international trade. In less than thirty years China has risen from a marginal player to become the largest trading nation in absolute numbers. By 2013 exports and imports totalled \$4,157 billion, corresponding to 11.2 percent of world trade, thereby surpassing the United States and taking the lead in the table of trading nations (see figure). Even as the existing domestic and external economic growth curves level off, it is foreseeable that China will come to dominate international trade in the way the United States did until into the 1970s. It is all too evident that China's secular rise as a leading trading nation has immediate repercussions on the production and income of its trading partners and it has far-reaching consequences for multilateral trade policy.

Given the importance of China's trade policy for the economic wellbeing of its trade partners and for the future of the multilateral trading system, there is still a surprising lack of understanding and interest in the matter. It is true; China's trade policy is still in a transitional mode and has not reached its final shape. It is also true, that the motives and the organizational structure of China's trade policy appears to be somewhat opaque from the outside. But it must be recognized that China plays an ever more important role in shaping international

trade relations and structures since it has entered the WTO in December 2001.

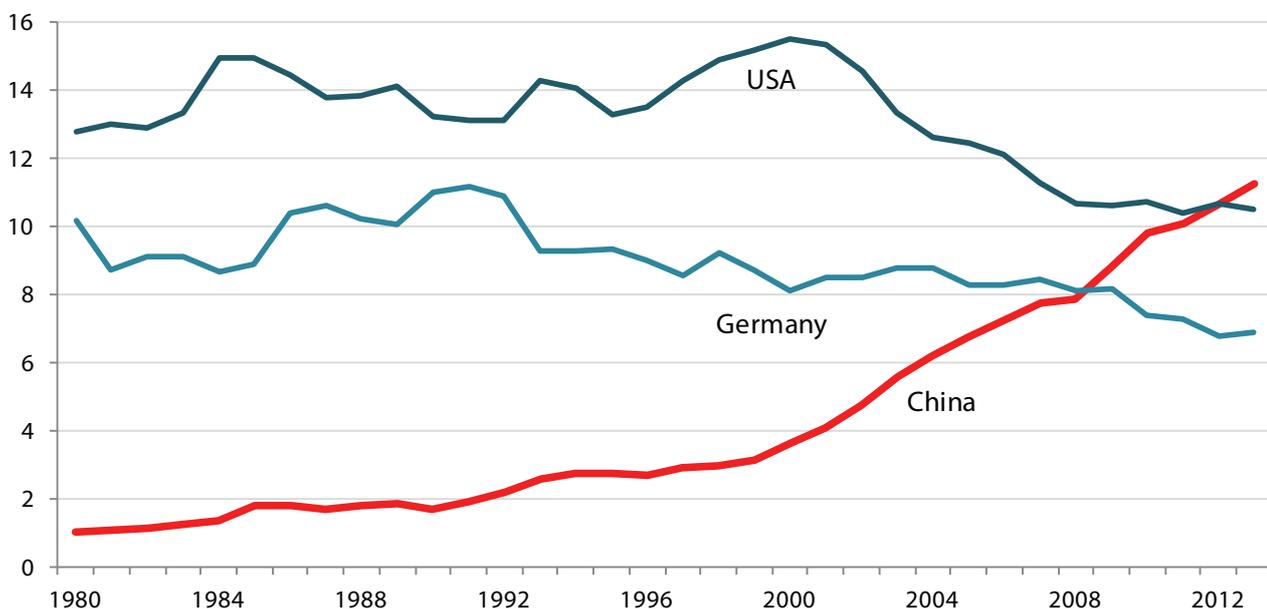
China not only stands at the centre of numerous trade conflicts, it also has a huge impact on the trade policy actions of its trading partners worldwide, even though China does not yet possess the ability or will to lead. Against this backdrop it should be asked: how can China's trade policy be characterized so far? What lessons can be drawn for Europe's trade policy?

Incomplete implementation of WTO accession obligations

Despite far-reaching tariff reductions, market opening and liberalisation, China's implementation of its WTO accession obligations remains incomplete. Yet it is true the country has poured enormous effort into far-reaching adaptations of legislation and jurisdiction to comply with WTO norms and opened its markets considerably wider than other major emerging economies. But deficits persist, in particular in observance of general WTO principles such as non-discrimination, transparency and rule of law.

Towards the middle of the last decade the process of unilateral non-discriminatory liberalisation ended and since then the opening process appears to be going into reverse. Foreign

China's rise to leading trade power: share of world trade (percent)



Source: IMF, Direction of Trade Statistics, May 2014

investors and importers are confronted with new barriers to market entry, while privileged domestic investors are backed and protected with taxes, subsidies and public contracts. Special measures 'behind the border' discriminate effectively against foreign businesses. These include mandatory approval for direct investments, restrictions on company acquisitions, restrictive licensing in the service sector, discrimination against foreign investors through special provisions on establishing a corporation, test procedures, environmental regulations, minimum local content requirements and public procurement, and complex conformity and certification requirements, which are generally also a source of technology leakage.

To further the domestic development of income and employment, the external economic priority of the past Hu Wen administration (2002–2012) lay in protecting the large state-owned enterprises and establishing globally competitive industries. In retrospect it might have been unrealistic to expect that China would abandon industrial policy favouring its domestic enterprise.

Maturing to become an established actor in the WTO-system

Such non-compliance notwithstanding and in spite of the frictions incurred with China's growing presence in world trade, fears expressed before its WTO accession that it would undermine the multilateral system have proved to be unfounded. China behaves like an established actor in the WTO world trade system. It sometimes breaks rules and grants its own trade interests greater importance than the existence and stability of the system as a whole, but in general it respects the status quo and pragmatically pursues its own economic interests. This development is all the more surprising as China - in comparison to the 124 founding WTO-members - had to assume additional obligations on accession, but received fewer rights.

As a non-market-economy, China is specifically disadvantaged by special safeguards permitting its trading partners to impose various import protection measures (until the year 2016). Pointedly formulated, China is still a second-class member. Since China draws great benefits from integration into the world economy, however, anger and criticism from the ongoing discrimination is not targeted at the WTO and the multilateral trading system, but on concrete protectionist measures directed against China.

What is more, China's participation at the WTO dispute settlement mechanism has been taking a decisively positive turn. Both as a defendant and as a complainant, China is participating increasingly actively. Since China correctly implements adverse rulings, the WTO mechanism offers good chances of depoliticising trade conflicts and bringing about legally objective resolutions.

Passivity in the Doha Development Round

China would have little to gain from a successful conclusion of the Doha Development Round, but is, as a trading nation, exceptionally dependent on the world market and has a lot to lose from its failure. China plays an ambivalent role in the current multilateral negotiating process. While it remains reserved and passive in talks, the successful global market campaigns of Chinese industry reduce the willingness of emerging economies to compromise on the issue of market access for industrial products, as market opening would cause them further losses of sales and profits. Thus the failure to date

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of the Doha Round can partly be explained by the failure of the WTO negotiating framework to take adequate consideration of China's new position in world trade.

China's rise has both fundamentally reconfigured the Doha negotiating calculations of many WTO members and it has shifted the power structures of international trade politics. In the face of powerful Chinese import competition, many emerging economies are practically no longer willing to compromise on the topic of non-agricultural market access (NAMA), for example when they were called upon to open their markets beyond the existing reductions in unbound tariffs.

What is more, the rise of China and other major emerging economies has broken up the former GATT negotiating monopoly of the 'Quad' group (Canada, European Union, Japan, United States). Now Brazil, China and India together form an effective opposition and blocking power that can prevent any conclusion it regards as unfavourable – but is itself not yet capable of shaping trade policy.

Active conclusion of bilateral FTA deals

To attain its trade policy goals, such as recognition of market economy status, securing and improving access to markets, resources, technologies, and insuring itself against Western protectionism, China has signed bilateral free trade and economic partnership agreements with fifteen partners to date, entered into negotiations with six further partners, and is considering the start of talks in six more cases.

Bilateralism permits China to play up its status as a major power and indirectly strengthens China's position as the centre of gravity of Asian trade. It is precisely the biggest trading powers that profit most from a shift to bilateralism, because the pull of their import markets lends them asymmetrical negotiating power and puts them in a position to wring concessions from smaller countries. Indirectly, discriminatory bilateral trade policies promote the emergence of centre/periphery structures that favour the businesses and production facilities of the centre.

Thrown on the defensive by mega-regional trade deals

However, at the same time, Beijing is on the back foot in the global trade bilateralism game because the Transatlantic and Trans-Pacific free trade initiatives of the industrialised countries would discriminate against China. Left out from these mega-deals, China would almost inevitably suffer from the creation of trade between their most important trading partners. If China were to seek to join the talks or later join the TPP, it would have to observe the complex, newly-drafted trade rules and accept stringent standards in the fields of social affairs, environmental standards, intellectual property rights and state-owned industries. And it would have to reckon with being confronted

with more or less arbitrary demands from the United States and other TPP members.

In order to remain in the game China will either seek to join the TPP (or even the TTIP) after all, forcing it, as in the case of WTO accession, to accept market opening and domestic liberalisation measures, or it will attempt, via free trade agreements with its Asian neighbours or the BRICS countries, to establish a trading counterweight. However, the latter course will be very difficult to achieve together with trade defensive nations such as Brazil, India, Japan and Russia, and it will be less attractive measured by the growth potential incurring.

Inside China's trade policy: no single unified strategic actor

A closer look at the actors, institutions, interests and debates reveals that the simplistic idea of a monolithic Chinese trade policy cannot be upheld. Any sweeping characterisation of China's trade politics as liberal or mercantilist, as compatible or incompatible with WTO rules, can easily be proven wrong in the complexities of Chinese reality. The different actors' interests and manifold possibilities of action and influence instead demonstrate how contradictory and erratic China's trade policy really is.

Generally, China's trade policy structures can be characterised as pluralistic, untransparent, reactive and unpredictable. As a result of the activities of interest groups and a sometimes nationalistic agenda, economic rationality and actual trade policy sometimes part ways. In general politics follows rather pragmatic, opportunist considerations more than paradigms or strategies. Although China's general political priorities are decisive for the substantive thrust and institutional framework of its trade politics, actual policies are driven more by hard calculation or crude economic interest than by paradigms or grand strategies. Thus China's trade policy is open to external influence, sometimes also to nationalistic instrumentalisation.

Both government actors and regional and sectoral interest groups play a role in shaping the negotiating and implementation processes. It's consequently sometimes less than perfect implementation of binding trade agreements devalues China as a serious negotiating partner. China's trading partners cannot and must not depend on the implementation of contractually promised agreements.

What is more, China's trade policy is in permanent flux. Whereas the influence of the central institutions of government waned under Hu Jintao and Wen Jiabao, the interest groups became ever stronger. The liberal episode under Prime Minister Zhu Rongji with a powerful Ministry of Commerce and efficient negotiating mechanisms is already history. It remains an open

question whether the trend towards state capitalism and protectionism will continue under Xi Jinping and Li Keqiang, or a free-market comeback is possible.

The hegemon in waiting. Towards landmark decisions

China's trade policy is heading for course-setting decisions for at least three reasons. Firstly, a new party leadership took charge in autumn 2012 and a new government in spring 2013. Where once the Hu Wen administration initiated a political shift to state capitalism and mercantilism, the new reform-oriented Xi Li administration can be expected to supply sustainable impetus for domestic and external economic liberalisation. The recent conclusion of free trade agreements with Switzerland, Iceland and Australia, China's interest in a WTO Trade in Services Agreement (TISA) and the opening of movement of capital and financial markets in the new special economic zone in Shanghai can thus be interpreted as the first indications of a more liberal alignment of trade policy.

Secondly, in trade policy China is directly challenged by the bilateralism of the EU, Japan and the US. Successful conclusion of the ongoing talks for Pacific, Atlantic and Japanese-European free trade agreements (TPP, TTIP, JAPEU) would cause China losses of profits and sales through trade diversion and exclude it from the ongoing development of international trade rules.

Thirdly, China has gained enormously in power and influence in international trade policy. While China could initially be 'primus inter pares' in a multipolar trade system, in the medium to long term hegemonic stability is even conceivable, where it would assume leadership and supply resources to support and stabilise the multilateral trading system. In any case, in future China will be in a position to decisively shape international trade policy through its own liberalisation proposals and by placing demands on its trading partners. It is unclear, however, how China's trade policy will respond to the internal and external pressures for realignment.

Despite numerous external economic controversies and conflicts, the European Union should not lose sight of the strategic objective of integrating China in the rule-based world trade system. In view of the growing number of free trade agreements, the West should take seriously the risk of a rift in the global trading economy. It would be both sensible and advisable to integrate China into the ongoing development of international trade rules, ideally by reviving the current Doha Round. Integrating China into TPP and TTIP could be a workable second best alternative. China itself also relies on an open global economy and a functioning WTO for maintaining domestic growth, modernisation and internal stability. There is plenty of room for meaningful negotiation. ■

