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CHINA'S STEEL IMPORTS: AN OUTLINE OF RECENT TRADE BARRIERS

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ABSTRACT.

Since 1993, amounts of iron and steel imported into China have steadily declined. Coincidentally, China's State Council released an administrative circular aimed at controlling steel imports.This paper describes trade barriers applicable to iron and steel imports. These barriers fall under three categories: (1) Tariffs. (2) Licensing and registration. (3) Trading rights and "canalisation". The paper develops a number of hypotheses for further investigation about the impact of barriers on steel imports.

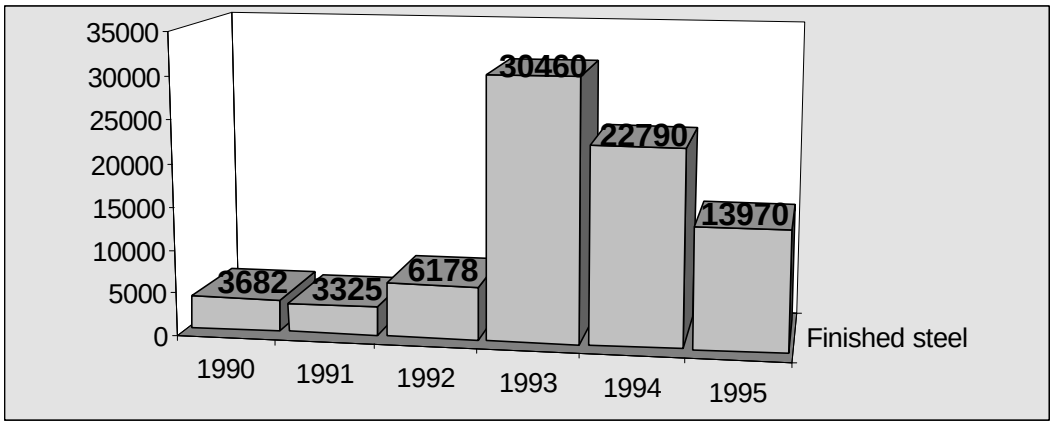
ABBREVIATIONS.

APEC.	Asia Pacific Economic Cooperation (Forum).
DRI.	Direct reduced iron.
EAAU.	East Asia Analytical Unit.
HS.	Harmonised System.
IMF.	International Monetary Fund.
MMI.	Ministry of Metallurgical Industry.
MOFTEC.	Ministry of Foreign Trade and Economic Cooperation.
MOU.	Memorandum of understanding.
NTB.	Non-Tariff Barrier.
RMB.	Renminbi.
VAT.	Value added tax.
WCO.	World Customs Organisation.
WTO.	World Trade Organisation.

INTRODUCTION.

This paper outlines trade barriers applicable to the import of iron and steel products into China. These barriers may explain why quantities of iron and steel imported into China have declined since 1993. As FIGURE 1 shows, during the course of this decade, China's imports of steel have fluctuated dramatically. In 1993, imports of iron and steel increased by nearly 400% over the previous year. In view of the fact that this increase coincided with accumulating stockpiles of domestically produced steel, commentators in Chinese media and industry circles began to suggest that imports were "blind" (*mangmu jinkou*) or "out of control" (*shi kong*).[1] However, in subsequent years, imports fell, so that the 1995 volume was less than half of 1993.

FIGURE 1: *Imports of finished steel. (1,000 tons).*



Sources: Chinese Customs, Ministry of Metallurgical Industry.

The question of why imports have fluctuated in this manner is not examined exhaustively here. It is worth mentioning in passing that probably the most important reason resides with the relative prices of Chinese and foreign steel. However, this paper instead focuses on an alternative explanation, particularly for changes in the period since 1993, namely, new trade policy measures to control steel imports.

[1] For a references to the stockpile situation, see, for example, *Guoji Shangbao* [14 Nov 1994: special "Market" supplement on steel].

Some of these measures were included within a circular issued by State Council on 26 August 1994. Essentially, the circular was a series of edicts from China's highest governing authority. As such, the circular reflected official concern at the high level
of steel imports at that time and the intention to prevent a repeat of the experience.

The State Council circular required that: (1) From 15 September 1994, all prospective imports of steel must be registered with local planning authorities. (2) Enforcement of imports of steel by foreign invested enterprises be improved. (3) Enforcement of imports into special economic zones be improved. (4) Beginning 11 September 1994, tariff and VAT concessions on steel imported through border, barter or donation trade regimes be cancelled. (5) Steel trade be recentralised in the hands of a limited number of state trading enterprises. (6) Customs more thoroughly inspect reported prices and descriptions. (7) Improved monitoring of steel imports be undertaken.

Whilst some of these stipulations in themselves lack detail or enforcement power, they are given greater articulation in the context of China's actual trade rules and regulations. The following aspects of China's import regime for steel products will be outlined in the discussion below: (1) Tariffs. (2) Licensing and registration. (3) Trading rights and canalisation.

1.TARIFFS.

TABLE 1 gives simple average tariff rates for various categories of steel product. Recent adjustments in China's tariff rates have occurred in 1993 and in early 1996 (the latter following President Jiang Zemin's announcements at the Osaka APEC conference of reforms to China's trade system). The pronounced effects of the 1996 tariff reforms are illustrated in TABLE 1. For all steel products, HS categories 72 + 73, tariffs decreased on average by 30% in 1996 over 1995, accounting for the greater part of the decrease in tariffs between 1992 and 1996 (38%).[2]

[2] The Harmonised Commodity Description and Coding System (HS) is a classification system for assessing duties on merchandise imports. The system is managed by the World Customs Organisation (WCO) (formerly the Customs Cooperation Council) and designed for world-wide application. HS tariff numbers have 8 digits. Generally, the first 6 digits are the same for all countries participating in the system. The last two are chosen by individual countries to suit their

The adjustments which occurred in 1993 and 1996 occurred on a permanent basis. In addition to this, there are also so called "provisional" tariff adjustments, made on a temporary basis, extended for one year only. TABLE 1 takes into account provisional adjustments for 1994, 1995 and 1996. Types of steel products to have benefited from lower provisional tariffs include certain types of tubular product, as well as silicon steel sheet, galvanised sheet and tin-plate.[3] Because in some cases 1995 provisional reductions were not extended into 1996, tariff rates increased on average by 31% for steel scrap and by 13% for beams and angles (rows A and F in TABLE 1). This led to small (negligible) increases in simple average tariffs for these two items.

TABLE 1 indicates that iron and steel products which involve relatively greater degrees of processing are subject to higher rates of duty. For example, classifications A to D, which include feedstock for electric-arc furnaces, alloy materials, pig iron, slabs and ingots, enjoy tariff rates of around 1-3%. On the other hand, steel wire (K), processed from wire rods (included at G), is subject to higher tariffs. Likewise, high tariff rates apply to classification L, which includes a wide range of value-added iron and steel manufactures.

However, there are exceptions to this general pattern of tariff escalation. For example, rates are relatively high for bars and rods (G), products which generally involve lesser degrees of processing. Higher rates of protection for these products may not reflect so much the desire to promote more technologically sophisticated, value-added production, but rather, to shield from foreign competition a state-owned industry which is geared towards production of long products.[4] In addition, the provisional tariff reductions mentioned previously for various types of sheet and tubular product also present an exception to the pattern of tariff escalation.

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own purposes. The system is divided into some 97 chapters, indicated by the first two numbers in each 8 digit code. Chapters 72 and 73 are of interest here.

[3] Tinplate is used in the manufacture of cans. China has a growing beverages industry, and its desire to secure supplies of tinplate is also reflected in an export licensing requirement -see TABLE 3.

[4] Note that higher tariff rates for wire would be necessary to maintain effective rates of protection, given that rod is the raw material.

Another interesting comparison can be made with other countries' tariff rates on steel products. The tariff rates shown in TABLE 2 are estimates based on Uruguay Round bindings and commitments.[5] China's tariff rates in 1996 are comparable to the projected rates for Australia and South Korea.

China's system of tariffs is applied inconsistently. Customs duty collected as a percentage of the value of total imports amounted to just 6% in 1992, according to the World Bank [1994: 59]. Effectively, 83% of goods entered completely tariff free. This situation is partly due to tariff treatment for imports under various concessional categories for outward processing, or under border and barter trade regimes. However, these trade regimes do not fully explain the low duty collection ratio, because the value of imports under these categories amounted to half, and not 83%, of the total for 1991. The World Bank indicates that imports for investment projects under China's state plan may help explain part of the remainder [1994: 59]. Smuggling may also play a role, but note that the issue here is why tariff revenues are so low as a percentage of *recorded* import values.

Steel is certainly no exception to the issue of inconsistent tariff application. As noted above, the circular issued by State Council in mid-1994 called for the cancellation of tariff and VAT concessions enjoyed by steel products brought into China under border or barter trade regimes [MMI, Oct 1994: 4]. Newspaper reports suggest a significant proportion of steel was imported through barter trade, donations, or smuggling [*South China Morning Post*, 10 Jan 1995; *China Daily*, 4 Oct 1994].

A consequence of this widespread avoidance of tariffs is that the dramatic decreases in official tariffs for steel undertaken in 1996 were easy for the Chinese government to undertake. There would be minimal revenue pain, because customs was not collecting the full amounts of revenues anyway.

Furthermore, China has been under pressure to make trade concessions in order to further its bid to join the WTO. Tariff reductions may be an easy way of demonstrating the necessary movement, whilst at the same time not jeopardising

[5] In order to arrive these estimates, a straight line reduction is taken between (1) bound tariff rates established during the Uruguay Round (usually September 1986) for negotiating purposes (rates in 1994 should be no higher than these), and (2) the concession rates to be achieved by the end of 1999.

protection for domestic industry, which may rely on non-tariff barriers. The following sections describe NTBs for steel imports.

2.LICENSING & REGISTRATION.

TABLE 3 shows percentages of steel products subject to important developments in the areas of licensing and registration during recent years. One such development was the signing in October 1992 of a Memorandum of Understanding on Market Access between the United States and China. In the MOU, China agreed to a program of trade liberalisation between 1993 and 1997, including the removal of all licensing on steel imports by the end of 1993. Indeed, this step was officially announced by China on 5 January 1994 (See TABLE 3).

Did pre-1994 licensing impose quota limits on steel imports? If imports of steel were centrally planned, then licensing would be a way of coordinating various firms to make imports up to a pre-determined quantity. However, steel has not been subject to compulsory import planning, at least in recent years. In addition, the rapid growth of steel imports in 1993 (FIGURE 1), when licensing was still in place, also suggest the licensing system was not binding.

One interpretation is that licensing for steel was not associated with quotas. Instead, licensing representing a discretionary instrument, under which the constraint on steel imports was kept slack but which could be tightened if necessary. The reluctance of the Chinese government to abandon such insurance mechanisms, despite the MOU with the United States, is illustrated by the introduction in April 1994 of a new scheme, called "automatic registration".[6]

TABLE 3 shows that steel products de-licensed at the beginning of 1994 became subject to the new registration scheme. In fact, the correspondence is exact for HS category 72, strongly suggesting that registration was designed to fill the hole left by the

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[6] The requirement that steel imports be registered was announced by MOFTEC on 26 April 1994, to take effect immediately. However, State Council required in its circular that registration procedures would apply from 15 September 1994. One interpretation of this discrepancy is that there were initial "teething" or enforcement problems in making the registration scheme operational. Note also, imports within contracted amounts for processing with supplied materials (*lialiao jiagong*), compensation trade and by foreign invested enterprises are exempt from registration.

abolition of licensing. In addition, copper, aluminium, paper, fruit, cosmetics and materials for the plastics industry are included on the list of commodities requiring registration, some of which China had earlier agreed in the MOU to de-license.

Under "automatic registration", a party wanting to import steel into China must lodge an application with a local registration authority appointed by the State Planning Commission. Three conditions must be satisfied: (1) The imported steel is required within the jurisdiction of the local registration authority for manufacturing or construction purposes, and represents a "market need". (2) RMB funding for the imports has already been secured. (3) The import agent (a state trading enterprise), the international supplier and domestic end-user all exist and are in positions to sign contracts (in other words, there must be three parties ready to participate in an agreement).[7]

If these conditions are met, registration is "automatically" granted. However, in contrast to the word "automatic", the presence of conditions on registration suggests scope for administrative discretion. For example, who determines whether the imports represent a "market need"?

The requirements on registration may limit the ability to import steel for the purposes of open sale on the Chinese market. The importing party must register in the planning jurisdiction where the steel is to be used. Under the regulations, there are 56 local registration authorities, so that if importers wanted to make steel available nation-wide, they would be expected to register in each and every jurisdiction.

[7] Note that this does not mean foreign supplier and domestic user be ready to sign contracts directly with each other. This is not possible under Chinese law. Rather, the two parties exchange contracts with the import agent. See section 3 (below) on trading rights and canalisation.

Moreover, the ability to resell steel after it has been imported may also be limited by the stipulation that a "user" (*yonghu*) be ready to sign an import contract. Whether "user" can include a wholesaler is a moot point.[8]

The requirement that RMB funding already be secured limits payment terms and conditions to remittance before the imports are received (ie., clean remittance or documentary credit rather than payment after goods are received, since the latter usually takes place when the importer does not have up-front funds). This would serve as an assurance to foreign suppliers, but may also limit their marketing options. As a result, this requirement also has the potential to restrict imports.

The importer who satisfies the conditions on registration is issued with a form in quadruplicate (ie. with carbon copies). One leaf is for presentation to a bank authorised to deal in foreign exchange. Another leaf is for presentation to Customs for release of the goods out of Custom's territory. The other two copies are kept by the applicant and the registration authority respectively.

Ostensibly, the registration scheme was introduced to help China's planning processes, for instance, by providing statistical information on imports.[9] In reality, registration fills the gap left by the removal of licensing.

[8] In 1993, merchants in Guangzhou were criticised for not securing commercial channels for steel before making the imports [MMI, May 1993: 24]. In similar vein, the *China Daily* [1 Dec 1994] reported that "many enterprises have engaged in blind imports by hefting purchasing prices and chopping sales prices at home" (as quoted). These and other anecdotes strongly suggest the conditions on registration are designed to curtail imports for the purposes of market re-sale: an end-user must first be secured. This view dovetails with provisions in the State Council circular aimed at ensuring steel imported by joint ventures, or into special economic zones, is not re-sold on the domestic market.

[9] According to an official from China's General Administration of Customs, China's negotiating partners in the World Trade organisation accession negotiations have asked why Customs statistics are not good enough for this purpose. China's reply has been that the registration scheme provides information before the imports are made, *ex ante* as opposed to *ex post*. China's negotiating partners have also expressed concerns about the responsiveness of local registration authorities appointed by the State Planning Commission.

3.TRADING RIGHTS & CANALISATION.

"Rights" pervade China's commercial environment. Commercial law sets limits on the authority to do business. For example, under China's Economic Contract Law, a contract is not valid if (1) either of the two parties do not have a business licence or (2) the business transacted is not within the "business scope" of either of the two parties. The "business scope" identifies the product or service range that the business is legally entitled to deal in according to its business licence.[10]

The presence of these restrictions is understandable for a country with China's legal and business environment. The restrictions are designed to minimise risks of contract default by preventing unqualified or under-resourced individuals and enterprises from signing contracts which can not be fulfilled. Arguably, the possibilities for such contract disputes are numerous in a country with China's legal and business environment, so the presence of these restrictions is at least understandable (although there is still the question of whether this is the most efficient and logical approach to the problem). Certainly, these kinds of restrictions do represent a restraint on freedom to do business.[11]

These "rights" are duplicated in China's foreign trade regime. Companies wishing to do foreign trade must be granted the right to do so, eg., by MOFTEC. Foreign trade in China is conducted under a regime of state trading.

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[10] China's Economic Contract Law is for domestic purposes only. There is a separate law for international transactions, the Foreign Economic Contract Law.

[11] By way of comparison, under Australian law, limitations on contractual capacity exist only for infants, mentally disturbed or drunken persons, aliens, bankrupts, convicts, spouses (presumed to be "married women"), and corporations. Under Australia's Corporations Law, corporations enjoy the "legal capacity of a natural person" [section 161]. Restrictions on this capacity may be included within the corporation's articles of association [section 162], but note that in contrast to Chinese law, such restrictions are *optional*. Furthermore, in Australia, a contract which contravenes any such restrictions in the corporation's constitution is *not* rendered invalid [section 162 (5)]. The fact that these restrictions were breached may be relied upon when seeking court orders under certain types of litigation specified in [section 162 (7)] of the Corporations Law, but regardless, the contract must still be respected.

State trading enterprises number in the thousands.[12] The types of enterprises allowed to conduct foreign trade has expanded in recent years, with the granting of trading rights to increased numbers of state owned production enterprises, and also to some scientific institutes. There is even consideration of allowing limited foreign participation in trading corporations. As with the business licensing system, state trading enterprises are generally restricted to a "business scope" or "product range".

The most important exception to state trading in China is the fact that foreign invested enterprises are allowed to import inputs needed for production. In the case of steel imports, this is significant. The afore-mentioned State Council circular [MMI, Oct 1994: 4] called for the strict policing of foreign invested enterprises, to ensure imports of steel were only for their own production needs, within contractual amounts, and not for sale on the domestic market.

State trading enterprises undertake imports for other parties on an agency basis. From the perspective of foreign exporters to China, however, the problem is that state trading enterprises generally do not undertake active marketing efforts of their own volition.[13] Typically, state trading enterprises do not act as distributors or take on title to the goods they import. Rather, imports are undertaken on an agency basis. This introduces a schism between import and marketing operations, invariably leading to administrative hurdles and information gaps which increase importation costs. The size of the cost increase varies case by case, highlighting the imponderables of trade impediments of a "deep" as opposed to "shallow" nature.

For many products, a reasonable degree of competition exists between state trading enterprises (their numbers, despite restricted "business scopes", remain large in given

[12] Numbers of enterprises with foreign trade rights (not including foreign invested enterprises) has fluctuated through time. Many trading enterprises were de-registered in the late 1980s, but numbers have since surpassed pre-retrenchment levels:

1978	12 (+ branches)
1986	1200
1988	5000+
1991	3600
1993	5000
1994	7000?

[13] In the words of the US & Foreign Commercial Service, they tend to be "order takers" only.

product categories), which may prevent these enterprises exploiting their market power by charging exorbitant agency fees. However, for other goods regarded as having an important effect on the people's welfare (*guo ji min sheng*), an additional arrangement is imposed which inhibits such competition. This arrangement is known as *canalisation*. Estimates of canalisation coverage ratios for steel products are shown in TABLE 4.

If these estimates in TABLE 4 are correct,[14] semi-processed products such as DRI, ferro-alloys and pig iron are no longer subject to canalisation, but coverage has become more comprehensive for finished steel items (for example, tubes / pipes).

Canalisation is the practice of giving just a few state trading enterprises the right to undertake imports and/or exports of a particular commodity. "Single desk" is the typical example, but in the case of steel there is more than one company involved, as indicated below.

The rules announced by China in 1994 and 1995 identify two classes of trading enterprise given exclusive rights to import iron and steel products. The first type refers to large, national import and export corporations associated with "ministries". In the case of steel, there are three such enterprises:

Zhongguo Wujin Kuangchan Jinchukou Zong Gongsi (Minmetals)
Zhongguo Jixie Shebei Jinchukou Zong Gongsi
Zhongguo Gangtie Gongmao Jituan Gongsi.

The second class of enterprises allowed to undertake steel imports are those associated with "localities". There are 55 companies which are approved to undertake imports to fulfil the needs of 42 particular localities. In many cases (although not exclusively), the state trading enterprises given local import privileges are affiliates of the afore-mentioned national enterprises. For example, two companies are approved to conduct imports into Beijing:

Beijingshi Wujin Kuangchan Jinchukou Gongsi.
Beijing Guoji Maoyi Gongsi.

[14] See notes to TABLE 4.

As another example, one enterprise was approved to import into Guangxi:

Guangxi Wujin Kuangchan Jinchukou Jituan Gongsi.

Likewise, there were two companies for Guangdong, with a separate company serving Guangzhou. A similar situation applies for other provinces and selected cities. These import franchises were awarded by MOFTEC after local foreign trade commissions had recommended a maximum of two local companies for the Ministry's consideration.[15] Only one enterprise was approved in 29 of the total 42 localities, with two enterprises given import rights in each of the remaining 13 localities.

The division of responsibility between "ministerial" and "local" trading enterprises is not completely clear. However, under normal circumstances private individuals, collective or state enterprises seeking to import steel would need to approach a "local" enterprise (depending on the locality involved).[16] Private interests or state owned enterprises may also find it possible to commission national or "ministerial" companies such as Minmetals to undertake imports.[17]

The conditions on the automatic registration scheme (outlined above) enshrine or duplicate this system of canalisation. Imports must be registered locally, and for every locality the number of approved import agents is strictly limited.

Effectively, therefore, MOFTEC limits competition that would otherwise exist between state trading enterprises, by conferring oligopoly or even monopoly positions upon

[15] For some commodities, canalisation is more severe, with no local franchises being awarded. The implementing regulations indicate that imports would be undertaken solely on a national basis by 2 enterprises in the case of wheat, 3 enterprises for crude oil, and 1 for tobacco products [MOFTEC, 22 July 1994]. According to more recent Customs information, however, for cotton, grains and tobacco, there was only one trading company in each instance, but with a larger number for crude oil [Customs, 1995a: 101].

[16] Note that "local" trading enterprises are limited to providing for the locality in which they are registered, and are not supposed to import goods into other regions.

[17] The role of national or "ministerial" enterprises may be restricted to making imports for government purposes only. The canalisation regulations [MOFTEC, 22 June 1995] indicate that "materials supply companies" (*wuzi gongsi*) and "industry and trade companies" (*gongmao gongsi*) are limited to making imports for the government ministries under whose supervision they fall.
Of the three national enterprises mentioned, *Zhongguo Gangtie Gongmao Jituan Gongsi* seems the most likely to be such a company.

designated companies. This leads to the hypothesis that agency fees charged by these companies will reflect the capacity earn economic rents.

Why canalisation? One answer flowing immediately from the previous argument is that canalisation is a deliberate rent redistribution exercise. There is fascination in China with South Korea's *chaebol* and associated trading arms (*chongap sangsa*).[18] The idea is often put forward that China should follow this model and develop similar conglomerate organisations with size and presence on the world stage. Guaranteeing lucrative income streams for certain trading enterprises may be one element in a
strategy to achieve this goal.

Other possible reasons why China chooses to canalise certain products become clear from an examination of TABLE 5. The range of products subject to canalisation in 1992 is listed in TABLE 5 under columns labelled "first and second category imports" (the first category was somewhat more restrictive in terms of the number of enterprises allowed to manage imports). Commodities subject to canalisation as of mid-1994 are shown in the last column. The changes occurring in 1994 represent a consolidation and reform of the system existing in 1992.[19] Based on information contained in TABLE 5, the World Bank outlines another reason for canalisation.

[18] See, for example, articles in *Guoji Shangbao*. (1) A series of three articles entitled *"Hanguo Zongheshangshe de Xingshi yu Fazhan"* [9 - 11 Nov 1994]. (2) *"Hangguo Zongheshangshe de Zhengfu Tuijin Moshi"* [21 Jan 1995]. On this issue, also see World Bank [1994: 210-216].

[19] One reform appears to be de-canalisation of aluminium and copper, but requiring instead that their import be registered. Iron ore, which according to TABLE 5 was subject to import planning, was not been canalised. How this product was handled is unclear.

The World Bank suggests that canalisation could be understood as an administrative mechanism for controlling subsidies associated with imports under the planning system [1994: 82]. From the second column in TABLE 5, all products subject to mandatory import planning were also subject to state fixed pricing (for example, procurement, ex-factory or retail prices). By virtue of state pricing, domestic prices were often below world equivalents. Importing corporations would therefore make a loss and the state would provide a subsidy to cover this. The World Bank believes nearly 18 billion RMB was paid in import subsidies in 1991 [1994: 28], a burden the Chinese government obviously sought to minimise. By designating the right to handle imports to a few select enterprises, it became easier to monitor import quantities and to assess and administer associated subsidies.

Whilst canalisation can be seen in this light, it is hard to see why other instruments, such as quota-licensing, would not do the job just as effectively. In some instances, however, limiting the number of firms allowed to negotiate with international suppliers may increase their bargaining power, allowing them to obtain lower prices and hence reduce the subsidy burden. Certainly, the bargaining power conferred upon Minmetals helps China secure lower prices on steel imports from Japan (see below), although import subsidies are not applicable here. In addition, China may be keen to avoid the appearance of putting explicit limits on imports, a point which will be returned to later.

In any case, as the World Bank points out [1994: 63], the explanation that canalisation is a mechanism for controlling subsidies cannot be extended to all commodities. TABLE 5 shows that not all canalised products were subject to mandatory import planning in 1992, and few, if any, are today.[20] In particular, there was no mandatory planning for iron and steel product imports in recent years, and furthermore, as an inspection of domestic steel prices versus world prices indicates [EAAU, 1995: 32-4], there would be no need for import subsidies anyway. For iron and steel products, then, a different explanation must be sought.

[20] The IMF says that in 1992, import planning covered 11 product groups (about 18% of total imports), whilst in 1993 this had fallen to 5 product groups. The IMF also says that all trade planning was eliminated in 1994 [Tseng *et al*., 1994].

In fact, for iron and steel products, canalisation may be a way of controlling imports in order to protect local industry. For instance, the regulations on canalisation require that designated state trading enterprises participate in the relevant industry Importer's and Exporter's Chamber of Commerce[21], and submit to "coordination and guidance" from that body as to import prices and volumes. In practice, it is open to question whether this requirement imposes sufficient discipline to ensure industry protection.

According to an official at the US Embassy in Beijing in early 1995, the Importers' and Exporters' Chambers of Commerce were not at that time well-resourced or effective institutions, despite the stated intentions of Vice Premier Li Lanqing to make them so [*South China Morning Post*, 11 Nov 1993].

Arguably, the Chambers are more important with regard to export trade than imports, because they have a role in the expanding use of auctions for export quotas, and also in monitoring anti-dumping cases against Chinese products. The function of the Chambers of Commerce was explained by Trade Minister Wu Yi in terms of preventing price-cutting wars by Chinese exporters, which lowered returns to China and increased the risk of
anti-dumping suits [*China Daily*, 10 Aug 1994]. In order to do this, the Chambers established guideline export prices for a series of products.

The role of the Chambers with respect to imports could be seen in a similar light, namely, providing guidance and monitoring on prices and quantities. In practice, participating enterprises may not provide complete information necessary for the Chambers to fulfil their role effectively. Enterprises enjoying healthy profits from importing particular commodities would not be keen to subject themselves to extra scrutiny. In China, as elsewhere, rules which cannot be enforced are often ignored. The requirement, then, that enterprises "cooperate" with the relevant Chamber of Commerce is not likely to hold much weight with pragmatic Chinese managers.

[21] For iron and steel, this requires participation in the steel products branch of the China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters (established in 1988).

Another way in which canalisation aids in the protection of China's iron and steel industry stems from the fact that the implementing regulations put designated trading enterprises under threat of losing import franchises should there be abrupt increases in imports or in the event of "market disruption". In contrast to the former requirement of submitting to "coordination and guidance", this measure is more likely to be effective in controlling the behaviour of designated enterprises, especially if their import monopolies are valuable ones which they would not wish to forfeit.[22]

There is a further degree of canalisation in respect of Japan, the largest steel supplier to China. Up until August 1995 at least, imports of steel were canalised through one firm, Minmetals. Since 1972, Minmetals has held bi-yearly negotiations,[23] to determine prices and volumes, with the 6 Japanese firms. These are Nippon Steel, NKK, Kawasaki Steel, Sumitomo Metal Industries, Kobe Steel and Nisshin Steel Company. Negotiated prices have generally been below Japanese domestic prices, and below those for Japan's other export markets, particularly Southeast Asia.

Press reports say American steel manufacturers have raised "anti-trust" concerns about the trading relationship between Japan and China [*The Daily Yomiuri*, 5 Jan 1995; *Nihon Keizai Shimbun*, 15 Dec 1995]. US steel producers have evidently been eyeing the potential of the China market, and have been identifying barriers to their own success. This would also explain why the 1992 MOU on Market Access negotiated the removal of all steel import licensing, surprising given that steel was not an important part of the US-China trade relationship and that such moves would seem to benefit other countries first. (For a 26 month period, January 1993 to February 1995, US market share of China's steel imports was 2.9%; 1.8% for HS chapter 72; 7.3% for HS chapter 73). Closer consideration suggests that the removal of such impediments may benefit the US relative to other steel producers such as Japan, where special arrangements made licensing barriers less relevant.

[22] Note that in the case of state fixed pricing below world levels, such monopolies would not necessarily be valuable.

[23] However, meetings are apparently held more frequently, eg., to make monthly adjustments.

According to media reports, the Japanese side has become increasingly dissatisfied with canalisation arrangements, and in early 1995 were casting doubt on their commitment to extend the joint negotiations framework beyond August 1995, although there may in fact be some public posturing involved. It would also appear that the system has been "fraying at the edges", that leakages have been occurring from the canalised stream, so that not all steel from Japan goes via Minmetals.[24]

Indeed, there is evidence that the whole canalisation system, at least for steel products, has been "fraying at the edges". [25] The State Council circular issued in August 1994 calls for "renewed approval of enterprises with special rights to import steel" [MMI, Oct 1994: 4]. The circular demands that those state trading enterprises, "who have not been ratified must not engage in the business of importing steel".

Finally, in light of the issues discussed above, it is worthwhile returning to the argument that canalisation confers market power on a select group of enterprises, by drawing attention to some possible qualifications. (1) The oligopoly positions created by canalisation may not be of great value when domestic prices are fixed by the state below world levels. Products for which this is the case would generate losses for the importing corporation. However, during recent years, prices for steel products in China have often been *above* international equivalents [EAAU, 1995: 32-4].

[24] Examples include: (1) When negotiations between Minmetals and the Japanese side became stalled over the issue of prices in 1994, delays in securing supplies ensued. (This was compounded by "no progress in import plans" from other countries including Korea and Brazil). In August 1994, China was forced to allow ad hoc Japanese sales to a Shanghai manufacturer of shipping containers, in order to secure urgently needed hot-rolled strip. It was widely reported this represented "direct" sales, by-passing Minmetals. In fact, Minmetals was the import agent for the Shanghai firm, agreeing to pay the higher prices the Japanese demanded. (2) The *Nikkei Weekly* [5 Aug 1994] reports that Japanese steel traders were receiving orders totalling more than 50,000 tons per month from individual Chinese firms. The difficulty for the 6 large Japanese producers is that although purchase prices for such deals would have been higher than those for the government purchaser, Minmetals, quantities would have been much smaller and subject to greater fluctuation. The combined evidence suggests that under given world market conditions, the threat to abandon the canalisation arrangements adds to Japanese bargaining power. But their interest lies in sticking to the arrangements when world demand is weak. Hence, the public posturing was not necessarily credible.

[25] For example, the *China Daily* has reported that over 3,000 domestic enterprises were able to import steel [4 Oct 1994].

(2) If domestically produced product substitutes are readily available, there may be some competitive pressure on designated trading enterprises to reduce their fees in order to win business. (3) Regulations introduced by the State Price Bureau (*Guojia Wujia Ju*) in 1992 govern fees and commissions which can be charged by state trading enterprises for their import agency services. These regulations may limit the ability of trading enterprises to mark-up prices. (4) Another qualification relates to the special trading relationship with Japan. Minmetals is given a bargaining position specifically in order to secure cheaper imports for China, the logic of which suggests authorities would not tolerate profiteering. (5) In addition, the Importers' and Exporters' Chambers of Commerce are supposed to undertake surveillance, to ensure that quantities remain within acceptable limits, but also over prices. Nonetheless, it would be natural to expect trading enterprises to set fees or prices as high as they possibly can. Information asymmetries (for instance, with regard to reported import costs) may help these enterprises charge higher prices yet evade monitoring. That some state trading houses have profited from monopoly positions is without doubt. Sinochem, with respect to its exports of oil, is an example [World Bank, 1994: 115-6].

CONCLUSIONS.

China's trade system is complicated and its effects are hard to assess. Lack of transparency is partly due to missing information. Whilst rules and regulations are publicly available, it is often hard to determine how one set of regulations interacts with another. Provisions in these regulations are often either vague (maximising discretionary power available to authorities) or obliquely written. For example, the three conditions on automatic registration discussed above seem almost trivial on first inspection, yet a more detailed consideration suggests they are aimed at preventing the market re-sale of imported steel products.

Whilst it is hard due to this complexity to analyse precisely the economic effects of China's trade system, some general conclusions have already been mentioned. These include the fact that canalisation confers import monopolies or oligopolies. Perhaps this is part of a deliberate rent redistribution exercise, spurred on by a desire to foster the development of conglomerate organisations in the fashion of Korean *chaebols*. But there is also evidence to suggest the government saw any such rent effects as undesirable, and sought a mechanism of redress through the requirement that designated trading enterprises submit to "coordination and guidance".

Another conclusion, with respect to iron and steel products in particular (but not necessarily other products), is that the system of protection does not impose binding quantitative constraints.[26] Instead of binding quota constraints, China seems to have designed a system which is discretionary in nature. The government gives itself the administrative leeway to impose control if necessary, for example, where "market disruption" is perceived.[27] The threshold for "disruption" would be anything threatening the viability of domestic iron and steel enterprises, so essentially the motivation is protection of industry.

Protection may be desired for a number of reasons. (1) Very strong national aspirations exist in China for the development of domestic, import substituting industries, iron and steel being no exception. China's steel industry, despite being a behemoth, is still an *infant industry*. (2) More immediately, iron and steel enterprises by and large reflect the difficult situation of state owned enterprises, with ramifications for urban employment and, possibly, social stability. There is an important "vested interest" to look after.[28]

If industry protection is an important motivation, why has a discretionary system

[26] The registration system may impose tacit quota limits (on construction steel, for example), but it is likely that so long as a *user* requires the steel, and no *re-sale* is envisaged, then imports will be permitted. This highlights another feature of China's trade protection system: sometimes it is *purpose*-based rather than *product*-based, a feature which makes it hard to assess trade restrictiveness statistically, since Customs data does not differentiate on this basis.

[27] China's reforms of the foreign exchange retention system in 1994, recentralising foreign exchange supply within approved banks, also provide evidence of the reluctance to dispense with "insurance" mechanisms. In this case, the government may seek to insure against balance of payments difficulties.

[28] For evidence of this point, see *South China Morning Post* article "Foreign imports hit residents in steel city" [10 Jan 1995].

been chosen instead of explicit quota limits? Besides the domestic constituency, China also has to consider foreign trading partners. Pressured by the United States, China has endeavoured to retain administrative control over imports but in a way which conforms with the 1992 MOU.

The bid to join the WTO has if anything heightened the balancing act. Many of the stipulations in the August 1994 State Council circular related to better enforcement of existing measures as opposed to introduction of new barriers, an attempt to use existing resources to better protect local industry without offending foreign partners. Likewise, China has been able to reduce tariffs considerably in order to produce a visible concession, without jeopardising domestic protection.

The argument, then, is that China protects domestic industry, whilst "keeping up appearances" in the international arena. But it should also be noted that much of the above evidence is also consistent with an alternative scenario. Under this alternative scenario: (1) The discretionary nature of trade controls embody a promise to "step in and protect industry if the situation gets bad", but never really acted upon. (2) The gesture of better enforcement is made, but new controls are not introduced. The result would be that China "keeps up the appearance" of protecting domestic industry, whilst at the same time progressing along the path of trade liberalisation. Of course, the issue of which scenario is correct is a matter for further empirical investigation.

Lastly, it would be remiss not to reiterate a point made in the introduction to this paper. The strengthening and reformulation of trade barriers is one candidate explanation for the decline in steel imports after 1993. Whether in fact these barriers are primarily responsible for the reductions in imports does depend on whether relative price movements are also a candidate, because in the final analysis the latter may prove to have stronger explanatory power. This also is a matter for further empirical investigation.

TABLE 1: *Simple average tariff rates.*

Classification	1992	1993	1994	1995	1996	Δ1995-96 [c]	Δ1992-96 [c]
By HS chapter:							
72.Iron and steel	14.1	13.8	13.2	13.1	9.1	-25%	-33%
73.Articles of iron or steel	36.9	32.4	32.2	32.2	16.0	-38%	-44%
72 + 73	23.8	21.6	21.2	21.2	12.0	-30%	-38%
By commodity description:							
A.Direct reduced iron / scrap	3.0	3.0	2.2	2.2	2.8	+31%	-7%
B.Ferro-alloys	6.5	6.1	6.1	6.1	3.5	-41%	-46%
C.Pig iron [a]	8.0	6.3	6.3	6.3	1.4	-64%	-75%
D.Semi-finished steel	5.4	5.4	5.4	5.4	2.7	-49%	-49%
E.Finished steel (F - K below)	16.0	15.3	14.6	14.6	10.6	-21%	-30%
F.Angles / shapes / sections	10.5	10.5	9.3	9.3	9.4	+13%	-9%
Alloy	12.0	12.0	12.0	12.0	8.0	-33%	-33%
Stainless steel	12.0	12.0	12.0	12.0	10.0	-17%	-17%
G.Bars / rods	16.7	16.6	16.6	16.6	12.5	-25%	-25%
Alloy	16.0	15.8	15.8	15.8	9.5	-39%	-40%
Stainless steel	26.3	26.3	26.3	26.3	20.3	-23%	-23%
H.Rails	9.0	9.0	9.0	9.0	9.0	0%	0%
I.Sheets / plates	15.2	14.8	13.8	13.7	9.6	-27%	-36%
Alloy (except below)	12.9	12.4	12.4	12.4	8.6	-30%	-32%
Silicon	15.0	12.0	9.0	6.0	6.0	0%	-60%
Stainless steel	22.0	22.0	22.0	22.0	17.2	-16%	-16%
Tin-plated	15.0	15.0	8.3	8.3	6.7	-21%	-56%
Zinc-plated	14.6	14.6	12.0	12.0	8.8	-22%	-40%
J.Tubes / pipes [b]	14.4	12.3	11.6	11.6	9.7	-14%	-29%
Alloy	13.0	11.8	11.0	11.0	9.8	-11%	-22%
Stainless steel	16.8	14.8	12.4	12.4	10.0	-12%	-42%
Seamless	12.8	12.8	11.6	11.6	10.0	-11%	-22%
Welded	16.6	11.6	11.6	11.6	9.4	-18%	-39%
K.Wire	27.5	26.5	26.5	26.5	16.0	-28%	-29%
Alloy	15.0	15.0	15.0	15.0	12.0	-20%	-20%
Stainless steel	15.0	15.0	15.0	15.0	12.0	-20%	-20%
L.Other	43.8	38.5	38.5	38.5	17.8	-45%	-49%

Sources: Author's calculations from Chinese Customs, MOFTEC.

Notes: [a] Including granules and powders.

[b] Does not include fittings.

[c] *Average change* for tariffs in each classification during indicated period, not change in *average tariffs*. Hence, figures cannot be calculated from first 5 columns.

TABLE 2: *Tariff rates by country.*
By HS chapter. 72: Iron and steel. 73: Articles of iron or steel.

Country	HS chapter	1992	1993	1994	1995	1996	1999
China	72	14.1	13.8	13.2	13.1	9.1	-
	73	36.9	32.4	32.2	32.2	16.0	-
	72 + 73	23.8	21.6	21.2	21.2	12.0	-
Australia	72	-	-	10.2	9.2	8.3	5.5
	73	-	-	18.6	17.1	15.6	11.2
	72 + 73	-	-	13.6	12.5	11.3	7.8
Brazil	72	-	-	43.0	41.3	39.6	34.5
	73	-	-	57.1	52.5	47.8	33.9
	72 + 73	-	-	49.3	46.3	43.3	34.3
EU	72	-	-	4.8	3.9	3.0	0.3
	73	-	-	6.3	5.4	4.5	1.7
	72 + 73	-	-	5.5	4.5	3.6	0.9
Japan	72	-	-	5.2	4.2	3.2	0.3
	73	-	-	5.1	4.2	3.3	0.5
	72 + 73	-	-	5.2	4.2	3.2	0.4
Korea	72	-	-	16.3	13.2	10.1	0.8
	73	-	-	24.3	21.0	17.8	8.1
	72 + 73	-	-	19.7	16.5	13.3	3.9
USA	72	-	-	5.1	4.1	3.2	0.3
	73	-	-	4.3	3.7	3.1	1.2
	72 + 73	-	-	4.7	3.9	3.1	0.7

Sources: Author's calculations from Chinese Customs, MOFTEC.
Notes: See footnote 5.

TABLE 3: *Changes to licensing and registration.*
Percentage of total tariff lines in each classification.

Classification	Total tariff lines in each classification	Import licensing required pre-1994	Import licensing cancelled Jan 1994	Automatic registration required Apr 1994	Export licensing (as of Jan 1996)
By HS chapter:					
72.Iron and steel	199	85%	85%	85%	58%
73.Articles of iron or steel	146	17%	17%	11%	23%
72 + 73	345	57%	57%	54%	43%
By commodity description:					
A.Direct reduced iron / scrap	9	56%	56%	56%	78%
B.Ferro-alloys	16	0%	0%	0%	25%
C.Pig iron [a]	7	0%	0%	0%	57%
D.Semi-finished steel	10	80%	80%	80%	60%
E.Finished steel (F - K below)	191	94%	94%	90%	67%
F.Angles / shapes / sections	14	100%	100%	100%	86%
Alloy	1	100%	100%	100%	0%
Stainless steel	1	100%	100%	100%	0%
G.Bars / rods	32	100%	100%	100%	56%
Alloy	10	100%	100%	100%	0%
Stainless steel	4	100%	100%	100%	0%
H.Rails	1	0%	0%	0%	0%
I.Sheets / plates	95	100%	100%	100%	67%
Alloy (except below)	7	100%	100%	100%	0%
Silicon	6	100%	100%	100%	0%
Stainless steel	18	100%	100%	100%	0%
Tin-plated	3	100%	100%	100%	100%
Zinc-plated	9	100%	100%	100%	78%
J.Tubes / pipes [b]	33	67%	67%	45%	100%
Alloy	8	100%	100%	50%	100%
Stainless steel	5	100%	100%	60%	100%
Seamless	19	74%	74%	37%	100%
Welded	14	57%	57%	57%	100%
K.Wire	16	100%	100%	100%	0%
Alloy	3	100%	100%	100%	0%
Stainless steel	1	100%	100%	100%	0%
L.Other	112	3%	3%	1%	0%

Sources: Author's calculations from MOFTEC, World Bank, US-China MOU.
Notes: [a] Including granules and powders.
[b] Does not include fittings.

TABLE 4: *Canalisation of iron and steel imports.*
Percentage of total tariff lines in each classification.

Classification	Total tariff lines in each classification	Canalisation 1992 [c]	Canalisation July 1994 [c]
By HS chapter:			
72.Iron and steel	199	100%	79%
73.Articles of iron or steel	146	54%	25%
72 + 73	345	81%	56%
By commodity description:			
A.Direct reduced iron / scrap	9	100%	0%
B.Ferro-alloys	16	100%	0%
C.Pig iron [a]	7	100%	0%
D.Semi-finished steel	10	100%	0%
E.Finished steel (F - K below)	191	97%	100%
F.Angles / shapes / sections	14	100%	100%
Alloy	1	100%	100%
Stainless steel	1	100%	100%
G.Bars / rods	32	100%	100%
Alloy	10	100%	100%
Stainless steel	4	100%	100%
H.Rails	1	100%	100%
I.Sheets / plates	95	100%	100%
Alloy (except below)	7	100%	100%
Silicon	6	100%	100%
Stainless steel	18	100%	100%
Tin-plated	3	100%	100%
Zinc-plated	9	100%	100%
J.Tubes / pipes [b]	33	82%	100%
Alloy	8	75%	100%
Stainless steel	5	60%	100%
Seamless	19	68%	100%
Welded	14	100%	100%
K.Wire	16	100%	100%
Alloy	3	100%	100%
Stainless steel	1	100%	100%
L.Other	112	46%	2%

Sources: Author's estimates & calculations from MOFTEC, World Bank.
Notes: [a] Including granules and powders. [b] Does not include fittings.
[c] For 1992, a detailed listing of all HS tariff lines subject to canalisation is available [World Bank, 1994: 277-87]. For 1994, the regulations list "steel, namely plate/sheet, wire rod, structural sections, tube/pipe..." [MOFTEC, 22 July 1994: 6]. In the absence of a more detailed listing,

canalisation is assumed to apply to all finished steel products (F - K) in 1994.

TABLE 5: *Commodities subject to canalisation, 1992 & 1994. By HS chapter.*

Classification	Mandatory import planning 1992	State fixed pricing 1992	1st category imports 1992	2nd category imports 1992	Canal -isation July 1994
10.Cereals	YES	YES	YES	-	YES
11.Milled products	YES	YES	YES	-	-
12.Soya beans	YES	YES	YES	-	-
17.Sugar	-	-	YES	-	-
24.Cigarettes, tobacco	-	tobacco, cigarette paper	YES	-	YES
26.Iron ore	YES	YES	-	-	-
27.Petroleum	-	YES	YES	-	YES
28.Inorganic chemicals	-	YES	-	caustic soda	-
31.Fertilisers	YES	YES	YES	-	YES
38.Herbicides, pesticides	-	YES	YES	-	-
39.Plastics	YES	YES	YES	YES	-
40.Rubber	natural rubber	YES	YES	-	natural rubber
44.Wood	log, veneer	log, plywood, veneer	log, veneer	plywood	log, plywood
47.Wood pulp	YES	YES	-	YES	-
51.Wool	YES	woven, yarn	YES	-	YES
52.Cotton	YES	YES	YES	-	YES
54.Synthetic fibres	-	-	YES	-	-
55.Synthetic fibres	-	-	YES	-	acrylic
72.Iron, steel	-	YES	YES	-	YES
73.Articles iron, steel	-	-	YES	-	YES
74.Copper	YES	YES	-	-	-
76.Aluminium	YES	YES	-	-	-
84.Mechanical machinery	-	-	-	boiler parts, marine engines	-
85.Electrical equipment	-	electric motors, TV receivers	-	cathode ray tubes, TV receivers	-

Sources: Author's tabulation from World Bank, MOFTEC.

APPENDIX.

The following provides a comprehensive listing of tariff classifications used in arriving at "commodity description" entries (rows A - L) in TABLES 1, 3 & 4. These classifications have been chosen to conform, as closely as possible, with aggregates published in the "Major Import Commodities in Quantity and Value" section of *China's Customs Statistics* (see references). Note that HS tariff lines correspond with those in use in July 1995 (in early 1996, WCO member countries re-organised HS tariff schedules). Some alternative classifications not actually used are noted in brackets.

A.Direct reduced iron / scrap:	7203.1000 - 7204.5000.
B.Ferro-alloys:	7202.1100 - 7202.9900.
C.Pig iron:	7201.1000 - 7201.4000, 7205.1000 - 7205.2900.
D.Semi-finished steel:	7206.1000 - 7207.2000, 7218.1000 - 7218.9000, 7224.1000 - 7224.9000.
E.Finished steel:	F - K.
F.Angles / shapes / sections:	7216.1000 - 7216.9000, 7222.4000, 7228.7000, (7301.2000).
F.Of which, alloy:	7228.7000.
F.Of which, stainless steel:	7222.4000.
G.Bars / rods:	7213.1000 - 7215.9000, 7221.0000 - 7222.3000, 7227.1000 - 7228.6000, 7228.8000.
G.Of which, alloy:	7227.1000 - 7228.6000, 7228.8000.
G.Of which, stainless steel:	7221.0000 - 7222.3000.
H.Rails:	7302.1000, (7302.1000 - 7302.9000).
I.Sheets / plates:	7208.1100 - 7212.6000, 7219.1100 - 7220.9000, 7225.1010 - 7226.9900, (7301.1000, 7302.4000).
I.Of which, alloy:	7225.2000 - 7225.5000, 7226.2000 - 7226.9200.
I.Of which, silicon:	7225.1010 - 7225.1090, 7226.1010 - 7226.1090.
I.Of which, stainless steel:	7219.1100 - 7220.9000.
I.Of which, tin-plated:	7210.1100 - 7210.1200, 7212.1000.
I.Of which, zinc-plated (galvanised):	7210.3100 - 7210.4900, 7212.2100 - 7212.3000, 7225.9000, 7226.9900.
J.Tubes / pipes:	7304.1000 - 7306.9000, (7303.0010 - 7303.0090), (7307.1100 - 7307.9900).
J.Of which, alloy:	7304.5110 - 7304.9000, 7306.5000.
J.Of which, stainless steel:	7304.4110 - 7304.4990, 7306.4000.
J.Of which, seamless:	7304.1000 - 7304.9000.
J.Of which, welded:	7305.1100 - 7306.9000.
K.Wire:	7217.1100 - 7217.3900, 7223.0000, 7229.1000 - 7229.9000, (7312.1000 - 7314.5000), (7326.2010 - 7326.9090).
K.Of which, alloy:	7229.1000 - 7229.9000.
K.Of which, stainless steel:	7223.0000.
L.Other:	7301.1000 - 7301.2000, 7302.2000 - 7303.0090, 7307.1100 - 7326.9090, (7205.1000 - 7205.2900).

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