SEMINAR PAPER 97-14

CHINA'S WTO ACCESSION: FINANCIAL SERVICES, INTELLECTUAL PROPERTY, STATE TRADING, AND ANTI-DUMPING

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Australia

November 1997

CIES SEMINAR PAPER 97-14

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ISBN 0 86396 375 7

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Editor's Introduction

Kym Anderson

In late 1995 the University of Adelaide established a Graduate Diploma in International Economics (GDIE) to offer training for trade policy analysts and diplomats interested in furthering their economics skills and their understanding of the global trading system. The papers in this collection were presented as term papers by four groups of students in the 1997 class. All relate to China's attempt to seek membership to the World Trade Organisation.

The first, on "Incentives and Initiatives: China Facing Financial Services Liberalisation" by Chang Chen, Jingxin Huang, Sarinee Kitisatthathik, To Lao and Lei Yuan, makes clear that while China has begun to open up its financial sector and reap rewards from doing so, there are many restrictions still in place. Removing those remaining impediments is bound up with the need to reform the state-owned enterprise system, both of which require attention as China seeks accession to the WTO.

The second paper is on "Intellectual Property Protection in China", by Lin Fu, Cuiping Zhang and Li Zheng. It too demonstrates that China has made great strides since the reforms began in 1978, in this case in strengthening laws to protect intellectual property rights (IPRs) especially of foreigners, but points to the difficulties being encountered in enforcing those laws especially outside the big cities. Given the tension this issue causes in relations between China and the United States in particular, further substantial progress on IPR protection is needed urgently if China wishes to join the WTO.

"State Trading and China's Trade Policy Reforms", by Xiaodong Wang, Jianhua Zhang and Changsheng Zuo, is the topic of the third paper. In it the authors argue that massive progress has been made in transforming China's trade away from being dominated by a few huge state trading enterprises (STEs). A number of strategic commodities remain under strict state control, however. Some of the agricultural ones may well continue to be controlled to some extent after China's WTO accession, since other WTO members also continue to use STEs as part of their tariff rate quota administration to fulfil import market access commitments under the Uruguay Round's Agreement on Agriculture. But other commodities still subject to state trading in China will need to be liberalized in the lead-up to China's WTO accession.

The final paper is on "Anti-Dumping and the WTO: Implications for China", by Yi Dong, Huijun Xu and Fang Liu. Establishing an anti-dumping regime is not a requirement for WTO accession, but neither is it GATT-illegal. In the face of

numerous anti-dumping actions by WTO members against China, it is not surprising the China has responded by establishing its own anti-dumping authority. This paper suggests China should use this new legislation cautiously and sparingly, and it offers administrative suggestions aimed at minimising the risk of economic welfare losses from imposing anti-dumping duties.

Most of the GDIE students this year are trade diplomats from China on AusAID scholarships. They and the University of Adelaide are grateful for that financial support from AusAID.

Incentives and Initiatives: China Facing Financial Services Liberalisation

Chang **Chen**, Jingxin **Huang**, Sarinee **Kitisatthathik**, To **Lao** and Lei **Yuan**

University of Adelaide

Introduction

The financial services sector is acquiring increasing importance in the world economy today. The recognition of its importance is rightfully reflected in the attention given to financial services negotiation under the Uruguay Round's General Agreement on Trade in Services (GATS). Liberalisation in the financial services sector will have profound impacts on economic development of reforming economies and their trading partners. However, given the broad implications of the sector for each national economy, the liberalisation process will not be straightforward. Greater commitments should be made by countries wishing to derive benefits from more-liberal policies in this field, especially transitional economies such as China.

Financial services liberalisation and GATS

By definition, financial services cover a broad range of transactions and are closely related with other economic activities. Under the GATS, financial services include all insurance and insurance-related services, and all banking and other financial services. Activities like deposit-taking and lending, commercial insurance, life insurance, funds management, securities trading and relevant advisory services all fall within the scope of financial services (Goode 1997). The financial services sector knits together the crucial economic establishments—the banking system, the foreign exchange market, the stock market and the real estate market—and provides the wheels for the running of economic vehicles.

The financial services sector is currently experiencing unprecedented development and has attracted great attention in both developed and developing economies. The evidence of the expansion of the sector is more than obvious. According to the figures from IMF, the Bank for International Settlements and the European Commission, the financial services sector is estimated to involve US$1.2 trillion per day in foreign exchange transactions. International financing extended by banks around the world is estimated at US$6.4 trillion. Total world banking assets are put at more than US$20 trillion, insurance premiums at US$2 trillion, stock market capitalisation at over US$10 trillion and market value of listed bonds at around US$10 trillion.

The development of the financial services sector is clear from both the supply side and the demand side. On the supply side, the development of communication and computing technologies has enabled the financial services to become more efficient and less costly. The enrichment of financial instruments during the past few decades has provided customers with more alternatives combined with higher quality services for various trading and investing purposes. On the demand side, the growing integration of national economies is playing a major role. With cross-border flows of trade, investment and financial capital increase there comes a rising demand for matching financial services to facilitate the process. The provision of financial services such as financial intermediations and risk managements in terms of credit, capital, foreign exchange and insurance form the prerequisites for the healthy flows of international transactions (Kono et al. 1997).

Additionally, the rapid economic development in regions such as East Asia opens new markets where the need for financial services increases dramatically in a bid to sustain the robust growth. As the global economy keeps growing, new opportunities of international trade and investment will rise in a significant scale, demanding greater supply of efficient financial services to lower costs and diversify the risks. However, institutional developments in the financial services sectors are unbalanced across countries. Inefficient and unstable financial systems hinder the growth of national economies and can have negative contagious effects on the world economy.

To improve the situation, an important strategy involves liberalisation of the financial sector. In this regard, GATS provides a useful basic framework for multilateral negotiations on trade in services, including trade in financial services. The current negotiation in this area is part of the GATS on-going work program and is also aimed at building on the positive WTO's 1995 Financial Services Interim Agreement in which the liberalisation process involves market access commitments to allow more foreign financial services providers into domestic markets, increased foreign equity participation levels, and reduced restrictions on operations of foreign providers.

The increasing level of deregulation and liberalisation of the sector reflects an attempt to fully reap the benefits of liberalised financial trade. First, financial liberalisation will greatly facilitate further growth in merchandise trade which heavily depends on the efficiency of financial services in terms of credit, capital, foreign exchange and insurance. Second, the growth-stimulating effect of liberalisation is likely to be largest in developing countries with less sophisticated financial systems (Kono et al. 1997). These countries need capital and financial infrastructure for their development. International trade in financial services can facilitate the inflow of capital into these countries and transfer services skills and expertise from foreign services providers. Emerging markets will also grow as more foreign capital is attracted to these markets. Third, financial liberalisation will result in more consumer options and consumers can choose from a wider range of available services to best suit their financing and insurance needs at reduced costs. Fourth, liberalisation will encourage competition and

increase efficiency. Competition from foreign companies will force domestic companies to reduce their costs and improve their management and ultimately pass on the cost-savings to consumers (Kono et al. 1997). With increased competition, consumers will get higher-quality services from financial institutions as they vie for customers in terms of both price and service. Finally, liberalisation in the financial sector will put pressure on governments to pursue prudent monetary, fiscal and exchange rate policies and eliminate distortionary interventions and introduce adequate prudential regulation and supervision of the financial sector.

The experience of East Asia suggests that the limited openness to date has been related to the high cost in terms of slower institutional development in countries such as Vietnam and China, and there seems to be a clear negative relationship between services and barriers (Claessens and Glaessner 1997). In recent years, some East Asian countries such as Singapore and Korea have been rapidly deregulating their financial systems. Financial deregulation is an integral part of financial service liberalisation in East Asia. In line with the global liberalisation trend, some countries in the East Asian region have made significant liberalisation commitments in the Interim Agreement as well as in the Manila Action Plan of APEC. Most of the countries in this region undertook measures to liberalise interest rates, reduce controls on credit, enhance competition and efficiency in the financial system (Tseng and Corker 1991). Judged by right of establishment and ownership and limits on business activity of foreign banks, Hong Kong is the region with the most open banking, security and insurance system in East Asia. Compared with some East Asian countries at a similar level of economic development, China still lags far behind in liberalising its domestic financial market. The experience of these countries can serve as a useful example for China's future efforts in this direction.

Liberalisation of China's financial sector

In China, the financial sector has long been viewed as the main vehicle for carrying out state interventionist policies, which is hardly surprising when one realises that China is still undergoing the process of transforming from a planned economy towards a market-oriented one. The state banks, state-owned enterprises and powerful state agencies still constitute the main framework of the economy. Directed credit has remained the dominant allocation tool because of the continued reliance on the credit plan. The commercialisation in the banking system was basically incomplete, lacking matching reforms in the industrial sectors, where the problem of State-Owned Enterprises (SOEs) is mounting to a menacing degree. In a sense, the SOEs prevented more profit-induced competitions among economic entities from emerging and greatly deterred the process of liberalisation in China's financial sector.

Although little liberalisation of China's financial sector has occurred so far, some initiatives have been taken. However, the impediments should be examined as the aggregate benefit promised by liberalisation would likely outweigh the aggregate cost

when the competitive mechanism introduced brings down the de facto state monopoly, offering a healthy market-oriented structure, and the supply of quality financial services eases the bottleneck and serves as a lubricant for the economic engine. Consider the main financial industries in turn.

Banking

Foreign participation in Chinese banking business has been substantial since the financial sector started opening up more than a decade ago. Initial market access was granted by licensing foreign banks to run representative offices in China after the Beijing government issued regulations in 1980. This made it possible for the prospective foreign participants to collect relevant information, perform credit analysis and promote banking services in China (Mehran 1996).

In 1985, foreign banks were for the first time allowed to set up their branches in five Special Economic Zones. By the end of 1995, 120 foreign branches had established in 13 designated cities (Lees and Liaw 1996). These foreign bank branches were are allowed to engage in deposit taking, loan making, trade service, and security underwriting. Other norms of foreign participation in China's banking sector include the establishment of joint venture banks and solely-funded overseas investment banks. There were 4 foreign funding banks and 5 joint venture banks established in China at the beginning of 1996 (Chen 1996).

However, as we mentioned above, all the banking businesses for the foreign participants are extensively restricted, both in breadth and in depth. Regarding the initial establishment, the thresholds are set high and the application processes are cumbersome, greatly deterring foreign banks from fully participation in the competition within the Chinese market.

In terms of business operations, foreign bank branches and joint venture banks can only handle the accepting of deposits and granting of loans in foreign currencies. In addition, all interest rates must be approved by the People's Bank of China (PBOC). In carrying out the authorised business, the types of clients that foreign banks can accept are limited and the handling of certain types of remittances to overseas destinations must receive PBOC approval.

Recently, preparations got underway to allow certain foreign banks chosen by the government to carry out transactions in RMB in Shanghai. Although the initial approval is on a selective and experimental basis, further expansion could be expected as the demonstration effect spreads and the government observes the benefits derived.

The liberalisation process will be on a progressive basis as the government aims to remove obstacles to the operations of financial institutions and raise their competitiveness. The primary concern is that the domestic banking sector remains quite unsophisticated and is currently facing grave problems. With lending activities to

the SOEs in compliance with government instructions, Chinese domestic banks are carrying a very heavy bad-debt burden and are not in a position to compete. Other limits coming with the ownership system, including prohibitions for the merger among banks and the bankruptcy of state financial institutions, also constraint the ability of the banking sector to pool resources and raise efficiency in the face of real competition.

However, the Chinese government has been making headway toward building an expanded and modern banking sector. For example, relevant laws governing the commercial banks, the policy banks and the central bank have been passed, clarifying the different businesses' scope according to type, which is allowing greater autonomy for the commercial banks in their decision-making. This represents substantial progress in the commercialisation of the whole banking system.

Adding to the elaboration is the political will to reform the problematic SOEs. Legislation in this regard has picked up pace to allow the bankruptcy of insolvent SOEs and the merging of activities in the capital market. Given the substantial reform of SOEs, the Chinese banking system could be set free from the vicious cycle of in-performance loans and ever-worsening debt burdens. Greater commitment to liberalisation in the banking sector could also back up the SOEs' reform by allowing more foreign capital and financial expertise into the market to help the restructuring of enterprises. As substantial reform in the SOEs also relies on the provision of a new social security network, which was formerly based at the enterprises level, greater foreign participation and competition could drive down the cost for the new establishments and guarantee sufficient resources.

The foreign exchange system

The foreign exchange system is crucial in financial liberalisation in the sense that it controls the availability and the mobility of foreign exchange and could facilitate flows of trade and investment. The present exchange system was introduced in 1994. Under the new system, a unified exchange rate is determined in an inter-bank market. To trade in this new system, a financial institution must become a member of the China Foreign-Exchange Trading System (CFETS), thus foreign banks are subject to different regulations as compared with domestic banks. Domestic banks may both buy and sell foreign exchange for the customers and for their own accounts, but foreign banks may only sell foreign currencies or trade among themselves on behalf of customers.

The new foreign exchange system allows foreign enterprises to retain all of their foreign exchange in designated banks. A swap centre, parallel and linked with the CFETS, can serve as the place for the foreign enterprises to conduct exchange transactions among themselves to balance their foreign-exchange revenues and expenditures. This makes it possible for the foreign enterprises to enjoy greater autonomy as long as their operations are self-equilibrating. The domestic firms cannot

retain foreign exchanges. Revenue and expenditure are balanced by trading with designated banks with relevant transaction contracts.

Although significant changes have taken place in the new system to cope with modern international economic transactions, further improvement is still to be made. Capital account liberalisation, which involves relaxation on both inward and outward capital flows and forms an integral part of financial liberalisation, is currently deterred by the inconvertibility of RMB and the restrictive control over foreign exchanges. Furthermore, the different rules regarding domestic and foreign enterprises and financial institutions cause segmentation in the foreign exchange market, an impediment demanding more attention in the future.

The stock market

The Chinese stock market is still in a premature stage and remains highly regulated. Consequently, participation by foreign investors is limited. The Shanghai and Shenzhen stock exchanges offer B-shares for foreign investors. B-shares are exclusively reserved for foreign investors compared with the A-share for residents, and the two are not substitutable. In addition, no individual overseas investor is allowed to own more than 5 percent of any single issue of B-shares outstanding, and short-selling such as day-trading is prohibited. These all reflect the primary stage of the current Chinese stock market, and impede the inward flows of international portfolio capitals (Lees and Thomas 1996).

The current Chinese stock market employs a membership system. Trading is limited to spot transactions by full members, who are all Chinese securities houses. The foreign securities firms, on the other hand, are only permitted to trade B-shares on the market by accepting a "special membership", which means they have to choose a local brokerage firm as a partner and pay them 20 percent of commissions.

The liberalisation in the stock market will necessarily involve the perfection of the market structure and the related legal system. Further opening-up by introducing international standards and allowing more foreign participants into the market will attract more foreign capital into the economy on the one hand. On the other hand, it will require a stronger supervisory system and more prudential regulations. The latter will help to form a healthy capital market which can stay alert of the possibility of a bubble economy, where imprudent lending for the purchasing of securities drives the market price to an unrealistically high level, leaving the investing entities insolvent and the lending banks incurring non-performing loans when the bubble bursts. This is basically the story of the current financial crises in Thailand, except that the bubble effect comes from both the securities market and the real estate market. The case should serve as a lesson for China since its stock market also has experienced a skyrocketing-nosediving style of fluctuations a few years ago. With more exposure to international scrutiny and the necessary prudential measures, particularly in terms of supervision, a financial system more integrated with the world market can be a strong

vaccine against serious financial distress for the national economy (Limthammahisorn 1997).

Insurance

The Chinese insurance industry is being deregulated and more insurance companies are being allowed to compete in the business. Certain market access is allowed for foreign insurance companies, and such businesses as marine insurance, property insurance, fire insurance and personal safety insurance now can be handled by foreign participants. According to Chen (1996), a newly established Sino-Canadian joint venture was selected as the first of its kind to deal with life insurance business, which previously was reserved for domestic players. By now, six overseas insurance companies and more than one hundred foreign insurance representative offices have been set up in China.

However, the whole process of liberalisation needs further acceleration as the current level of competition in the industry still lags far behind the rapidly growing demand brought about by the booming economy.

Furthermore, great potential remains in the market as the reform of the SOEs will create greater demand for non-commercial insurance which forms an integral part of the social security network. The current market capacity will be far from adequate if the reform transfers the formerly state-provided social security programs such as the health-care into the insurance sector. Liberalisation in the industry to increase the market capacity and lower the price to some affordable level for average working class households will help to facilitate the reform process.

This summary of industry developments makes it clear that the Chinese government has put reform in the financial sector high on its agenda. The process of restructuring and opening-up in the sector was demanded by the ever-growing economy. Now it is coming to be realised that in order to achieve sustainable development in this sector, efforts should be directed into a more multilateral dimension as well. Mechanisms such as GATS offer WTO members chances to cooperate in eliminating relevant impediments with common features, and they have proven to be efficient (Kono and Low 1996). China, in an effort to gain WTO accession, should treat further reform and liberalisation in the financial services sector as both obligations and opportunities.

Conclusion

We have seen from above that, given their profound implications for the economy, financial services form an important focus for the international community in its search for a greater level of liberalisation. GATS has provided a mechanism for WTO members to negotiate mutually beneficial means to liberalise and allow more sensible competition in the financial sector, which we believe will be conducive to economic growth in general.

China is still in its transition from a planned economy to a market economy, and the once much-controlled financial sector will be difficult to fully deregulate and liberalise in a short time span. However, on the basis of bilateral negotiation or of voluntary reforms, China has taken initiatives in relaxing the inflexible rules along its way to reform and development, and foreign participation is more than obvious nowadays.

Once the incentives for reform are revealed and reform initiatives are taken, there are good opportunities for China to continue marching along its growth path. The participation of China would be welcomed for its contribution to multilateral liberalisation efforts, given the size of the economy and its growth momentum. For China itself, in a basically gradual reform process, exercises of both decisiveness and caution should be balanced in deregulating and liberalising the sector according to the country-specific conditions and its level of the economic development.

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Intellectual Property Protection in China

by Lin **Fu**, Cuiping **Zhang** and Li **Zheng**

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Introduction

Over the past two decades, the protection of intellectual property rights (IPRs) has attracted great attention in the world trade arena. Americans claim they lose billions of dollars annually from inadequate intellectual property protection abroad, primarily in developing countries (Oksenberg, Potter and Abnett 1996). China represents a potentially vast market for the sale and licensing of intellectual-property-based goods and services, particularly computer software and information technologies, but it has not established a strong regime of IPR protection. The widespread unauthorised reproduction and distribution of goods such as computer software and movies in China has been an area of great concern of high-technology firms operating in the Chinese market. IPR protection has been a significant stumbling block in U.S.-China, and more broadly the industrialised countries-China, relations. This paper describes briefly the evolution of international intellectual property protection, presents the current situation and remaining problems of IPR protection in China, attempts to analyse the effects of improving IPRs in a developing country such as China, and draws out some policy implications.

The evolution of IPR protection

Intellectual property rights are defined as a mix of ideas, inventions and creative expression on which there is a public willingness to bestow the status of property (Sherwood 1990). They mainly include copyright, patents and trademarks as well as industrial designs, geographical indications and trade secrets. The need for international cooperation on IPRs arose as early as the 19th century because IPRs are country-specific, created by national legislation. The existing international legal and institutional framework for IPRs protection consists of several multilateral conventions which lay down standards for protection. The most important of these are the Paris Convention (on patents, trademarks and industrial designs), the Berne Convention and the Universal Copyright Convention (both on copyright), the Rome Convention (on neighbouring rights), and the Treaty on Intellectual Property in Respect of Integrated Circuits. Most of these conventions are administered by the World Intellectual Property Organisation (WIPO) or UNESCO.

Following substantial growth of international trade in goods embodying intellectual property, a number of industrialised countries, especially the United States, have

increasingly felt that the existing international regulations are too weak or poorly enforced and the inadequate protection of IPRs in technology-importing countries has reduced the advanced economies' comparative advantage in the high-tech area. With the support of Japan and the European Union, the U.S. spearheaded the movement to have IPRs included as an integral part of Uruguay Round negotiations of GATT and finally reached a comprehensive agreement on Trade-Related Intellectual Property Rights (TRIPs), which represented a complex balance of conflicting national perspectives and interests with respect to IPR protection between developed countries and developing countries (Hoekman and Kostecki 1995).

The TRIPs Agreement covers copyrights and related rights (rights of performers, broadcaster and phonogram producers), layout designs of integrated circuits, geographical origin indications, trade marks, industrial designs and patents. Its main rules are summarised as follows:

- all the basic GATT principles as MFN, national treatment and transparency are applied to IPRs;
- The TRIPs Agreement establishes the minimum substantive standards for protection of the above IPRs and prescribes the necessary procedures and remedies members should provide for the enforcement of rights;
- The general dispute settlement mechanism of WTO is available to address IPRs issues;
- Tte TRIPs Council will be the monitoring body of the Agreement;
- Developing countries and transitional economies could have a 5-year transitional period until 1 January 2000.

For the first time, the TRIPs Agreement recognises the importance of intellectual property rights in the global trading system. The TRIPs will, to a large extent, have a harmonising effect on standards for the protection of intellectual property rights throughout the world. With the exception of the obligation to protect pharmaceutical products, harmonisation can be expected by 2000 when the transitional period for the implementation of the Agreement by developing and transitional economies comes to an end.

Current IPR protection in China

The progress of China's IPR protection

Over the past 18 years, China has made considerable progress in developing an intellectual property rights regime. The National Science Conference in 1978 was a

turning point of development of IPR protection in China. Since then, China has promulgated an impressive array of laws and regulations regrading intellectual property, which include Trademark Law in August 1982 (revised 1993), the Patent Law in March 1984 (revised 1993), the Copyright Law in September 1990, and the Computer Software Regulations in October 1991. In addition, the General Principles of Civil Law, adopted in April 1986, recognised the rights of individuals and legal entities to hold copyrights, patents and trademarks. This enactment and a subsequent Civil Procedure Law passed in April 1991 enabled Chinese citizens and legal entities, as well as foreigners and foreign enterprises and organisations, to demand in Chinese courts that infringements can be halted and that courts can award claimants compensation for damage (Oksenberg, Potter and Abnett 1996).

The government also began to create the bureaucratic infrastructure to enforce IPR laws and regulations. At the national level, the State Copyright Administration, China Patent Office and the Trademark Office take the main responsibilities concerning IPRs. Six other agencies have important enforcement responsibilities: (1) the Ministry of Public Security for arresting violators of the law and accumulating evidence against alleged criminals; (2) the People's Procuracy for bringing IPR cases to court; (3) the courts and especially their recently created intellectual property tribunals at national and provincial levels for hearing complaints of infringement and imposing fines and imprisonment; (4) the Ministry of Culture for inspecting all retail and wholsale outlets selling cultural commodities (books, records videotapes, CDs paintings) and for fining IPR violators; (5) the State Administration of Industry and Commerce for withdrawing business licenses from IPR infringers; and (6) the Customs Administration for halting the export or import of pirated products.

Along with IPR law-building and enforcement, the government has also encouraged the formation and registration of associations which have natural interests in IPR issues. For example, the China Software Alliance (CSA) was founded in 1995. Two other important associations are the China Intellectual Property Association (CIPA) and the Copyright Society of China (CSC). They have helped the promotion of IPRs through increasing public awareness of IPRs and through close cooperation with state policy-making, administrative, law enforcement and judiciary organs to combat piracy, infringement and other illegal activities (Oksenberg, Potter and Abnett 1996).
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In the training area, the State Council has established a China Intellectual Property Center, under the supervision of the China Patent Office. Its purpose is to provide training in patent, copyright, and trademark law to judges, lawyers, customs officials, public security personnel, and other officials from both the national and local levels.

The government has encouraged publications on IPR issues as well. *China Patent News* is published twice a week by the China Patent Office. *Zhuzuo Quan* (Copyright) is published by the CSC and SCA while *Zhishi Chanquan* (Intellectual Property Right) is a joint effort of the Chinese Branch of the Intellectual Protection of Industrial Property Association and the China Associations of Export License and of Trade

Workers. These publications chronicle legal developments and meetings, and report important speeches and articles by top officials.

In the international arena, China was accepted as a member of the Geneva-based WIPO in April 1980. It jointed the Paris Convention in December 1984 and Berne Convention in October 1992. The rapidity of these developments earned widespread praise from the international community, especially from WIPO.

Remaining problems in China's IPR protection

From the above-mentioned, it is clear that a policy community devoted to IPRs has emerged in China. Major bureaucracies responsible for intellectual property have been created, and linkages with the external world have been established. However, creating an effective IPR regime is still an enormous challenge for China. In particular, it is still in the early stages of creating a legal system, as that term is understood in the West, enforced by an independent judiciary.

Currently, China is facing the following problems in its IPR protection. One is the lack of coordination among governmental agencies. China's IPR policy community consists of many diverse and loosely integrated parts: various governmental agencies, policy coordinating bodies, state-sponsored professional associations, specialised publications, and the producing, distributing and consuming industries. The large number of agencies involved in IPR produces problems of coordination.

Another problem is the reliance on administrative punishment instruments. The IPR regime in China, which heavily relies on administrative punishment instruments such as withdrawal of licenses, heavy fines, and disruption of business, will not only lead to corruption and arbitrariness but also encourage different legal and administrative agencies to compete for fines and fees. Consequently, violations are left to continue. Public-punitive methods are also subject to the inconsistent personal commands of senior officials, and they undermine the development of private law, especially in the area of property and contract.

A third problem is the inadequacy of damage remedies. The remedy in IPR cases in western countries, particularly in the U.S., is to compensate the plaintiff or injured party (Oksenberg, Potter and Abnett 1996). But in China the tendency has been for the tribunals to evaluate the damage to society at large. This results in lesser fines being imposed on violations compared with the financial damage to the injured party. Special IPR tribunals at lower levels have approached IPR cases primarily from the vantage point of protecting the state and enforcing the public interest, rather than assessing and awarding damages to private parties.

Fourth, there is ineffective IPR protection at local levels. Unlike in Beijing and Shanghai, other cities in China do not have the IPR policy communities on the same scale. The intellectual and bureaucratic gap on IPR protection issues between Beijing

and the provinces is a major factor impeding effective IPR protection at the local level. Local officials feel enormous pressure from above and below to place a premium on economic growth and employment, rather than IPR protection. Thus in most instances, they have strong incentives to earn short-term gains by allowing IPR-infringing manufacturers to operate in their territory.

To sum up, the situation is that while laws are in place, the institutions and norms are nonetheless weak. The existing laws and regulations need further enforcement. For instance, China agreed in late February 1994 to strengthen its Copyright Laws and to close down some compact disc factories violating US copyrights. However, in June 1995 there was indication that some factories had been reopened (Konan, Croix, Roumasset and Heinrich 1996).

Effects of improving IPR protection in China

China is facing great pressure to improve the level of protection for intellectual property rights, especially in its WTO accession negotiations. Once China becomes a member of WTO, it must reach the IPR protection standards of TRIPs Agreement, which are higher than the current ones in China. Will China be better off or worse off by so improving its IPR protection level?

Much has been written about the effects of improving IPR protection in developing countries. Neo-classical trade theory suggests that the level of protection for IPRs in a particular country will depend on whether its comparative advantage lies more in innovation or imitation. A higher level of IPR protection is well-justified for countries, such as the United States, with a significant comparative advantage in innovation; haowever, a lower level would be optimal for those whose comparative advantage lies more in imitative activities and adaptation of other’s innovations. This does not apply only to developing countries. Borrus, Trebilcock and Howse (1995) studied IPR protection in Japan’s economic performance and concluded that Japan’s success at imitation and adaptation of innovations developed elsewhere, aided by a strategic use of IPR protection to stimulate imitation in some sectors and innovation in others, accounted for its dramatic economic growth in the 1960s and 1970s. Evidence also shows that the strength of Canadian multinational enterprises has been linked to their capacity to find and adapt technology from elsewhere. In sum, it is far from clear that increased intellectual property protection would benefit even developed countries with a strong advantage in imitation. Deardorff, Trebilcock and Howse (1995) argue that global aggregate welfare may well be maximised if certain countries are exempted completely from requirements for IPR protection. Further study by Maskus, Trebilcock and Howse (1995) has yielded the result that “static global welfare would suffer from the extension of IPR protection by information-importing countries”. It has also been recognised that granting of IPRs allows the owners to enjoy monopoly rights which reduces competition and social welfare.

It seems that IPRs will cause great losses to producers and consumers in countries like China, whose R&D sectors are not competitive in investing in new products and processes but are strong enough to be good at imitation. Strengthening IPR protection will increase product prices and lead to decreases in real wages. This will hinder the China's economic growth and enlarge its gap with developed countries in the short run.

However, when one considers some dynamic effects and long-run gains, China could be better off with a stronger IPR protection. First, China could benefit from innovation which occurs both inside and outside its own border. Inadequate IPR protection normally induces the "free rider" problem, under which circumstances individuals or firms would be much less likely to make any investment in R&D. A strong and effective IPR regime will no doubt increase incentives to both domestic and foreign producers since innovation will be compensated at its full social value, and yield greater amounts of innovation. The strengthening of IPR in China, together with trade liberalisation, will provide a more affirmative path to economic growth.

Second, China will attract greater amounts of foreign direct investment (FDI) and technology transfer if foreigners believe that products, processes and trade secrets will be adequately protected. Although strong IPRs alone are insufficient for generating strong incentives for firms to invest in a country, a recent study of Lee and Mansfield (cited in Maskus 1997) shows that weakness of IPRs has a significantly negative impact on the location of American FDI, and both the volume and quality of investment diminish in countries with limited intellectual property rights. There is also direct evidence that the weak IPRs in technology-importing countries reduce the quality of technology transferred since returns to a technology supplier increase with patent protection in the recipient country. This may contribute to the fact that technologies transferred to developing countries tend to be significantly older that those transferred to industrial economies (Contractor, cited in Maskus 1997).

Third, China can expand foreign trade with other countries through improving IPR protection. Recent evidence suggests that a country's IPRs regime also has impact on trade flows. Maskus and Penubarti (cited in Konan, Croix, Roumasset, and Heinrich 1996) find that bilateral trade flows increase with strengthening of IPR protection and that this impact is stronger in larger countries. A stronger IPR regime will also remove obstacles to China's accession to WTO. As Anderson noted in 1996, "Only when such commitments are firmly embedded in China's WTO accession package will countries such as the United States be prepared to allow the accession to proceed". And only then will China benefit fully from increased market access to western markets for agricultural, textile and manufactured products and enjoy the other fruits of the Uruguay Round in terms of trade in goods and services, once it becomes a WTO member.

Fourth, the improvement of IPR protection will control and reduce the trade of

counterfeit goods which is a severe problem in China nowadays. Not only are Chinese being cheated by the lower quality of counterfeit goods, but in certain areas - such as pharmaceuticals, electronic commodities, and processed foods and beverages - counterfeit goods pose health and safety hazards. Chinese consumers may well be better off with the reduction or elimination of counterfeit goods even though some prices may rise.

Fifth, IPRs do not necessarily generate monopoly market positions that result in high prices, limited access, and exclusive use of technologies. They are more similar to standard property rights, in that they define the conditions within which a rights owner competes with rivals (UNCTAD, 1996). There are likely to be competing products and technologies, including new ones that do not infringe existing property rights. Thus IPRs may encourage dynamic competition with long-run consumer benefits.

Conclusion

China has made substantial progress in IPR protection since 1978 in terms of law-building, bureaucratic infrastructure establishment and cooperation with the outside world. But the IPR issue is still one of the major sources of economic conflicts between China and other countries, especially with the United States. To set up an effective IPR regime, it is important for China to develop a long-term strategy for improving IPR performance: fostering new attitudes about IPRs among leaders, bureaucrats, and the populace at large; strengthening the legal and administrative regimes, especially at the local levels; and providing necessary training for officials, judges and lawyers. Although China may suffer from the price rising in the short run, a stronger IPR regime can generate long-term growth and efficiency benefits as it attracts additional FDI and licensing and spurs further follow-on innovation and technology spillovers. China would be better off if it moved gradually to a strong IPR regime. Any losses in the short term are likely to be outweighed by dynamic effects and long-run gains. It should be noted that this outcome is far more likely if the implementation of stronger IPRs is accompanied by complementary policies such as further market liberalisation, removal of investment regulations, and development of modern and efficient infrastructure.

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State Trading and China's Trade Policy Reforms

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Introduction

State trading has long been an important issue in the global trading system. It potentially enables individual governments to evade their commitments made under the GATT through direct control of state trading enterprises. As for China, state trading has been the main component of its foreign trade regime. Since 1979, one of the major objectives of China's reform of its foreign trade regime has been the easing of direct control over trade and decentralisation of trading rights. After two decades of reform, the number of controlled commodities has been greatly reduced and a large number of firms have obtained access to foreign trade in China. Despite all these achievements, state trading still appears to be one of the major concerns of other major member countries in China's negotiations for accession to the World Trade Organization (WTO).

This paper reviews the development of rules on state trading under the multilateral trading system, examines China's reform in this, and analyses the remaining challenges China faces in its accession to WTO.

State trading under WTO

History and definition

In the Tokyo Round, disciplines to address state trading enterprises were included in the GATT for the first time. This reflected the fact that contracting parties realised that state trading enterprises might not be bound by tariff commitments (Hoekman and Kostecki 1995). State trading is covered under Article XVII in the General Agreement on Tariffs and Trade (GATT-1947). However, relevant provisions of the GATT-1947 did not provide a clear definition of what constitutes state trading, and contracting parties provided their own interpretations of what was meant by state trading in their notifications. Hence in the Uruguay round, the final agreement for the first time defined state trading enterprises, which appeared in the "Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs And Trade 1994" ("Understanding"), as:

> "Government and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including

> statutory or constitutional powers, in the exercise of which they influence through their purchase or sales the level or direction of imports or exports" (World Trade Organisation, 1994).

The definition made it clear which enterprises are subject to notification. The agreement also sets up arrangements for review of notifications and counter-notification. Article XVII of GATT covers state-owned enterprises, enterprises granted in effect exclusive or special privileges, marketing boards, enterprises controlled by a Member and import monopolies. As Hoekman and Kostecki (1995) indicate, "State trading enterprises may be government owned or fully privately owned. What matters is not the ownership, but exclusivity."

Why is it an important issue?

With continuing worldwide trade liberalisation and the successful conclusion of rounds of multilateral trade negotiations, the average tariff level has been greatly reduced and non-tariff barriers have been included within the WTO framework and further regulated. Under such circumstance, the ability of individual governments to control trade has been constrained. However, for different reasons, governments still seek various means of protecting domestic industries or influencing trade. State trading has been one method of achieving that goal. Firstly, state trading enables governments to use quantitative restrictions by requiring state trading enterprises to import only limited amounts of foreign products; secondly, governments could provide protection to domestic industries by allowing large markups of import goods on the domestic market. However, state trading is not effectively regulated under current WTO articles and thus risks raising more impediments, countering to some extent the trend of global liberalisation.

As explained above, state trading clearly raises two quite distinct concerns—the use of state enterprises as mechanism for direct policy control of trade volumes, and the possible adverse consequences of monopoly power on the level and fairness of trade outcomes. Direct policy control of trade might nullify or impair market access opportunities by bringing a separate, undeclared and unrestrained use of such a policy instrument (Hoekman and Kostecki 1995; GATT 1993).

Legal obligations under GATT

Article XVII of GATT and the "Understanding" outline two main legal obligations imposed by the GATT/WTO relating to state trading: non-discrimination and transparency. Firstly, according to GATT, the basic obligation for state trading corporation is to operate following the general principle of non-discrimination. In fact, this can be achieved through making any purchases or sales solely in accordance with commercial considerations, including price, quality, availability, market ability, transportation and other considerations of purchase or sale; afford the enterprises of other Members adequate opportunity, in accordance with customary business practice,

to compete for participation in such purchases (Article XVII: 1b); and Members must ensure that enterprises in their jurisdiction are not prevented from acting in accordance with the non-discrimination principle (Article XVII :1c).

Another main obligation of the Agreement is transparency. The notification obligation of GATT-1947 is further strengthened by the “Understanding”. The Understanding requires members to notify the Council for Trade in Goods the names of state trading enterprises doing foreign trade, whether or not imports or exports have in fact taken place; the products they import or export; and also provide other information in accordance with the questionnaire so as to permit a clear appreciation of the manner of operation of the enterprises notified. Also, on the request of another party having a substantial trade in the product concerned, information is to be provided on the import markup on the product during a recent representative period, or, if not available, the resale price (Article XVII: 4b).

State trading in the context of China’s WTO accession negotiations

China was regarded as a centrally- planned economy, or at least not a market economy, when it started its negotiations to re-join GATT. China’s foreign regime was believed to be pure state trading at the beginning. As Goode (1997) worded it, “state trading is a feature of non-market economies where price may not be the only or dominant consideration in making import or export decisions. In this case, there is significant potential for market distortions and little transparency.” Most contracting parties feared that the existence of state trading enterprises in China would make any tariff commitments meaningless. With respect to China’s importing regime, other GATT members will undoubtedly want some assurances from China beyond its mere acceptance of GATT (Jackson 1989). This reflects a commonly-shared concern WTO members have over China’s trade regime.

In the history of the GATT, certain non-market economies were accepted into GATT under special provisions or protocols, such as Poland, Hungary, Romania and Yugoslavia. Why has China met so much difficulty in being accepted? We believe there are two main reasons. The above-mentioned countries are relatively small in terms of their impact on trade. Even though the trade relations between non-market Contracting Parties and other members are troublesome, other members are willing to tolerate them because they either have special arrangements of their own or the amount of trade is small (Jackson 1989). China, however, is a special case. It is very large and therefore has significant impact in terms of the GATT context. Also, the rules for accommodation that are worked out in the China context will set an important precedent for future similar activities of GATT, including the possible future accession of Russia and other former Soviet republics, and revision of Article XVII relating to state trading.

For market economies, the market distortion created by state trading is mainly measured by the markup charged by state trading enterprises. However, the issue is more difficult in non-market economies because their foreign trade regime is less transparent. In addition, domestic market prices need not reflect actual scarcity values or respond to international prices. Government orders or plans play an important role in trade and other economic activities too, as the pre-reform Chinese economy shows. That is why major trading partners are concerned and sensitive about state trading in China and it has become one of the impediments for China's accession into WTO.

China's trading rights reform

Considering the needs of its own economic development, China began its foreign trade regime reform in 1979, especially in the area of decentralising trading rights. Prior to reform and opening up to the outside world in 1978, China's trade regime was pure state trading, with imports and exports of all products essentially monopolised. Since then, there have been great changes in the structure of policies, including freeing up the prices of most goods, introducing indirect trade policy instruments, making the exchange rate convertible on current account, and allowing a wide variety of firms to participate in trade (Martin 1997). In the 1990s, China quickened its pace by further liberalising its trade regime. This evolution of China's foreign trade regime can be broadly divided into three phases.

Phase One (1950-1978): pure state trading

Under central planning, almost all trade was carried out by 12 large Foreign Trade Corporations (FTCs). These corporations acted as an "airlock" between domestic and international prices (Lardy 1992). At that time, the principal objective of foreign trade was to earn foreign exchange in order to import advanced technology and equipment and develop national economy. The government made annual import and export plans. The central government bore the profits and losses of foreign trade. The control over foreign trade was supplemented by strict control of foreign exchanges. This period of time could be named "pure or complete state trading". Administrative orders, instead of market prices or any other commercial considerations, played a decisive role in guiding business operations of these enterprises.

Phase Two (1979-1989): gradual decentralisation

The 1980s witnessed a rapid increase in China's foreign trade due to gradual liberalisation and decentralisation of its foreign trade regime. Firstly, trading rights were selectively extended. Provincial and municipal branches were dispatched from their mother companies (National FTCs) and became legally independent economic entities. Some large producing firms were also allowed to trade. The number of foreign trade corporations with trading rights was progressively expanded. At an earlier stage, joint ventures and firms located in the special economic zones were allowed trading rights.

Secondly, the number of controlled import and export products was greatly reduced in this period. The process of decentralising trade was gradual, but the trend was very consistent, with commodities removed from export and import planning progressively (World Bank 1994). In 1978, 3000 categories of export products were controlled by plans, whereas the number was only 120 in 1986 (Wang 1991). Lardy (1991) indicates that import and export licensing measures were introduced in 1980 to replace the control imposed under the previous trade monopoly. The coverage of licensing has since fallen dramatically.

In this period, China reformed its foreign exchange system by introducing the Foreign Exchange Retention System (FERS) and establishing Foreign Exchange Adjustment Centers (FEACs). These centers were also known as “swap centers”. FTCs, export producing enterprises and their superordinate level of governments were allowed to retain a certain percentage of the foreign exchange earned from exports. Later, China gradually increased the retention rate.

However, the central government still produced national plans to control the total volume of imports and exports, and the plans were fulfilled by FTCs at different levels. Important products were still imported and exported through designated FTCs. All other FTCs could operate the import and export of the remaining products within their specified range of business. Producing enterprises and foreign companies were only allowed to export their own products and to import materials needed for their own production. To a large extent, trading enterprises still did not have free access to foreign exchange for importation.

Phase Three (1990-present): further liberalisation

Since 1990, the foreign trade plan has been abolished and the central government only provides guidance on total trade volume (Wang 1991). Import and export approval procedures for controlled commodities are substantially decentralised and simplified. In 1996, 114 categories of export commodities were controlled by quotas and licenses, of which 16 were operated by designated companies (MOFTEC 1997, pp. 80-81). On the import side, only 15 categories of electrical and machinery products and 12 categories of staple raw materials were under quota administration. The imported commodities under special registration requirements were reduced from 570 tariff lines of 20 categories to 470 tariff lines of 14 categories (MOFTEC 1997, pp. 90-91).

With the principles of “efficiency, fairness and openness”, the quotas were distributed through auctions, biding or regulated procedures. Quota distribution through biding was experimented with on 27 categories of export commodities. International bidding was introduced for the import of most of the special electrical and machinery commodities (MOFTEC 1997, p. 82).

The pace of entitling the large and medium-sized state-owned enterprises with trading rights was greatly quickened. At the same time, some of the domestic trade firms as well as the scientific research institutes were also provided with trading rights. By the end of 1996, alongside the 150,000 foreign adventures in China, there were more than 12000 enterprises engaging in foreign trade, of which more than 5000 were state-owned production enterprises (MOFTEC 1997, p. 97).

A recent reform development was that foreign firms which meet certain criteria will be allowed to form joint venture FTCs. This experiment has been carried out in Shanghai and Shenzhen (Martin 1997). This is the first time China has allowed the entry of international companies to this field.

In 1991, the Chinese government phased out all forms of subsidies to trade. In 1994, China abolished FERS and made the Renminbi (RMB) *conditionally* convertible under current account. In 1996, the conditions implied were eliminated (MOFTEC 1997).

Even though trading enterprises are still subjected to restrictions on the range of products that they may trade, the constraints imposed in the business scope of most FTCs appear to be very liberal. While joint ventures and foreign owned enterprises are subject to tighter restrictions on the scope of the products they trade, the sheer number of these enterprises means that a large number is likely to be active for most important product groups. As a consequence, consumers and producers wishing to import or export will have a range of enterprises through which they can undertake these transactions (Martin 1997).

Remaining challenges for China's foreign trade reform

The reform of China's foreign trade regime have greatly reduced governmental distortions and have made a remarkable progress in establishing an competitive, fair and efficient environment. Nonetheless, there are still many trade controls denying access of foreign products and slowing necessary structural adjustments within the economy. For example, a number of central FTCs and large state-owned enterprises are given selective monopoly power to import and export strategic commodities. These important commodities are 16 categories of export including maize, soybean, cotton, coal, crude oil, refined oil, and tea, and 12 categories of imports including rice, maize, wheat, vegetable oil, sugar, chemical fertiliser, cotton, tobacco, crude oil, and processed oil. These are exclusively traded by designated trading companies. The trade mentioned above accounted for about 7 per cent of China's exports and 11 per cent of imports in 1995 (Martin 1997). If China phases out the state trading system after its accession to WTO, the volume of imports of grain, oil, refined oil, steel, lumber, cotton will be much larger, and the exports of them will be much lower as a result of production adjustment according to China's comparative advantage.

The trading right is still strictly assessed and approved by the Ministry of Foreign Trade and Economic Cooperation (MOFTEC). Most domestic enterprises still lack rights to trade on their own account. Although the quotas of a few commodities are distributed through bidding at auctions, most of the quotas are still distributed by the traditional administrative procedures. These untransparent methods, which are at the discretion of officials, are most likely to be contributing to inefficiency and corruption.

Recently China has offered to phase out the restrictions on entry into foreign trade (for both domestic and foreign firms) within three years of entry to the WTO for all commodities except those currently subject to state trading and designated trading. The trading rights for goods subject to designated trading are to be phased out over periods up to five years. Only the products subject to state trading will continue to be subject to restrictions on entry into foreign trade.

Even though China has met most of the obligations under relevant GATT articles on state trading, and the establishment and maintenance of state trading corporations is allowed under Article XVII of GATT, the question remains as to what extent state trading can help to meet the objectives of the government. The major relevant policy objectives in China are to ensure supplies and avoid fluctuations in the price of strategic commodities. As pointed out by Martin (1997), "It is far from clear that these institutions are the most effective means for achieving these objectives. An important problem with the current Chinese system is the long lags in the procurement processes for imports, and the planning process for exports; these lags and the inflexibility of the system frequently result in imports being insufficient and exports being excessive." State trading not only is inefficient in achieving the government objectives, but also it distorts domestic markets by creating monopolies. Alternative policy instruments such as tariffs or tariff quotas may be used to achieve these objectives more efficiently, as these methods are more transparent and flexible. This imposes a real challenge to China's foreign trade reform. China is now preparing to introduce tariff quotas for the importation of grain and edible oil. As tariff and tariff quota are more consistent with WTO, reform in this direction will make China more consistent with the global trading system.

Conclusion

State trading has been an important issue within the framework of World Trade Organisation. Due to its potential to enable individual governments to evade GATT obligations, it will be increasingly emphasised during the next round of multilateral trade negotiations and its use will probably face more restrictions. In the context of the negotiations on China's accession to the WTO, China has been making great progress in liberalising its foreign trade regime. With the deepening and expansion of liberalising process, the access to foreign trade for both domestic and foreign companies will be more open and the number of commodities subject to state trading will decrease steadily. China's foreign trade regime will eventually be transparent,

competitive and efficient. China's accession into WTO would encourage China to take further steps in reforming and accelerating the progress of its trade liberalisation. This will benefit both China and the rest of the world economy.

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Anti-Dumping and the WTO: Implications for China

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Introduction

Anti-dumping has been a hot topic in China for years, but China has been a victim rather than a user of anti-dumping mechanisms in the past two decades. On 25 March 1997, China promulgated its first legislation on anti-dumping — The Regulations on Anti-dumping and Countervailing Measures -- and vowed to establish its own anti-dumping institution (Li and Zhong 1997; Li 1997). In this paper we briefly review China's anti-dumping legislation; examine what is behind dumping and anti-dumping; appraise the anti-dumping regime under GATT/WTO; and make some policy suggestions to China's anti-dumping authorities on the basis of the forgoing discussion.

Review of China's anti-dumping regulations

China's Regulations on Anti-dumping and Countervailing Measures include six chapters and 42 articles. Chapter 1 states the source and objective of the legislation. The Regulations are formulated under China's Foreign Trade Law with the objective of maintaining foreign trade order and fair competition, and protecting domestic industries. Under these Regulations, anti-dumping measure may be taken where an imported product, by way of dumping, causes or threatens to cause material injury to an established domestic industry, or materially retards the establishment of a domestic industry.

Substantive rules on anti-dumping are found in Chapters 2, 3 and 4. Chapter 2 defines dumping, injury and domestic industry, and provides for the determination of normal value, export price, dumping margin and injury. Under this chapter, dumping occurs when the export price of an imported product is lower than its normal value. Chapter 3 sets out the requirements on petition, initiation, conduct of anti-dumping investigation. It stipulates that upon initiation, the Ministry of Foreign Trade and Economic Cooperation (MOFTEC) and the Customs General Administration (CGA) are jointly responsible for investigating the existence of dumping, whereas the authority of injury investigation is delegated to be the State Economic and Trade Commission (SETC). Normally, an investigation shall be concluded within twelve months. Preliminary and final determinations are to be made by MOFTEC and SETC separately and published

by MOFTEC. Under Chapter 4, anti-dumping measure may be taken where dumping, injury and the causality between them are found. The imposition of an anti-dumping duty is subject to the determination by the Tariff Commission of the State Council (TCSC) once proposed by MOFTEC, and it is enforced by the CGA. The duty shall not exceed the dumping margin. An anti-dumping measure shall not be in force in excess of five years (the sunset rule), during which period anti-dumping order will be reviewed. Counter-measures may be taken when an anti-dumping measure is being circumvented (Article 35). Noteworthy about Chapter 6 is Article 40, under which China may take counter measures against any country or region that applies discriminative anti-dumping measures to China's exports.

Basically, the provisions set forth in China's anti-dumping legislation (eg. determination of dumping and injury, investigation procedures, imposition of anti-dumping duties, the sunset rule, and review) are compatible with the WTO Anti-dumping Agreement. However, a few articles may still be problematic. For instance, the wording of "the relevant authorities under the State Council" (eg. in Articles 17, 19 and 35) is quite ambiguous. The provision on the capacity of a petitioner (Article 11) is also not worded in full consistency with the WTO Agreement (Paragraph 4 of Article 5). Another possible loophole is that although the rule of de minimis is introduced (Article 18), the percentage requirements are not specified as the WTO Agreement requires (2% and 3%). Finally, the language in Article 35 (anti-circumvention) and Article 40 (retaliation) has no clear provenance in the WTO Agreement. If not redressed or clarified, such ambiguities and inadequacies may lead to implementing difficulties. More importantly, they are likely to be challenged by other WTO members should China be admitted into the WTO.

Analysis of dumping and anti-dumping

No investigation has been initiated since the promulgation of China's anti-dumping legislation. We suggest that, before the law is enforced, China reconsider the good and the bad of dumping and anti-dumping. This is because plenty of research has revealed that anti-dumping may create more problems than dumping (Banks 1990; Cartland 1996; Gould and Gruben 1997; Hoekman and Kostecki 1995).

Why dumping?

Dumping often refers to an exporting firm's behaviour of selling at a lower price in a foreign market than it charges in other markets, most usually its home country (Lindert and Pugel 1996). According to Hoekman and Kostecki (1995), dumping may occur in the following circumstances:

1. when the exporter has to decide how much to produce before demand conditions or exchange rates are known or the exporter lacks experience in pricing a new product (sporadic dumping);

2. when the exporter practices price discrimination in different markets that are separated by barriers to re-importation of the dumped product back to the exporter's home market, in which situation the problem is the barriers rather than dumping;
3. when the demand is slack, such that it is perfectly rational for the firm to reduce prices to cover only average variable costs so as to stabilise its production over the business cycle and ensure job security (cyclical dumping);
4. when the firm prices its exports below production costs to minimise losses resulting from excess capacity which is maintained to deter entry by potential competitors into its home market (defensive dumping);
5. when the firm prices its exports below production costs on a long term basis to realise economies of scale or to attain full capacity utilisation or to move down its learning curve as fast as possible, in which situation dumping is part of a strategy to attain an optimal scale of production; and/or
6. when the firm is trying to establish market share quickly, in which case dumping may also be an effective competitive strategy (head-on dumping).

Generally, except sporadic dumping, dumping is part of normal pricing strategies of firms and is driven by market structures, business cycles or the characteristics of the products. As Banks (1990) put it, in most cases dumping is simply normal market behaviour. Anti-dumping proponents may still argue that dumping may be practiced with a predatory objective. That is, a foreign firm may deliberately price products low enough to drive existing domestic firms out of business and establish a monopoly. Once established, the monopolist could more than recoup its losses by exploiting its market power. Therefore, such dumping is detrimental to the economic welfare of the importing country. In practice, however, the fear about predatory dumping is unnecessary, because to achieve its predatory objective, the monopolist must not only eliminate all domestic competitors, but also be able to prohibit entry by new overseas competitors. In other words, it has to have a global monopoly or else be able to convince the host government to impose or tolerate entry restrictions, which is quite unlikely to happen. Furthermore, once the price goes up, the eliminated local suppliers could re-enter the market. Not surprisingly, rarely has successful predatory dumping case been documented in the postwar era (Banks 1990; Gould and Gruben 1997; Hoekman and Kostecki 1995).

Concluding the analysis, we find that there is little ground to blame dumping for a firm's difficulties in competing internationally. In any case, from the viewpoint of the importing country, when dumping does occur the lower-priced imports normally benefit the importing economy's, for it allows consumption gains from lower prices and a re-allocation of resources into areas of comparative advantage (Banks 1990).

Why anti-dumping?

Given that dumping is not so prevalent or evil after all, why there is there a need for anti-dumping action? For the industry in the importing country, the rationale is straightforward: anti-dumping has the attraction of being a "low-track" route for

obtaining protection against imports (Finger, Hall and Nelson, cited in Banks 1990) and can even be used as a weapon to harass foreign exporters (Arnott 1996). For the anti-dumping proponent policy-makers, the logic, explicit or implicit, is that for a certain product, there must be a *domestic* producer on the domestic market. Unfortunately, such a view seems narrow-minded in a liberalising trading environment. Starting from such a point of view, an anti-dumping action may most likely impede competition from foreign producers and, by protecting the inefficient industry, keep the country's resources in industries in which it may have a comparative disadvantage (Banks 1990). In some situations, anti-dumping may have become popular largely because of a weakening commitment to free trade (Messerlin and Reed 1995).

Anti-dumping has quite a few drawbacks. Firstly, it has strong protectionist flavour. As Banks (1990, p.16) notes, if protection is defined as "barriers to imports which assist a local industry to maintain a level of activity which it could not otherwise sustain", anti-dumping obviously could be classified as protection, or at least be said to share many of the attributes of pure protection (Gould and Gruben 1997; Hoekman and Kostecki 1995). In most circumstances, a reasonably competitive firm can well weather the impact of low-priced imports without being shielded by the government (Banks 1990). The high degree of administrative discretion in the anti-dumping system often makes it vulnerable to business and political pressures. Indeed, date requirements, time limits, normal value construction, price comparison can all be manipulated to achieve protectionist objectives (Gould and Gruben 1997).

Secondly, it is difficult to say anti-dumping is competition-minded because nothing is mentioned in the current legal framework about the anti-competitive intent or effect that a dumping may have. On the contrary, anti-dumping may often facilitate collusion between domestic import-competing firms or overseas exporters (Hoekman and Mavroidis 1994). A U.S. case well illustrates the situation where an anti-dumping action can quite likely produce anti-competitive outcome. In that case the petitioner, who was the sole sebacic acid producer in the U.S., captured the whole domestic market after foreign competition was wiped out by the anti-dumping duty. Conceivably, the price was driven up to a monopoly level (Dolack 1995).

Thirdly, anti-dumping legislation is also inherently discriminative in the sense that the same behaviour of a domestic seller and a foreign exporter are often subject to different disciplines. For example, under Australian law, selling at prices which do not recover full costs is not deemed unfair internally but is treated as the unfair trading practice of dumping internationally (Banks 1990).

Finally, anti-dumping action often brings about welfare losses to the importing country. The following Australian experience can shed some light on this. In the 1980s Australia took an anti-dumping action against imported fertiliser. While undoubtedly benefiting the local fertiliser industry, the action imposed substantial costs on the much larger and economically more important agricultural sector (Banks 1990). A

study by Gould and Gruben (1997) also observed that for each dollar gained by the U.S. industries protected by anti-dumping measures, the U.S. economy as a whole lost $3.6 on average. Sometimes, the existence of anti-dumping procedures per se can lead to pre-emptive price increases (a trade-deterrent effect) and incur welfare losses because foreign suppliers are not willing to offer their best price for fear of being charged with dumping (Banks 1990).

To sum up, anti-dumping is fundamentally flawed from an economic perspective, it is just a reflection of the political economy of international trade (Arnott 1996; Hoekman and Kostecki 1995). It contains inherent protectionist bias and by its nature is anti-competitive and discriminatory. In most cases, anti-dumping incurs welfare losses on the importing country as a whole (Anonomous 1996; Tharakan 1995). Anti-dumping may even pose a potential threat to the liberal trading order by impeding international competition and shifting world resources in wrong directions.

Anti-dumping in GATT/WTO

Not surprisingly**,** anti-dumping is often regarded as a major loophole in the GATT. In fact, anti-dumping is an option under GATT, namely, adoption and enforcement of an anti-dumping legislation is a right rather than an obligation: nothing in the GATT requires Members to promulgate and implement anti-dumping laws. The only obligation on Members is to ensure its anti-dumping legislation and its enforcement are strictly consistent with GATT/WTO Agreements (Hoekman and Kostecki 1995). The Uruguay Round attempted to address the above concerns. Although the GATT disciplines were tightened up in some ways (e.g. the sunset clause and the de minimis rule were added), the new Anti-dumping Code still falls short of what critics were hoping for (Grimwade 1996; Gould and Gruben 1997).

What is the future of anti-dumping? Since anti-dumping mechanisms are at heart about safeguarding the interests of particular industries, there will always be conflicts between anti-dumping policy and the broader interests of the national economy and the liberalising world trading order. Hence simply tinkering with the procedures and criteria for taking anti-dumping action, as people have done in the successive rounds of GATT negotiations, can only limit the protectionist bias but not eradicate this tension (Banks 1990; Hoekman and Kostecki 1995).

Aware of this, there have been increasing calls recently for reforming the current anti-dumping mechanism (Cartland 1996; Hoekman and Mavroidis 1994; Miranda 1996; Morgan 1996). Most researchers suggest that anti-dumping should be re-considered in a broader competition policy context. Basically two options are proposed: replacing anti-dumping regimes with competition policy; and recasting anti-dumping laws in some ways to make them more competition-friendly (Cartland 1996; Gould and Gruben 1997; Miranda 1996). In fact, the inclusion of a "national interest" provision was proposed during Uruguay Round (Arnott 1996). A working group has been

established under WTO to study the interaction between trade and competition policy, including any anti-competitive practices (WTO 1997).

In the foreseeable future, however, it is not likely that anti-dumping mechanisms will be completely replaced by competition policy on a global scale. Firstly, as tariff and non-tariff barriers are being lowered the lobbying for protection will focus increasingly on remaining protectionist measures of which anti-dumping is one that is GATT-legal (Hoekman and Mavroidis 1996; Gould and Gruben 1997). Ironically, anti-dumping may even be used to win some industries' support for trade liberalisation (Banks 1990). Secondly, consensus will not be easily reached soon on what substantive rules should be included in the uniform competition policy. But some competition-related considerations may be incorporated into the current regime. In the long run, nonetheless, the anti-dumping mechanism currently sanctioned under WTO will tend to be phased out and subsequently replaced by a set of uniform competition rules. This process may start from regional or bilateral arrangements, e.g. the European Union and CER between Australia and New Zealand (Hoekman and Marvoidis 1994).

Policy suggestions for the implementation of China's anti-dumping regulations

Given all the drawbacks of anti-dumping, the best option for China seems to be not to implement its legislation or, as Hoekman and Kostecki (1995) suggest, not to have the law at all. But, since the law is already in place and the pressure from domestic industries is mounting, most probably China's anti-dumping law will be enforced (Li 1997). Therefore, the question: now is how to avoid or minimise the possible negative effects and protectionist biases that may easily arise from the enforcement of that law. Failure to address this question may lead to extensive use of the anti-dumping mechanism, which would induce some industries (mostly inefficient ones) to rely heavily on the protection provided by anti-dumping actions. The potential danger is clear: resources may be mis-allocated and substantial interests may be vested in "wrong" industries. Such failure will also hamper the future reforming of the anti-dumping regime, while costing consumers dearly in the meantime.

Mindful of the negative impact that an anti-dumping measure may likely impose on the economy as a whole, we would like to suggest that Chinese anti-dumping authorities, before ordering an anti-dumping measure on the accused imported product, carefully calculate the *economy-wide* welfare effects of such a measure. Moreover, we would also like to suggest that the administering authority of competition policy (ie. the State Industry and Commerce Administration) be invited into the investigation process to determine the impact of such a measure on the contestability of China's domestic market, to see whether such measures would produce any anti-competition outcomes.

An example has to do with photographic film. As Shi (1997) revealed, China's film industry, which has been under mounting pressure from low-priced imports such as

Kodak, Fuji and Agfa for years, is considering filing an anti-dumping petition. Should the investigation be initiated, the authorities ought to consider the following: firstly, would the gain to the industry from an anti-dumping duty (plus the anti-dumping duty to be collected) outweigh the loss to over one billion consumers who could not enjoy the cheap (maybe better quality and service also) imported films any more? and secondly, would the anti-dumping measure substantially lessen the competitiveness of the Chinese film market or even drive all foreign competitors out and leave the market monopolised by a sole *domestic* producer?

The bad luck of a domestic industry can often be blamed on various causes. Hence, when implementing the anti-dumping legislation, China should ensure that factors other than dumping which are hurting the domestic industry are distinguished from dumping itself. Taking the above film example, in addition to the alleged dumping, smuggling and under-invoiced declarations also contribute to the low-price advantage of imported films (Shi 1997). Such problems must be dealt with separately. Anti-dumping is not an efficient way to cure such problems.

Moreover, the present institutional arrangement is also worth questioning. Firstly, since the authority of investigation into dumping and injury is split among MOFTEC, the CGA and the SETC, and the responsibility of determining the anti-dumping duty to be levied resides in the TCSC, efforts should be made to ensure that these agencies cooperate and coordinate effectively and that the law is implemented in a consistent manner. Secondly, since the SETC is charged with the responsibility for China's industrial sector, the findings of SETC might favour Chinese complaining industries. Therefore, when conducting injury investigation, the SETC should be particularly aware of this possible bias and keep alert to the influence of domestic interest groups.

Summarizing the foregoing suggestions, we propose some possible amendments to China's anti-dumping legislation. Firstly, a clearly-defined public or national interest provision is to be introduced. Interested parties that may be negatively affected by an anti-dumping measure (e.g. user-industries) should be explicitly allowed into the investigation process. (Such "national interest" provision can be found in Australian anti-dumping legislation – see Banks 1990.) An anti-dumping measure should be imposed only when the economy-wide welfare analysis demonstrates that advantages created by the measure for the economy as a whole outweigh the disadvantages. Secondly, it should be added in the law that the administering authority of competition policy has a role to play in anti-dumping proceedings. The effect of the alleged dumping and the anti-dumping measure on the contestability of the domestic market should be examined. Thirdly, some rules should be tightened, e.g. relaxing the de minimis percentage requirement, shortening the duration of an anti-dumping measure (sunset), or raising the initiation threshold to reduce the frequency of the use of anti-dumping.

Finally, we also put forward some suggestions from a long run perspective. As discussed above, the present anti-dumping provisions in the WTO will not stand still.

Competition policy may well be phased into the anti-dumping mechanism and eventually replace it. Thus China should keep abreast of this development and adjust its anti-dumping regime accordingly. Furthermore, China may take the initiative in existing regional settings such as APEC to speed up the phase-in of competition policy in place of anti-dumping.

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