

# WESTERN PERCEPTIONS

SO CHINA IS IN THE WTO; DO WE KNOW  
WHAT THAT MEANS YET?

BY DANIEL H ROSEN



**T**he long road and arduous debate over China's accession to the World Trade Organization is over. China has formally acceded to the Organization, and its obligations and commitments are beginning to take hold. And yet after the sixteen-year run-up to this momentous occa-

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sion, the implications of China's WTO membership are still largely misunderstood in the United States—not just by the general public, who can be forgiven for not following such a seemingly arcane event, but by many of those whose job it is to understand and explain what is happening in China. Intellectually, this is very interesting; practically, this is somewhat worri-

some. These misconceptions have a 'bipolar distribution'—they fall on opposite extremes of concerns about what WTO membership means for China and for the United States.



*Curiously anticipating the spectacle of international competition.*

Consider two examples of misconception that illustrate the dichotomy of misunderstanding characterizing US perceptions toward modern China. In one corner stands a “Coming Collapse of China” camp (from the title of a recent book by Gordon Chang); on the other stands a red-star-rising club fearing that we’re giving away the store. Let me review what each group argues and why each is mistaken, then offer a few observations on why this polarized tendency is so common in American sinology, and finally express my own expectations for the implications of Chinese WTO membership.

Many American political scientists, a few economists, and a smattering of business professionals have concluded that the economic liberalization implied by the terms of China’s accession to the WTO will impose too great a shock to China and

that a latent social unrest just beneath the surface will soon burst onto the surface. Some correctly note the causality between changes in the system of commercial regulation, administration and jurisprudence that China is now committed to imple-

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menting (and has already begun to change, with thousands of law modifications in the past six months) and spillover into political reform. Thus, they further fret that the Communist Party is totally incapable of responding to such spillovers peacefully. A significant subset of this group sees foreign-invested enterprises poised to destroy the weak state-owned enterprises under

cover of the WTO’s ability to enforce market access commitments. A common variant on this line is that China will manifestly refuse to implement the commitments it has negotiated for fifteen years precisely to avoid the apocalypse outlined above, becoming the rogue state of international commerce for refusing to pay its club tab.

The simplest way to lower the anxiety level that arises from the Coming Collapse camp is to review the course of Chinese economic reform over the past twenty years. In brief, China has gradually but very consistently reduced barriers to commerce (including international) and withdrawn distortions to domestic economic efficiency (like monopoly rights and intra-provincial trade barriers) for a long time. This has not been painless, but nor was it painless to deal with the social ills of a billion extremely



poor people in a stagnant economy prior to the decision to marketize in 1979. On the whole, the social and economic pains and challenges that have arisen under reform to displace the problems of poverty and stagnation from the prior era have been easier to address. And with dramatically rising income levels, more of the social responsibilities previously assigned to an inefficient government can be effectively shouldered by individuals and civil society instead. China's WTO obligations do not present a "step function" wherein sudden, dramatic redirection is required. Instead, the terms of accession by and large maintain—in a more formal way, importantly—the pace and trajectory of change that China has followed with increasing competence and stability for two decades.

A second point to bear in mind is that many of China's obligations are phased in over many years, some not fully imposed until 2010. This is not to say that China has not embraced a heavy schedule of front-loaded commitments; it has. But China's negotiators were not neglectful of weak sectors in the economy and did build in—with American sympathy and agreement—appropriate transitional terms for sectors (like agriculture) not ready for prime time competition. One benefit of the WTO is that it helps rationally minded Chinese technocrats to design adjustment for weak sectors using the least distorting means possible (both in terms of harming foreign commercial interests and in terms of addressing in a meaningful way the long-term interests of the Chinese economy.) For instance, non-tariff barriers are almost always more wasteful than simply defining the tariff and making it transparent. That often takes political effort, and without a WTO obligation most politicians fail to get around to dealing with such business when a "second best" policy is already in place. It's funny how

this is true in an authoritarian socialist regime as much as in a representative democracy. So WTO membership doesn't so much strip uncompetitive Chinese workers of all protection but rather force their designated representatives to stay at work a little later to work out a trade adjustment regime that is less costly to everyone else in their own economy and in economies that trade with them.

Finally, there is a tendency to extrapolate from the difficult economic adjustment experiences of other developing countries in Asia and Latin America to predict the risks for China going forward. And indeed, many developing economies have burst their seams in recent years and recent months. But there is actually a significant difference between China and many of these countries. China has decisively broken with the Japan-inspired development strategy of protecting domestic national champion companies while basing GDP growth on export-led growth. While vestiges of such an approach were apparent until the Asian Financial Crisis, they were largely cast overboard by serious thinkers in light of the bankruptcy of Keiretsu and Chaebol across northeast Asia. And Japan's decade long commercial coma is a present reminder to the new generation of leaders about to take the Chinese reins that this model of growth is outdated as the two dollars per minute international phone calls that some big national champion telecom companies try to sell. China is not a reluctant structural adjuster, doing just enough to stay out of WTO court while cynically trying to minimize foreign competition. Instead, a robust and earnest course of competition-led growth has been taken, and China's health and prospects are stronger for it. China will withstand heightened competition vis-à-vis WTO because it is committed and has benefited already in ways several richer neighbors have yet to know.

While the Collapse crowd writes obituaries for the rapidly modernizing China they once knew, their colleagues in the China Threat guild prepare us for a Communist menace strengthened

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commercially and military through more open trade, coming back at us like Japanese ships made of American steel to take away jobs, undermine our standards and ultimately threaten our security. It's actually a lot easier to refuse to deal with someone out of fear than out of pity, so not surprisingly more special interests opposed

to China's entrance to WTO piled into this camp—which makes for a polyglot caucus of interests. Here we have "blue-team" military analysts fearful of an aggressive China threatening US security and allies in Asia, environmental groups opposed to regime building that promotes economic development until firmer environmental restrictions are in place, labor interests concerned with competition from abroad that will undermine their bargaining power with corporations, and human rights lob-

bies concerned that a richer China means a richer and hence less constrained Chinese government more than anything.

It may be too much to address all these facets of the China Threat camp in US thinking toward China. But a few rejoinders are straightforward. Today, Chinese industry does not really threaten US jobs. Most US industry at risk of displacement by more efficient production in the emerging markets was shut down and moved between 1975 and 1990. Today, China is indeed taking jobs away from inefficient workers: but those workers are generally the ones in Korea, Taiwan, Japan and elsewhere who took the jobs from textile and steelworkers in the US twenty years ago. After all, it is important, indeed essential, to pay attention to the fact that WTO accession entails unilateral market opening by China, not a reduction of tariffs or other trade protection by the US or any other country. China alone opens! (The exception is that China gets to join the rest of the world's textile and apparel producers in the global reform of this industry over the next ten years, which means the elimination of quotas for US imports of textiles. But if China did not benefit from this increased US market access, approximately one hundred percent of its gains would instead be taken by India, Brazil, Thailand and the rest.) The only thing that will create more pressure on the US economy from China is a more competitive China, not a less protected United States. And indeed, the best economic modeling does suggest that China is reforming so much that its share of exports to the US will indeed rise for this reason.

A new US-China Security Commission is currently gearing up to ask the question, whether China's participation in the world economy will strengthen it militarily and undermine US security. It is true that economic modernization will mean a wealthier and more technologically sophisticated China, and hence the ability to upgrade militarily. But two further questions must be asked: what is the related impact on the Chinese government's control over national wealth and power and the use of that power; and to what extent would China's military be more constrained with China left outside the international trade regime.

The structural adjustment of the Chinese economy under economic reform has shifted the role of the Chinese government to an historic degree. The government has gone from controlling 99% of prices to a mere 10% or so in twenty years. From 100% of GDP coming from state owned enterprise two decades ago, over 60% of Chinese output today is from the private sector, and most new jobs and taxes at the margin are generated by the one and a half million private sector firms that populate China today (versus only one-hundred thousand in 1991). Bank loans are still disproportionately directed to the state owned sector, but that is finally shifting today. The arbitrary power of the government to control the actions of the productive sector of China is shrinking in order to make it more profitable, and the profits are increasingly withheld by the entrepreneur to reinvest based on returns instead of intermediated through the state for non-commercial goals. And in fact, if

economic proficiency is the goal, then there is really no alternative to this more hands-off stance. The Chinese government cannot both glom the profit of the economy for state aggrandizement and also have a domestic economy that is competitive in the world economy.

This is not to say that the current share of taxes harvested will not amount to more resources for military activity as the pie grows—it will. However, that would be the case were China left out of the WTO as well. As noted above, WTO does not radically change the direction of Chinese development; it makes it more predictable and more governed by rules. The efficiency gain to the Chinese economy by virtue of this rules-oriented tact might be a few percent a year—very significant, but not significant enough to change American strategic force doctrine in Asia from what it would otherwise be. Meanwhile, the tendency to administrative accountability has a profoundly moderating effect on the behavior of Chinese policymaking at home over the long term, and opens up tremendous room for American influence—direct and indirect—in the shaping of Chinese behavior.

Why are there extreme over-interpretations of the significance of China's WTO membership among American China scholars today? It is worth noting that this tendency has been constant in American thinking since the 1700s. Maybe it is because China is so far away from our shores, so seemingly impenetrable linguistically and culturally, and so overstated in its own rhetoric toward the outside world, that an exaggerated impression is often transmitted. Perhaps it is because many American sinologists are prevented from traveling to China due to limitations placed by the Chinese government on scholars who were critical in the past, leaving them at a disadvantage in doing first hand research. I believe it is only a minority of cases where commentators are certifiably negligent in their thinking or purely political in their motivations. Most are simply unconvinced of the profoundness of changes taking place in the private economy and understandably take from history the lesson that the past is



*Over China's acceptance: a line has been drawn.*

the best predictor of the future. And that is true: except for the punctuation points of history when sea changes occur and centennial tendencies are really altered. The changes taking place in China are more than centennial, in my opinion; they are millennial. The economic returns from a liberal system of society wherein self-correcting institutions (like elections, bankruptcy, audits, consumer advocacy, the right to withdraw money from a bank) are for the very first time in China's long history being developed today in a sincere way.

We should see the WTO in more modest terms, not as a determinant of Chinese military throw-weight or American manufacturing excellence, but as a narrow template for implementing rules, transparency and predictability on China's nascent but deeply rooted commitment to economic reform. The implication is that China will administer its domestic economy

in a more nuanced and careful way, taking due process and procedure more seriously. Locked-in to a restriction against arbitrary interference with commerce in order to protect local firms, China will work harder to engineer a marketplace that will bolster the strength of firms without a permanent lifeline to government bailout. For the United States, this is pretty good news. In the future, we can look forward to a China less likely to present an economic crisis or meltdown to the world, thanks to more earnest efforts to address structural adjustment at home; a more dependable center of world economic growth in East Asia in terms of consumption,



*Moving at an energetic pace, not just talking the talk.*

not just production; and a China impelled to take a greater leadership role in its region to try to assuage the risk of regional malaise that would effect it adversely. On this last point, China has already stepped up to pressure Japan more publicly for trying to hide behind a weaker Yen as an alternative to dealing with economic reform. Though China and the US must agree to disagree about a range of contentious issues, many of them symbolic, some of them deeply imbedded in principle, the US is likely to find China one of the most suitable candidates to be a co-proponent of structural adjustment and proactive economic reform in the Asian region. Visitors to China today from the business community quickly realize that Chinese don't just talk the talk on economic competition—they walk the walk. China has one of the most competitive domestic economies in the world. Sinologists might spend some more time with these business professionals, and see the meaning of WTO in light of the real marketplace conditions it is really all about. ■