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Working Paper

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Kieler Arbeitspapiere, No. 1194

Provided in cooperation with:
Institut für Weltwirtschaft (IfW)

Suggested citation: Langhammer, Rolf J. (2004) : China and the G-21 : a new North-South divide in the WTO after Cancún?, Kieler Arbeitspapiere, No. 1194, In: Institut für Weltwirtschaft, Kiel (Ed.), http://hdl.handle.net/10419/3133

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China and the G-21: A New North-South Divide in the WTO After Cancún?

by
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January 2004

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Abstract

The paper analyses the interests of China as a member of the G-21, which contributed to the failure of the WTO Ministerial Conference in Cancún/Mexico in September 2003. It concludes that the median member of G-21 is more inward-looking and less reform-minded than China. A failure of the Doha Round due to a North-South divide between the US/EU on the one hand and the G-21 on the other hand would cause more harm to the latter than to the former group and would also impact negatively upon China, which has fewer alternatives to a multilateral round than both most of the other G-21 members and the two big players. Thus, China would be well-advised to remain unconstrained in its trade policies and does not become member of any group.

Keywords: Multilateral trade policies, trade liberalisation, world trading order

JEL classification: Fo, F1

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I. Causes and Triggers of the Cancún Setback

Those not acquainted with the multilateral trading system must be puzzled by recent events and developments in the WTO system which are difficult to reconcile at first glance.

On the one hand, club membership in the WTO seems to promise net gains which are not achievable to outsiders. Otherwise it would be not conceivable why countries like China accepted painstaking and time-consuming questions-and-answers trials together with far-reaching concessions in all parts of domestic economic policy to join the club. Candidates like Russia and Saudi Arabia, to name the very few prominent outsiders, behaved similarly. Furthermore, the WTO as a legal device with an institutionalised dispute settlement mechanism (DSM) is unrivaled as witnessed by the high acceptance rate of decisions coming out of the DSM. Since 1995, when the DSM was introduced more than 200 complaints were filed and only very few went through repeated „slopes“ including the Appellate Body without consensus on the implementation of rulings and recommendations (WTO 2001: 27).

On the other hand, there is empirical evidence that the distinction between WTO membership and non-membership is not statistically significant for explaining the intensity of bilateral trade flows (Rose 2002) so that one might argue that non-members face similar conditions of market access as members. And above all, a mounting north-south divide seems to have breaken ground with substantial frustration in developing countries including emerging markets. Frustration has been fuelled by two factors. First, there has been slow implementation of Uruguay Round (UR) commitments in products of export interest to developing countries such as textiles and clothing. Second, developing countries felt under pressure of strong lobbying activities of vested interest groups in developed countries (including NGOs) to negotiate issues outside the core of market access. These issues are either labeled „non-trade concerns“ (environment, health, investment, social standards, competition) or are seen as a one-sided gain for developed countries only such as the „extraction of royalty payments“ (Bhagwati 2001) for protecting intellecual property rights under the TRIPS agreement. Southern countries had good reasons to presume that widening the negotiation agenda was part of a deliberate strategy of northern negotiators to prevent one-to-one trade talks in sensitive items as agriculture, subsidies and labour-intensive goods and to play divide-and-rule games.

Developing countries hesitantly agreed to start a new multilateral round before the commitments of the UR were fully implemented and enforced. Though this round was coined as a „development round“ (interestingly enough, by the EU and not the developing countries themselves), from the very beginning, frustration and scepticism dominated the preparatory meetings of the Doha Round (DR) on the side of developing countries. Lines of arguments among developing countries were by no means homogenous. Some developing countries like the Latin American agricultural producers closed ranks with agricultural exporters from the „north“ camp such as Australia and New Zealand in the Cairns Group which was already active in the UR. Other developing countries such as India and Egypt which do not figure prominently as major exporters and pursue more inward-oriented policies, dominated the group of „like-minded“ countries. Finally, least developed countries had neither resources nor much interest to take an active pro-trade part in the negotiations because they either feared terms-of-trade losses as net agricultural importers after the phasing out of export subsidies or worried about the erosion of their exclusive trade preferences with OECD countries (in particular the African countries).

In the pre-Cancún meetings, overlapping participation in both the Cairns Group and the „like-minded“ countries promoted the emergence of the Group-21 (G-21)[1] as the spearhead of resistance against what they criticised as the same procedure as in the UR: an implicit understanding of the EU and the US in compromising on their bilateral conflicts and in proposing a negotiation agenda which reflected common transatlantic trade interests. Two aspects supported the G-21 in their critics before they met in Cancún: First, the common EU/US negotiation proposal on agriculture which - viewed from the G-21 side - basically reflected the EU position of protecting the agricultural sector against excessive adjustment challenges and, second, the reference to the 1996 Singapore Ministerial Meeting where negotiations on competition, investment, trade facilitation and government procurement were agreed upon (so-called Singapore issues). The EU (together with Japan and insisted that these negotiations should be started in Cancún though both conceptually and strategically there were good reasons for denying that these issues belonged to the core WTO tasks rather than mirroring the interests of pressure groups in the EU.

**The author acknowledges critical comments and suggestions received from the participants of the Conference.*

[1] The G-21 comprises Argentina, Bolivia, Brazil, Chile, China, Colombia, Costa Rica, Cuba, Ecuador, Egypt, El Salvador, Guatemala, India, Mexico, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand and Venezuela. During the meeting, Turkey joined the Group.

The outcome of Cancún is well known. Negotiations were terminated by the Mexcian host without a result. The trigger of the Cancún failure was the dispute about the Singapore issues just when the EU seemed to compromise on dropping two of the four issues (investment and competition) while several African countries insisted that none of the four issues should proceed and the Rep. of Korea insisted that all four should proceed. Yet, the trigger of the failure was not identical with its cause. The Singapore issues were the iceberg of „non-trade concerns“ while the G-21 insisted on concentrating negotiations on the basic trade concerns such as abolishment of agricultual export subsidies in the EU and the US, the phasing out of domestic suppport to farmers in the two areas and alleviating market access in both industrial products and agricultural products. Causes of the setback were also rooted in the reciprocity issue. The US and EU demanded full participation of all developing countries in order to discourage freeridership whereas developing countries saw slow implementation of previous commitments in the EU and US as the bottom point to request unilateral liberalisation measures from the Big Two first. Mercantilist games underlying these attitudes can be described as the industrialised countries' view: „without reciprocity no concession“ and the developing countries' view: „without concession no reciprocity“.

It is a fact that the stalemate situation which emerged from mercantilist games was particularly applauded by the poorest countries without taking into account that they had more reasons to be concerned about the costs of the Cancún setback than other developing countries. Likewise, it is important to note that China was not among the frontrunners of those G-21 countries like India, Egypt, South Africa and Brazil which accentuated the dissense with the EU and the US and welcomed the setback (Schott 2003). Indeed, at the October 2003

Summit of APEC in Bangkok, the Chinese government reiterated the expectation of overcoming the dissense in the multilateral round and to bring the DR to a success.

Yet, to simply argue that Cancún was the typical mid-round crisis which also the UR had experienced with the failure of the 1988 Montreal Conference and the 1990 Brussels Conference neglects the importance of the formation of a developing countries' pressure group which did not yet exist during the UR. This group points to the importance of a traditional GATT-originating sin, i.e. the trade off in the system between allocation targets (MFN treatment and national treatment) on the one hand and distribution targets (special and differential treatment for countries „in the stage of development").

Mainstream economics express considerable doubts about how meaningful it is to anchor distribution targets in the WTO instead of concentrating them solely in development cooperation. Yet, mainstream economics also underline that welfare gains from liberalisation accrue from own market opening rather than from better access to export markets, but very few in trade diplomacy adhere to this view. Instead, the majority applaudes the infant industry protection argument to legitimise special and differential treatment and follows the mercantilist rule that imports cause adjustment problems while exports are outrightly beneficial. Given this view, one cannot neglect the formation of a pressure group simply because its underlying economic reasoning is rejected by mainstream economics.

Therefore, it is necessary to take the G-21 as a new pressure group and to analyse their likely impact upon the ongoing development of the Doha Round. In this respect, its homogeneity as well as possible conflicts between major actors in G-21 including China are to be assessed as well as its retaliatory potential vis-à-vis the Transatlantic Group (Section II).

Section III then discusses the alternatives which the major players have should the DR fail in order to assess the credibility of their endeavours to overcome the setback of Cancún.

Section IV addresses the self-interests of China to urge for a successful conclusion of the DR instead of adhering to the alternatives discussed in the preceding section.

One special aspect for China is the parallel debate on exchange rate protection which can, rightly or wrongly, backfire on trade policies especially of the US. This aspect is raised in Section V.

Section VI concludes on the results.

II. The G-21 Group as the Third Major Player: Common Interests For What or Against What?

Table 1 highlights characteristics of the G-21 countries with respect to growth of their foreign trade, the sectoral structure of their exports, their openness, their trade policy and their degree of restrictiveness concerning trade with abroad. Overall, an extreme extent of heterogeneity emerges. Group members comprise emerging markets as well as low-income countries, inward-oriented countries as well as very successful exporters of manufactures such as China and Mexico, large economies as well as small open economies.

Furthermore, the countries differ strongly in their trade policy orientation. Except for South Africa, India and Pakistan, the countries are either potential members of the Free Trade Area of the Americas (FTAA) or members of APEC or both. That means, that their links to the US as the only leading member of both groups is essential for formulating a policy in the DR which could be understood by the US administration as confrontation. Mexico and China are the two polar cases with respect to sovereignty on national trade policies. Mexico is a member of NAFTA and is free in determining its trade policy against non-NAFTA members since NAFTA is not a customs union. Yet, its dependence on exports to the US and the need to coordinate a number of trade-related policies with the US (such as rules of origin) make it highly unlikely that the country can support a confrontational G-21 policy against the US without incurring large losses due to retaliatory actions of the US and without damaging NAFTA. On the other hand, China is still one of very few WTO member states without any institutionalised regional or bilateral trade policy ties to other countries. For the time being, China is a pure MFN champion and therefore enjoys the freedom to choose its trade policies without coordinating them with other countries.[2] APEC is neither a free trade area nor a set of bilateral hub-and-spoke type free trade agreements. Ideas to conclude a FTA between China and the ASEAN Free Trade Area (AFTA) are neither concrete nor forthcoming for the time being since AFTA itself has not yet implemented free trade among its member states.

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[2] APEC is not a formalised free trade area like NAFTA and therefore has not been notified to the GATT as an Art. XXIV GATT exception. China’s trade policy sovereignty is not at all impaired or curtailed by its APEC membership.

Table 1 Trade and Trade Policy Indicators of G-21 Countries

	Share of exports and imports in GDP		Share in world merchandise trade				Growth of merchandise export volume		Change in product structure (share of manufactures in merchandise exports)		Freedom to trade index (Scale from 0 to 10)		MFN applied tariffs for non-agricultural products				
			exports		imports								Simple average	Coeffi-cient of variation	Maximum	Duty-free (per cent)	Year
	1990	**2001**	**1990**	**2001**	**1990**	**2001**	**1980-90**	**1990-2000**	**1968-70**	**1998-00**	**1990**	**2001**					
Argentina	11.6	17.5	0.36	0.43	0.12	0.32	5.0	9.3	13	33	4.3	6.1	12.7	0.5	35.0	2.4	2001
Bolivia	33.1	37.8	0.03	0.02	0.02	0.03	3.1	2.8	1	31	6.4	7.1	9.3	0.2	10.0	4.5	2002
Brazil	11.6	23.2	0.91	0.95	0.64	0.92	6.3	5.1	10	55	4.4	6.4	14.9	0.4	35.0	2.3	2001
Chile	53.1	52.2	0.24	0.28	0.22	0.27	9.1	10.0	4	16	7.2	8.3	7.9	0.1	8.0	0.7	2001
China	32.5	44.0	1.80	4.32	1.51	3.83	13.7	10.6	42	88	4.8	7.0	11.3	0.6	51.0	3.3	2002
Colombia	30.7	30.4	0.20	0.20	0.16	0.20	7.9	4.5	9	31	5.0	6.4	11.8	0.5	35.0	1.1	2001
Costa Rica	60.2	71.9	0.04	0.08	0.06	0.10	3.7	13.9	19	62	6.7	7.9	4.6	1.2	48.0	52.4	2001
Cuba	n.a.	n.a.	0.15	0.03	0.13	0.08	-1.1	-1.0	1	3	n.a.	n.a.	10.9	0.6	30.0	5.1	2002
Ecuador	42.8	54.5	0.08	0.07	0.05	0.08	7.1	6.3	2	9	5.8	7.0	11.5	0.6	35.0	2.1	2000
Egypt	36.8	17.1	0.10	0.07	0.35	0.20	2.1	2.7	27	41	3.6	6.1	19.4[3]	0.8[3]	135.0[3]	0.6[3]	2002
El Salvador	38.4	57.4	0.02	0.05	0.04	0.08	-4.6	2.9	31	48	4.8	7.4	6.5	1.3	30.0	51.9	2000
Guatemala	36.8	39.4	0.03	0.04	0.05	0.09	-1.1	8.5	25	33	6.1	6.6	7.1	1.3	28.0	51.4	1999
India	13.1	19.5	0.52	0.71	0.67	0.78	-3.0	2.6	52	78	4.1	5.7	30.5	0.3	105.0	0.8	2001
Mexico	32.1	54.2	1.18	2.58	1.24	2.77	15.3	15.5	26	85	7.4	7.3	17.1	0.5	35.0	0.7	2001
Pakistan	32.6	33.8	0.16	0.15	0.21	0.17	-0.3	-6.3	54	84	4.5	4.3	19.9	0.6	250.0	0.0	2001
Paraguay	43.9	43.5	0.03	0.02	0.04	0.03	12.8	-0.2	9	16	6.2	7.2	13.2	0.5	28.0	2.1	2001
Peru	25.5	29.1	0.09	0.12	0.10	0.14	2.7	9.3	1	18	4.4	7.3	13.1	0.2	20.0	0.0	1998
Philippines	47.7	88.9	0.24	0.52	0.37	0.49	-7.5	17.1	7	74	6.3	7.4	5.2	0.9	30.0	2.4	2002
South Africa	37.5[1]	50.9[1]	0.68[1]	0.48[1]	0.52[1]	0.45[1]	3.3[1,2]	7.4[1,2]	32[1]	54[1]	6.6	7.3	5.3	1.5	43.0	52.5	2001
Thailand	65.7	110.9	0.67	1.06	0.94	0.98	11.2	4.0	n.a.	n.a.	6.6	7.7	15.5	0.9	80.0	1.2	1999
Venezuela	51.1	36.4	0.51	0.45	0.21	0.28	3.4	5.3	1	13	6.9	7.0	12.1	0.5	35.0	0.7	2001
Median	**36.8**	**41.5**	**0.20**	**0.20**	**0.21**	**0.20**	**3.4**	**5.3**	**11.5**	**37.0**	**6.0**	**7.1**	**11.8**	**0.6**	**35.0**	**2.1**	

[1]Data refer to the South African Customs Union (Botswana, Lesotho, Namibia, South Africa, and Swaziland)

[2]Data are from International Monetary Fund's International Financial Statistics database.

[3]Indicates data sourced from UNCTAD.

Sources: World Development Indicators 2003. - World Trade Organization; Annual Report 2002. - Gwartney, James und Robert Lawson, Economic Freedom of the World, 2003 Annual Report, Vancouver. B.C. - World Trade Organization; 2003b.

In between Mexico and China as polar cases within G-21, there are members of bilateral or regional trade agreements which are either under considerable stress (Mercosur, Andean Group, Central America) or not functioning as the South Asian Association of Regional Cooperation SAARC (India, Pakistan). For all Latin American countries, in particular Brazil as a leading member of the G-21, the critical question is whether G-21 should be instrumentalised against the US and thus also inject tensions into the FTAA process. Hence, given these overlapping memberships, the majority of G-21 members (but not China!) have to assess whether a confrontational stance against the US in the DR will not impair their trade relations with the US either bilaterally or as a member of regional groupings. The probability is high that the US will raise this issue in bilateral trade talks, for instance, with Latin American countries in order to initiate a less confrontational strategy of G-21 or even to diffuse the pressure. In this respect, it is interesting to note, that shortly after the Cancún meeting and after bilateral trade talks with the US administration, some Latin American countries (Colombia, Peru) announced to withdraw from the G-21.

To less extent, these considerations also hold for relations between the EU and specific G-21 countries. South Africa (through membership in the EU-ACP agreement), and some Latin American countries (Mercosur members Brazil and Argentina, as well as Mexico) maintain institutionalised preferential or non-preferential trade relations with the EU. Yet, except for South Africa, the link is much weaker as for the US since the EU is neither a dynamic nor the most important trading partner. Thus, its retaliatory potential is smaller.

Differences in the degree of vulnerability against economic pressure of the two big WTO players is not the only and perhaps not even the most important dividing element in the G-21. Table 1 lists various structural performance indicators and trade policy characteristics which describe the state of openness, change in export supply and the degree of outward orientation in domestic trade policies. The latter can be stylised by the level of import protection which is an equivalent to an explicit export taxation. The breakdown suggests two conclusions. First, measured against a median G-21 country (last line in Table 1), leading proponents of G-21 such as Brazil, Egypt, India and South Africa have a relatively high level im implicit export taxation and thus are inward-oriented. Three of them (except for South Africa) offer less freedom to trade with abroad than the median country. Second, China is the clear outlier. It does not only expose the highest gains in world trade shares on both the export and import side among all G-21 countries. It has also been the most successful country in diversifying its exports from commodities toward manufactures; two sides of the same coin. During the nineties, progress in freedom to trade with abroad has been remarkable and was almost at par with the median G-21 country in 2001. It is only Mexico which rivals with China with respect to these performance figures.

Coming to the core area of dispute in Cancún, agriculture, there are striking differences in vested interests between net exporting Cairns Group members on the one hand and net importers on the other hand. As China belongs to the latter group, empirical estimates on the effects of liberalisation of agricultural trade do not suggest that this sector is as important for China under an export-biased view as for the Cairns Group members Brazil or Argentina. China, for instance, is a major importer of cereals (about 8 per cent of world cereal imports in the nineties and 13 per cent of developing countries' imports) compared to Argentina and Thailand (4 per cent each and 26 and 25 per cent, respectively). Should world market prices rise in the short run because of abandoning price support and export subsidies in the EU/US, China could incur welfare losses (Francois, Weijl, van Tongeren 2003: Table 4.1). The country would gain from better market access to the OECD markets in those agricultural products it exports. Medium term gains from incentives to increase domestic production are less certain as the costs of expanding agricultural production by drawing productive resources from industrial sectors which show increasing returns to scale (while agriculture is a constant returns to scale sector) should not be underrated (ibid).

There are two further political economy arguments in favor of diverging vested interests between China and other G-21 countries.

First, any liberalisation of textile and clothing trade in the DR contributes to release Chinese presence in world markets for textiles and clothing and to exert pressure upon low-income developing countries in South and Southeast Asia which are specialised in producing substitutes to the Chinese supply.[3] If they are not advanced in producing intermediate manufactures to be exported to China as a result of increasing domestic demand such as textile machinery, they could suffer from terms of trade losses due to a DR „with China". It cannot be excluded that some countries in Southeast Asia are responsive to sector-specific lobbying

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[3] The impact of Chinese WTO accession for Asian regions has been empirically portrayed by Ianchovichina et al. (2002) and Francois and Spinanger (2002). Further lifting of textiles and clothing tariff and non-tariff barriers in the DR would lead to further pressures on world market prices due to the fact that tariff peaks are still most prominent in this sector. Wang (2003) shows that while Asian newly industrialised economies would benefit from the accession due to the expansion of world trade and ToT improvement, some countries in Southeast Asia would experience more competition in labour-intensive exports and lower prices for their products. Again, these are first-round terms of trade effects which do not take into account second-round dynamic effects.

against the conclusion of a Round which is feared to hurt them in the short run.

Second, interestingly, it is not even clear that the short-run effects of the outcome of the DR based on terms of trade effects are positive for China. The empirical estimates have been ambiguous. On the one hand, Francois et al. (2003) conclude based on Computable General Equilibrium (CGE) modeling that the one region which consistently and significantly is hurt by manufacturing liberalisation (the most important sector relative to agriculture and services) is China. Its terms of trade are eroded driven by expansion of textile exports and decline in prices and furthermore by increased competition from other low wage countries, in particular from India. Trade and income effects arising from intensified competition with low wage countries are expected to yield downward pressure on Chinese wages. On the other hand, Dessus et al. (1999) show (again based on CGE modeling) that China would benefit from multilateral tariff liberalisation in terms of welfare gains equivalent to 5.5 per cent of its GDP. The latter estimates include endogenous total factor productivity gains and thus concentrate on dynamic effects which go beyond static terms of trade effects assessed to be always smaller than the dynamic effects. Anderson and Yao (2003: Table 8) support the distinction between short-run terms of trade losses for China due to removing remaining post-UR distortions against merchandise trade (equivalent to a Doha Round) on the one hand and dynamic medium terms welfare gains due to higher resource use efficiency. Though, the latter gains are higher than the former losses, Chinese policy makers familiar with these estimates could give priority to the short run income effects and therefore prefer a „slow go“ attitude. Such attitude would support a „sequencing“ of policies, that is first to manage the effects of WTO accession on the domestic economy, second to wait until the transition period for full implementation of WTO rights for China has passed (until 2008) and only in third place support a new round of multilateral trade liberalisation. This gradualism would be much more cautious and defensive than the outright pressure of Cairns Group members in the G-21 for dismantling of domestic subsidies in the agriculture sector, for alleviating market access and for abolishing export subsidies.

To sum up, G-21 countries are a fragile pressure group with highly diverging interests. Given its unrivaled role as both an export giant (Dutta 2003) and highly absorptive import market, China does not represent the median country in the Group which is less dynamic and more inward-oriented. It is open to debate (in fact, it can be questioned) whether Chinese interests would be furthered if the country would follow an uncompromising stance of a median G-21 country.[4]

III. Alternatives to the Doha Round: Which Actions Might Major Players Take?

The DR has suffered a severe setback but not yet a defeat. Negotiations will continue though with more uncertain outcome than before the Ministerial Meeting. Yet, one cannot deny that a continuous liberalisation track stretching breaklessly from the implementation of the UR commitments by the end of 2004 to the beginning of further liberalisation steps under DR commitments by early 2005 is at risk to say the least.

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[4] China's role in the G-21 during the Cancún meeting has been recognised as moderate and passive (Schott 2003). This raises the question whether the country sees its interests well represented by the leading proponents of an uncompromising stance against the EU and the US.

The essential imperative is to fix an understanding between G-21 and the EU/US which state of negotiations from Cancún should be taken home to start with new negotiations. This refers to the Singapore issues which in the view of G-21 should be dropped at all but at least three of them (except for trade facilitation). As concerns agriculture, the understanding should be feasible as the Meeting did not break over agriculture but other issues. It is in this sector where a time limit has to be taken into consideration, the so-called „peace clause“ from the UR under which WTO member states refrain from dispute actions against other member states, primarily the EU, on subsidy issues. Should member states argue that the EU was the major actor responsible for a non-agreement on agriculture, the Cairns Group and G-21 countries could put the EU in legal jepardy and thus aggravate tensions unless the EU could buy extension via more concessions offered (Thompson 2003). The earlier the „bicycle will move again“ in the presupposed direction of a single undertaking for the entire round, the less attractive will be the alternatives for the major actors.

Yet, these alternatives do exist, mainly for the EU and the US, to some extent for Latin American G-21 countries but only weakly for Asian G-21 countries including China.

Alternatives for the EU

Traditionally, the EU has been both the inventor and the multiplier of regionalism. The majority of „effective“ (in terms of workable) regional trade agreements (free trade areas, customs unions or common markets) notified at the WTO has some involvement of the EU. They are mostly so-called bilateral hub-and-spokes-agreements with the EU as the hub and the partner countries as the spokes which do not share the same preferential trade relations among each other as the EU does. Yet, with the beginning of the nineties, EU regionalism has changed in two ways (Langhammer 2003). First, the EU concluded free trade agreements beyond Europe (such as with Mexico) and these agreements could no longer be legitimised as a training field for future full EU membership. Therefore, today questions of WTO compatibility (Art. XXIV GATT) are even more at stake than in the past. Second, the EU started to negotiate agreements with a group of countries, the Latin American Southern Cone Group Mercosur and thus departed from the hub-and-spoke type. The latter new form of regionalism requires a minimum of regional policy sovereignty in the partner group which seems to exist in Mercosur though unilateral trade policy changes in the Argentina-Brazil relationship have undermined the credibility of Mercosur. These negotiations are reported to be difficult given the EU restrictions on agricultural products and the deliberate policy target of Mercosur just to remove these barriers. Hence, in a nutshell, EU-Mercosur negotiations mirror conflicting views in the EU-Cairns Group context at the multilateral level.

The EU would be in a position to accelerate this new type of regionalism, for instance, in the Mediterranean region, with new arrangements in the Middle East and Central America, and finally, also in Southeast Asia where there is a non-preferential agreement with ASEAN since 1980. Stumbling blocs against an easy proliferation of EU regionalism beyond the European continent are EU claims for minimum requirements of respect for democratic rules including human rights in the partner countries. Asian partner countries have always insisted on separating economic and political issues in bilateral agreements thus excluding any political concession to the EU from the economic agreements.

Another EU alternative to the multilateral round reflects a longstanding position of some EU member states, notably France, i.e. to deepen EU internal integration without a parallel initiative toward extra-area liberalisation. To some extent, this inward orientation is prescheduled. The EU enlargement toward ten Central and Eastern European countries (CEECs) in 2004, the implementation of the ambitious Lisbon targets to become the world center of innovation by 2010, the reform of the budget and the common agricultural policy as well as working on the political integration in tailoring a reasonable division of labour between Commission, Ministerial Council and Parliament in a constitution will absorb so many financial and governmental resources that the interest to revitalise the WTO process could fall behind. Seen as an entity, the EU has become as inward oriented as the US.

Finally, the setback of Cancún can refuel joint transatlantic trade policy initiatives. Given the extraordinarily intensive mutual linkages in foreign direct investment on both sides of the Atlantic, companies can act as pressure groups to harmonise policies in competition and investment to their benefit. Even more importantly, more companies can prevent an escalation of retaliatory actions arising from DSM decisions either against the US or the EU. A de facto transatlantic free trade area could have sizable trade-diverting effects to the detriment of outsiders including China (Langhammer et al. 2002).

Alternatives for the US

The Bush Administration has increasingly given regionalism higher priority in its trade policy and ranks close to multilateralism. So-called „competitive regionalism“ is motivated by the belief that US trade policy interests should be enforced in two ways once multilateral trade negotiations would fail. First, hub-and-spoke type arrangements with individual countries should include areas of special export interest to the US, for instance, in services. Second, the hemispheric Free Trade Area of the Americas (FTAA) should encompass all Latin American countries plus North America. The post-Cancún situation points to the former rather than the latter way. The FTAA includes all Latin American countries which in Cancún were most critical against specific US trade policies, for instance, in agriculture. Such critical stance can be duplicated in the FTAA as has already emerged in diverging views between the US and Brazil. The former way has already been chosen in bilateral Free Trade Agreements between the US on the one hand and Singapore as well as Jordan on the other hand. Further agreements with Asian countries are in the stage of negotiations. They allow for meeting special US political objectives (such as cooperation in security issues) and liberalise trade in services which are specific export interest to US service exporters.

Alternatives for China

Both, the US and EU alternatives point to regional or bilateral agreements as a viable alternative to multilateral negotiations should these negotiations end in a stalemate. Note that the viability is seen from an individual country perspective and not from a world welfare point of view. The US and the EU are large economies with considerable economic, financial and political leverage and can enforce their interests in bilateral negotiations. This is not to say that smaller partners do not benefit from negotiations which are not at level playing field. The „new regionalism" just argues that smaller countries liberalising multilaterally first and then docking on to successful regional schemes with an institutional setting which promises economies of scale can benefit from joining a „club" (Ethier 1998). The CEECs in Europe and Mexico within

NAFTA are examples of such sequencing of policies with „multilateralism first and regionalism later".

Yet, for various reasons, it is very much debatable whether such alternatives are available for China, for instance.

First, there is the option of south-south regionalism, for instance, between China and Southeast Asian countries linked in the ASEAN Free Trade Area (AFTA). The standard trade theory workhorse Heckscher-Ohlin-Samuelson (HOS) theory based on factor endowment suggests that such regionalism widens the income gap between the poorest member state (with unskilled labour as the most abundant factor) and the richer member state with a factor endowment where unskilled labour is less abundant). The poorer countries would suffer from trade diversion because imports formerly supplied by non-member states would now be supplied by member states. The poorest country would have much less opportunities to increase its exports to the richer partner country (Venables 2003). The history of south-south integration in Africa and Latin America offers a rich source of experiences of conflicts on so-called equitable distribution of benefits from integration. Disintegration measures were mainly due to distributional conflicts. Due to its vast scope of richer and poorer regions inside the country, China's potential record from south-south integration cannot be easily assessed. In free trade with ASEAN, for instance, advanced ASEAN countries as Singapore and Malaysia would be able to substitute for sophisticated manufactures which formerly were imported from countries outside the China-ASEAN area. On the other hand, China would benefit from exporting to the poorer members of PR Lao, Cambodia, Vietnam and Indonesia to the detriment of third country suppliers. Yet, such trade diversion is known to be welfare decreasing and should therefore be minimised. South-south integration, however, is inherently trade diverting. It is a side aspect that AFTA is far from being complete and that various non-tariff barriers will continue to exist even if tariff barriers in intra-AFTA trade have been dismantled. Furthermore, a China-AFTA Free Trade Area would have to cope with the problem of trade deflection, i.e. the circumvention of Chinese tariff borders by transshipping imports through a low tariff ASEAN country. Singapore, a near free trade area, would be the ideal candidate. To discourage such practices sophisticated rules of origin would have to be introduced and enforced. More often than not, these rules are highly protectionist (World Bank 2003b: Box 3.8).

In general, tariff barriers in south-south trade are much higher than in south-north trade. This holds particularly in agriculture where they are often twice as high as high as those tariffs imposed by the OECD countries (ibid: 82). Moreover, production structures are often substitutive rather than complementary. Therefore, barriers are politically difficult to remove. And finally, poorer countries rely on tariffs as a major fiscal revenue and thus oppose dismantling if there is no alternative to financing the budget.

China will have to meet each of these impediments when negotiating regional or bilateral agreements with developing countries. Most of these countries probably fear China's competitiveness. As the rule of thumb, they will be the more reluctant to „go regional“ with China the less they see opportunities to penetrate the Chinese market. These are definitely the low-income countries which fear trade diversion and losses in tariff revenues from free trade with China without being compensated on the export side.

North-south regional trade agreements both from the theoretical HOS point of view as well as from the CEEC-EU and Mexico-US/Canada experiences offer the best alternatives of docking on to a large „natural“ neighbouring market. At first glance, a Japan-China trade agreement possibly supplemented by the Rep. of Korea appears as the Asian version of the European and North American type of north-south integration. Yet, the first glance is misleading. It can be shown that the discrepancies in all areas of trade policies between Japan and China are still much too large to be bridged without welfare losses, safeguards, rules of origin and other bureaucratic red tape (Langhammer 2001). Following the recipe of new regionalism, China requires just the prerequisite of multilateral liberalisation first before entering into a free trade agreement with an industrialised country. This would hold for a China-NAFTA agreement as well[5] but not for the APEC Bogor targets (intra-APEC free trade by 2010 for developed countries and in 2020 for developing countries) provided that they would really be open to non-members as the defenders of „open regionalism“ have argued. Nonetheless, a multilateral trade agreement appears superior to either open regionalism or bilateralism.

In this respect, it is essential to differentiate between regional integration and regional co-operation. The former aims at removing barriers to trade and factor movements within a region (therefore sometimes labeled „negative“ integration) while the latter concentrates on joint actions and

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[5] This is a purely economic view which neglects political tensions in Northeast Asia. From a post-WWII European perspective, one is reminded of the situation in the early fifties when discrepancies between national trade policies of the West European countries were large and political considerations to tie the former political enemy into a set of regional treaties with economic integration as a vehicle for future political integration (Langhammer 2001).

projects („positive“ integration). Based on the experience of other regions, Langhammer (2001) argues that China and the entire Northeast Asian region could, substantially benefit from regional co-operation with joint projects in cross-border issues like maritime research, preserving fish stocks, fighting regional environmental pollution problems, common cross-border services like coast guards, and harmonising rules for cross-border flows of capital, labour and individual persons.[6]

IV. The costs of „Non-Doha“: More Vulnerability and Uncertainty for China

The preceding discussion has shown that unlike the EU and the US, China (and other Asian emerging markets) has fewer alternatives to gain safe access to export markets outside the multilateral system. Regional trading arrangements and bilateral agreements are imperfect substitutes to a multilateral agreement unless they include the EU, the US or Japan as the major markets for more advanced manufactured products. Overall, a failure of the DR would expose China’s economy in general and its manufacturing sector in particular to costly vulnerability and uncertainty. Under this heading, a number of issues can be discussed.

1. Market access

One of the „evergreen“ aspects of market access are tariff barriers. While they have on average been reduced to 4-5 per cent levels in OECD

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[6] Such joint projects are of course aslo feasible in relations between China on the one hand and US or EU on the other hand. At the October EU-China Summit, common projects were discussed. Yet, given the geographical remoteness between the two regions, the scope of cross-border common projects is more limited than within a group of neigbouring countries in the Northeast Asian region.

countries for industrial products originating from low-income countries, averaging hides tariff peaks which plague just those developing countries which either specifically supply goods subjects to such tariff peaks or generally supply goods in downstream industries at the end of the processing stage. The maximum tariff of the EU for non-agricultural products, for instance, is 26 per cent (WTO 2003b: 206). The reason is that nominal tariffs usually rise with increasing stage of processing in order to protect domestic valued added in labour-intensive final consumer goods. In technical terms, the effective rate of protection exceeds the nominal rate of protection the more the larger is the difference between the nominal tariff rates on final goods and intermediate goods. China is the prototype of a supplier suffering from such tariff escalation. This is why China proposed a tariff-cutting formula that would sharply reduce tariffs and reduce high tariffs relative to average tariffs (World Bank 2003: 91) For instance, using the Chinese formula, the EU initial average applied tariff imposed upon imports from low-income countries such as China would decline from 5.3 per cent to 2 per cent (ibid: Table 2.11). A DR failure would leave China with the burden of the tariff escalation.

Textile quotas are the other major barrier to market access for China. Though the abolition of quotas by 1 January 2005 has already been negotiated in the UR and therefore correctly should be treated separately from the DR, it is evident that industrialised countries (ab)used the options of the textile commitments to delay the abolition of quotas. It is estimated by the World Bank that by the beginning of the third stage of phasing out quotas in early 2002, about 85 per cent of the effective quotas against developing countries were not yet abolished (ibid: 79). It cannot be excluded that industrialised countries will invoke general safeguards (and perhaps special safeguards against Chinese exports in the transition period after WTO accession) in order to further delay the process. A DR failure due to north-south tensions could fuel such attitude. How restrictive quotas are still for China is exemplified by the high share of clothing exports to non-quota markets in total Chinese clothing exports in 2001 (almost 80 per cent; see ibid: Figure 2.8) Abolishing quotas would lead to rapidly shifting exports to former quota markets and expanding exports in general. As, however, trade is not a one-way flow, an expansion of textile and clothing production would stimulate imports of China in capital goods, for instance, textile machinery, as well as intermediate (fibres, yarn) and thus in particular would benefit more advanced neighbouring countries in Asia, such as Japan, Taiwan, China, Hong Kong, China and Rep. of Korea. (Ianchovichina et al. 2002, Francois, Spinanger 2002).

2. Efficiency in resource use

It was discussed above that CGE model results suggest that short run terms of trade losses due to the dismantling of trade restrictions in the DR would be outweighed by medium-term efficiency gains. Net gains are estimated in the range of 9 Bill. US $ per year by 2005 in 1995 dollars; about 4 per cent of total world gains (Anderson, Yao: 477). This is a magnitude which neither can be neglected nor substituted for by other measures. It would help China to internally integrate the poorer provinces of the country and to raise their income relative to economically leading provinces located along the coast. Especially, the high share of the non-traded sector in the economies of hinterland provinces would decline thus offering potential for productivity gains and real income increases for the poorer parts of the population.

3. Anti-dumping measures

A recent report of the WTO Secretariat for half year 2003 lists China with 12 anti-dumping (AD) investigations (out of 79 in total) at the top of the list of defendant member states subject to investigations. Traditionally, China has mostly topped the list though in general the total number has been on the decline (in first half 2002, 21 investigations were filed against China). China itself launched 11 investigatons against other member states in first half 2003 (WTO 2003a). Definite anti-dumping duties raised by China against its trading partners before 2002 ranged between 27 and 50 per cent and were far lower than duties raised by some Latin American countries at 3-digit levels (World Bank 2003: Table 2.10). Such discrepancies witness that AD duties are often discriminatory. The other negative effect is uncertainty. Investigations, even if they do not lead to ultimate anti-dumping duties, have a highly distortive effect as they fuel uncertainty during the period of investigations when provisional measures are taken. Moreover, there is a vast body of literature which witnesses the protectionist abuse of AD measures: in many cases, there is no „predatory“ dumping. The costs of dumping for the income of consumers and the competitiveness of downstream industries of intermediate and commodities[7] (cascading effect) are underrated or even neglected and the measurement of AD margins is often arbitrary if prices in reference countries are taken as a yardstick. In total, AD has become the most widely abused „grey measure“ against exporters.

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[7] Intermediates and commodities (such as basic chemicals, base metals, plastics) are the most heavily affected industries.

Any successful conclusion of the DR would also include reforms of the AD agreement because of the single undertaking principle that forbids „raisin picking“ and commits all members to approve decisions taken on all sub-issues and their agreements unter the WTO umbrella. Thus, China has the chance to remove protectionist tendencies from the AD agreement only if it concludes on the entire DR.

4. Safeguard measures and dispute settlement procedures

The discipline of the WTO relative to the GATT has been strongly improved by the introduction of a more binding dispute settlement mechanism which enables the WTO to pinpoint violation of the rules and to identify the member state which is responsible for violating the rules. Furthermore, resorting to safeguard clauses has been conditioned to clearer preconditions in order to avoid that domestically rooted weaknesses of an industry are taken as the starting point of actions against trading partners (see the recent decision of the WTO in the US-EU steel trade dispute against US safeguard measures and in favor of EU countermeasures). China participates in the safeguard notifications by responding to questions posed by WTO member states on the implementation of its safeguard regulation (according to Art. 12.6 of the safeguard agreement (WTO Document G/SG/Q1/CHN/12 of 20 Oct. 2003). It also requests to be informed in third country safeguard measures such the EU/US steel import dispute (see WTO Document G/SG/Q2/CHN/4 of 17 Oct. 2003) as third parties become directly or indirectly affected through changes in international trade flows and prices if two parties clash on safeguards.

The same holds for dispute settlement. Apart from direct involvement as respondent China can and has already made use of its rights to be included in third party conflicts such as in the dispute between the EU and the Rep. of Korea on the alleged subsidisation of Korean ship production (WTO Document WT/DT301/2 of 17 Sept. 2003) and in the US/EU steel trade dispute where China has joined the group of successful complainants against US safeguard measures against steel imports.

Beyond the unquestioned benefits of the WTO DSM, there is undeniable demand for improvement especially with respect to the extent of implementation of decisions and the timespan required for complying with decisions of the DSM panel. Thus, it is China's self interest that such reforms are accelerated before the country itself becomes subject to complaints. In the international arena, there is no substitute to the DSM.

V. „Jobless Growth" and „Exchange Rate Protection": Threats for China's Export Base in the Absence of a DR

It is not only due to the US election year 2004 why China has become increasingly confronted with complaints which in the 1980s were already raised against the Rep. of Korea, Taiwan China and Japan. In fact, allegations of „beggar thy neighbour policy" or deliberate undervaluation of Asian currencies has been for long on the agenda of conflicts across the Pacific Rim. The question has always been whether Asian countries manipulate their exchange rates and their macroeconomic policy in favor of the tradable goods sector by raising prices for these goods relative to non-tradables such as services with a high labour content or vice versa by suppressing the rise of prices in non-tradables such als labour costs (real devaluation). Without going in too much detail, there is consensus in literature (Corden 1985) that a devaluation is neither necessary nor sufficient to sustain a deliberate policy of exchange rate protection. Nor is a bilateral trade surplus of a country against the another country an indicator for exchange rate protection of the former. The key indicators in favour of assuming that exchange rates are manipulated are monetary and fiscal instruments which are targeted to suppress domestic absorption so that absorption is lower than it otherwise would be. It is also acknowledged that to sustain exchange rate protection over a longer period requires companion policies such as capital controls to prevent capital inflows which are attracted by a high interest rate policy. Such policy could be part of sterilizing capital inflows (the analogy of a trade surplus) and be necessary to prevent domestic absorption from rising. Such a companion piece does exist in China but seemingly is not used as a sterilising device.

It is not evident that China has pursued an exchange rate protection strategy for a long time. Domestic absorption is high as witnessed by the rapid rise of imports. Furthermore, the Chinese trade surplus with the US is relatively low (relative to cases like Japan and Taiwan China in the eighties).

Yet, as long as the US runs an overall current account deficit, vested interests will argue that this deficit has not its roots in US domestic policies but in mercantilist strategies of countries which implicitly subsidise their exports and thus export unemployment to the US. China is the only G-21 country which is confronted with such attacks and thus again shares other self-interests than the typical inward-looking G-21 median country.

For three reasons, it can be assumed that a conclusion of the DR is instrumental to diffuse protectionist threats from the US (and/or from other OECD countries' side) against China. First, the DR would strengthen intellectual property rights and thus induce further US technology transfer inflows into China and/or draw implicit royalities out of China to the benefit of the US. Second, the DR would both specify Chinese commitments to further open the market and to secure the export base. Chinese economic growth which essentially hinges upon imported technology could thus be stabilised and remain a major absorptive power in world demand. Sole reliance on US demand as a locomotive could be prevented with positive effects on containing the US current account deficit. Third, the DR would help China to make its financial sector more competitive and to facilitate economic restructuring of state-owned enterprises. With the advancement of such process, the exchange rate regime and the convertibility regulations could gradually approach the standard of market economies.

VI. Concluding Remarks

Seen from Europe, Chinas plays an important role in giving a new momentum to the DR and to save the WTO from a post-Cancún stalemate trauma. Yet, to play this role, it is crucial for China that it does not join any „South“ coalition in controversy against the „North“. It has been shown that the typical G-21 median country is relatively inward-looking and thus tempted to revitalise such conflicts which we know from the seventies. China would be a strange bedfellow in this group. Its own interests make it a separate player for various reasons. First, its alternatives toward regional integration are very much weaker than those available to the EU, the US or the Latin American economies. Second, it is exposed to the restrictions and uncertainties of the transition period in becoming a „normal“ WTO member. This holds especially for sensitive industries like textiles and clothing. An early harvest in the DR would stabilise the Chinese export base and guarantee full implementation of the UR commitments of dismantling all quantitative restrictions in textiles trade. Third, the DR would lower peak tariffs and remove one of the most damaging elements of the tariff structure for developing countries, i.e. tariff escalation. China as a typical finished goods producer in the labour-intensive segment would especially benefit from declining tariff escalation. Fourth, it secures access of China to state-of-the art technology as the „single undertaking“ procedure would commit China to fix intellectual property rights protection further. Without such further protection, technology-intensive FDI in China would not be induced. Fifth, China needs the WTO discipline in safeguards, DSM and AD measures in order to be protected against unilateral pressure. The existing framework needs improvement as recent sageguard and DSM cases have shown. Finally, China is not directly involved in the conflict between „true“ agricultural exporters (Cairns Group), „subsidy-driven“ exporters (EU), „free trade scenario“ net importers (Japan) and technology-intensive agricultural exporters (US). To conclude, given China’s economic size and leverage both on the export and import side, a stronger voice of China pro-DR would have a valuable pump primer effect for a new start.

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