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China's Long March to a Market Economy

The Case for Permanent Normal Trade Relations with the People's Republic of China

by Mark A. Groombridge

Executive Summary

The U.S. Congress is in the historic position of being able to help pro-reform leaders in China move their country in a market-oriented direction. A vote to grant China permanent normal trade relations (PNTR) status will bolster the position of those leaders in Beijing who are attempting to deepen and broaden the scope of China's two-decade experiment with economic reform. Granting PNTR and China's subsequent accession to the World Trade Organization will benefit, not only the United States and the world trading community, but most directly the citizens of China, millions of whom are still mired in abject poverty.

Granting PNTR to China will enable U.S. companies to take full advantage of the market access provisions that China has agreed to adopt in order to comply with WTO rules and obligations. Import-using businesses and consumers here in the United States will also have better guarantees that low tariff rates will continue to apply. If Congress does not extend PNTR to China, China can still enter the WTO and extend benefits to competitors in Europe and Japan while denying them to U.S. companies.

Nontrade issues will and should remain an important part of the U.S.-Chinese relationship, but the annual debate on whether to extend normal trade relations is an ineffective tool for influencing China's long-term behavior. As a member of the WTO, China will be subject to a multilateral dispute settlement process that is likely to be far more effective than sanctions imposed unilaterally by the United States.

Ultimately, Congress should ask a straightforward question: *Is it in the U.S. national interest to encourage China to liberalize and reform its economy in a more market-oriented direction?*

The answer is a resounding yes. A vote in favor of extending PNTR to China is a vote for reform of the Chinese economy. It is also a vote for U.S. business and citizens who will reap the benefits of expanded U.S-Chinese trade.

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The present annual debate on whether to extend NTR is neither an effective nor an appropriate tool for influencing China's long-term behavior.

Introduction

The vote on the extension of permanent normal trade relations (PNTR) to the People's Republic of China is one of the most important decisions the U.S. Congress has faced on international trade–related matters in the past decade. While China itself ultimately controls its own economic and political destiny, the United States is in a historic position to assist pro-reform Chinese leaders who have agreed to adopt sweeping economic reforms in return for accession to the World Trade Organization, the multilateral institution governing international trade. China's accession to the WTO will help move the country in a more market-oriented direction. This benefits, not only the United States and the world trading community, but most directly the citizens of China, millions of whom are still mired in abject poverty due to tragic policy errors made by China's leadership in the past.

The arguments against extending PNTR and China's ultimate accession to the WTO are many but spurious. Some observers suggest that the annual review of the extension of normal trade relations (NTR) with China is the only leverage we have over China's economic and political behavior, that China will not abide by the rules of the WTO after accession, and that U.S. jobs will be lost because of a flood of Chinese imports.

Although nontrade issues will and should remain an important part of the U.S.-Chinese relationship, the present annual debate on whether to extend NTR is neither an effective nor an appropriate tool for influencing China's long-term behavior. China is more likely to abide by multilateral WTO agreements that enjoy broad international legitimacy than by bilateral agreements that are inherently much more politicized. As a member of the WTO, China will be subject to a multilateral dispute settlement process that is likely to be far more effective than sanctions imposed unilaterally by the United States. Finally, although some sectors of the U.S. economy may suffer as a result of China's accession to the WTO, the long-term benefits to U.S. consumers, firms, and the overall economy will far outweigh any short-term dislocation costs.

In the final analysis, the correct resolution of the PNTR issue turns on a straightforward question: *Is it in the U.S. national interest to encourage China to liberalize and reform its economy in a more market-oriented direction?*

Regardless of what one thinks of China's behavior in other arenas, the answer to this question is yes. The agreement extends unprecedented opportunities for U.S. firms to access China's market through the expansion of exports and the establishment of operations in China. Import-using businesses and consumers here in the United States will also have better guarantees that low tariff rates will continue to apply. China will benefit as well, particularly average citizens struggling to free themselves from the shackles that chain them to China's disastrous socialist legacy—one responsible for the impoverishment and starvation of millions of people.[1] China's leadership now acknowledges its past mistakes and recognizes the need to lower trade barriers and liberalize its moribund state-dominated economy; the United States should take advantage of this opportunity and support China's reform efforts.

China's Incomplete Transition to a Market-Oriented Economy

China's bid to join the WTO comes in the midst of a decades-long and still incomplete transition from totalitarian communism to a full-fledged market economy. Over the past two decades, the Chinese economy has undergone a breathtaking transformation, opening up to the outside world and permitting the explosive growth of a market-oriented commercial sector. Yet the Maoist legacy still exerts a powerful influence over the economy: the state-owned sector remains huge, state controls are still pervasive, and true market institutions are still woefully underdeveloped. And, of course, the Maoist political apparatus continues to deny citizens even basic political freedoms.

In evaluating the true significance of WTO membership for China, it is important to understand how far China has come over the past 20 years—and how far it still has to go.

Two Decades of Rapid Growth

After decades of inefficient central planning and overemphasis of heavy industry at the expense of light industry, not to mention the chaos unleashed by the Cultural Revolution, China's economy was in near ruins by 1978. Although growth figures in a number of sectors such as industry and agriculture were positive at that time, numerous analysts have pointed out that those figures "masked increasingly serious structural problems," which led the government to conclude that the economy had been pushed to "the brink of disaster."[2]

China has made impressive strides toward a more market-oriented economy in the 20 ensuing years. To be sure, this process is by no means complete. Elements of central planning continue to be prominent in some parts of the economy, and there is a pervasive statism to many elements of the reform program.[3] China is still best characterized as a "hybrid" economy, in which markets have developed amidst continuing state controls.[4] Nevertheless, as the last 20 years of reform history unequivocally show, the overall trend of China's moving toward an economy based on market principles, while not irreversible, is quite clear.

Today, the most vibrant and dynamic sector in China is the burgeoning nonstate sector, which consists of a growing number of private-sector firms as well as joint ventures between foreign and Chinese firms. State-owned enterprises (SOEs) now account for about 28 percent of gross output value in China, down from some 80 percent in 1978. This contrasts with the trend we observe in the private sector. Individually owned and private firms with more than seven employees, Sino-foreign joint ventures, and fully foreign-funded firms now account for 40 percent of gross output value, up from virtually zero in 1978 (collective and township-village enterprises, both of which are quasi-public, account for the remaining 32 percent).[5] A report by the Chinese Academy of Social Sciences notes that today some 70 percent of labor allocation, 62 percent of product pricing and distribution, 51 percent of enterprise management, 23 percent of land transfers, and 17 percent of capital distribution are market regulated—up from basically zero percent in the late 1970s.[6] China has experienced impressive economic growth rates throughout the reform period. China's gross domestic product has nearly quadrupled since 1978 and now stands close to 8 trillion yuan (U.S. $960 billion).

China has also integrated itself more deeply into the world economy. In 1978 international trade totaled roughly 10 percent of the country's GDP; in the late 1990s trade totaled closer to 36 percent of GDP.[7] Government officials in Beijing routinely note that export growth was responsible for about 20 percent of the growth in China's GDP in the 1990s.[8] Of particular relevance here is the fact that the nonstate sector has generated about three-quarters of total export growth since 1978.[9]

It is difficult to overstate how the reforms since 1978 have improved the life of the average citizen of China. According to China's Office on Poverty Alleviation and Development, well over 100 million individuals have risen out of destitution and now live above the official poverty line, set at the miserably low annual per capita income of 640 yuan (U.S. $77).[10] In addition to helping alleviate poverty, the economic reforms in China have brought overall progress, as the gains in per capita income for both urban and rural residents suggest. Although there is some question about the accuracy of the data (given the questionable reliability of macroeconomic data related to China's GDP, particularly in the early reform period), the trend is clear (Table 1).

The overall quality of life for the average citizen in China has improved dramatically as well. Citizens now have access to better services in crucial areas such as health care and education. Millions more people now have electricity (and consequently, refrigeration) and telephone service. The better lives that Chinese citizens now lead are a direct result of the deci-

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Table 1
Per Capita Income in the People's Republic of China

Location	1978	1988	1998
Urban	$38	$135	$657
Rural	$16	$66	$259

Sources: Figures derived from: People's Republic of China, State Statistical Bureau, *1999 China Statistical Yearbook* (Beijing: China Statistical Publishing House, 1999), "Monthly Statistics"; and People's Republic of China, State Statistical Bureau, *1998 China Statistical Yearbook* (Beijing: China Statistical Publishing House, 1998), "Monthly Statistics." Figures from the United States correspond well, although they are sometimes higher. For example, the U.S. Department of State in its 1998 *Country Report on Economic Policy and Trade Practices for China* says that China had a per capita income of 6465 yuan, or U.S. $779. Related information can be found at:http://www.state.gov/www/issues/economic/trade_reports/eastasia98/china98.pdf.

Note: U.S. dollar values reflect the value of the Chinese yuan in 1990.

sion by China's leadership in 1978 to pursue the path of economic reform in a more market-oriented direction. Increasing trade has played a major role, although the internal rationalization of China's economy undoubtedly accounts for most of the gains. Astute observers wisely caution that although "trade is important to China . . . what goes on in the rest of its huge economy remains the critical factor."[11]

Darkening Prospects

Despite 20 years of reform, China still has far to go to redress the problems stemming from decades of misguided socialist policies. Dire poverty remains widespread. Yu Shuning, minister-counselor at the embassy of the People's Republic of China in Washington, conceded in mid-1999, "At present, 42 million Chinese still live below the poverty line" of $77 a year.[12] Even the vast majority of Chinese with incomes above that appallingly low threshold live on incomes that are unthinkably meager by American standards. Indeed, China's per capita income, even after quadrupling in two decades, is still only about one-fourth of that of democratic, market-oriented Taiwan 100 miles away.

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Continued economic progress will require massive restructuring. Prospects that the Chinese economic miracle will continue, however, are clouded. After two decades of rapid growth, the economy appears to be faltering. Zhu Rongji has been forced to slow his ambitious reform program, which he launched two years ago after being promoted to the office of premier in response to pressure from anti-reformers. Consequently, the risk of a full-blown economic crisis—with the attendant risk of political reaction against market-oriented reform—is growing.

Several problems stand out. One is the need for fundamental reform of the chronically loss-making state-owned industrial sector and the insolvent state-owned financial sector. The two problems are inextricably linked. According to government statistics, about half of China's 75,000 SOEs incur net losses, up from one-third just a few years ago. Total losses hover just over $83 billion. Officially, the government provides about $33 billion a year in subsidies to those SOEs. More problematic, though, is that those SOEs absorb more than 75 percent of domestic bank credit, much of which is extended in response to political directives from above, not according to market-based criteria. Government estimates are that about 20 percent of those loans are nonperforming. Western analysts suggest that the estimates are low and that the actual amount is much higher, given inadequate accounting procedures in China.[13] Some analysts estimate that bad debt accounts for some 20 percent of China's trillion-dollar economy, five times the level five years ago.[14]

As a result of the state's continuing to bail out loss-making SOEs, there is a great deal of overcapacity in the marketplace; goods and products are collecting dust on store shelves. Inflation was the perennial problem of the late 1980s, but deflation plagues the current regime. Prices have been declining for a stunning 29 months. China's response has been to cut interest rates seven times in the last two years in an attempt to stimulate spending. However, the continued deflation strongly suggests that consumer fears of a flagging economy have mitigated the impact of interest rate cuts.

It is not lost on the state leadership, of course, that continuing to fund loss-making enterprises only exacerbates chronic overcapacity. Moreover, government attempts to "prime the pump" by investing in the economy are a double-edged sword. To increase growth rates, China has pumped $19 billion into the economy in the last two years and plans to invest another $12 billion this year. In addition to contributing to the problem of overcapacity, many of the projects in which the government is investing are of dubious quality. The east coast of China is littered with half-empty or half-finished office buildings and high-rise hotels.[15]

Although government-led investment has helped boost growth rates over the short term, growth rates are still down. In 1999 China grew at a rate of 7.1 percent (a questionable figure, given the padding of figures by local officials), down from double-digit growth rates in the early to mid-1990s.[16] Moreover, it is quite clear that the attempt to stimulate the economy cannot continue beyond the next two or so years. Government figures indicate that China's 1999 budget deficit will total $22 billion, nearly twice the 1998 figure.[17]

Chinese government officials also acknowledge that some 35 percent of China's 140 million workers in state and collective enterprises are superfluous, and that urban areas will need to absorb some 150 million workers who will migrate from rural areas to seek work.[18] Those numbers create the potential for massive unemployment and even social instability.

The issue of Chinese membership in the WTO thus arises just as China's economic transition has reached a precarious and critical juncture. The market-opening commitments agreed to by China would provide a much-needed shove in the direction of market-oriented reform at a highly opportune time. Over the longer term, anchoring China in a system of pro-market international obligations could make it much harder for China to stray from the path of reform.

China's Bold WTO Offer

It is no coincidence that China has pushed to join the WTO just as its economy seems to be running out of steam. The inescapable conclusion is that China's current leadership views WTO membership as a tool for reviving its flagging economy.

Nearly 14 years ago, in July 1986, China sent a delegation to Geneva to submit a formal request to join the GATT (General Agreement on Tariffs and Trade), the predecessor organization to the WTO.[19] Negotiations dragged on with few major breakthroughs until the weeks leading up to the visit of Chinese premier Zhu Rongji to the United States in April 1999. Widely known as the most pro-reform leader in China, Zhu recognized that China's economy was deteriorating. Consequently, he came to Washington and presented a market access package detailing a number of sweeping economic reforms that China would implement in order to join the WTO. Zhu clearly presented this package in order to jump-start economic reform back home.

Bowing to domestic political considerations, however, President Clinton unwisely rejected Zhu's offer. Negotiations were then put on indefinite hold after the accidental NATO bombing of the Chinese embassy in Belgrade in May 1999. Recognizing its mistake, the Clinton administration made a concerted effort to get WTO negotiations back on track before the WTO ministerial conference in Seattle last November. On China's side, despite worries that his hand was weakened vis-à-vis anti-reform elements in China, Zhu personally intervened to get negotiations back on track when U.S. Trade Representative Charlene Barshefsky flew to Beijing to negoti-

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ate the final deal days before the Seattle Ministerial Meeting in November 1999.

In March 2000 the Office of the U.S. Trade Representative published the full bilateral agreement signed by the United States and China in November 1999. Although the exact terms under which China will join the WTO are not fully spelled out, given ongoing negotiations with other members such as the European Union,[20] the broad outlines of the agreement are clear. According to the Office of the U.S. Trade Representative,[21] China has committed to the following market access concessions (this list is not exhaustive):

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- *Agriculture:* Significant cuts in tariffs will be completed by January 2004. The overall average tariff on agricultural products will be 17 percent. For U.S. priority products such as beef, grapes, wine, cheese, poultry, and pork, the average will be 14.5 percent, down from a preagreement level of 31.5 percent. China will also eliminate export subsidies for the first time ever and permit private trade between importers and exporters. Finally, China has agreed to base restrictions of agricultural imports for health reasons on stricter scientific evidence.
- *Industry:* China will lower industrial tariffs from an overall average of 24.6 percent to an average of 9.4 percent by 2005; the rate will fall to 7.1 percent for U.S. priority products such as wood, paper, chemicals, capital, and medical equipment. China will also participate in the Information Technology Agreement, eliminating all tariffs on computers, telecommunications equipment, semiconductors, and other high-technology products. China will cut tariffs on automobiles from the current 100 percent or 80 percent to 25 percent by 2006.
- *Telecoms:* China will become a member of the Basic Telecommunications Agreement and adopt its regulatory principles, including cost-based pricing, interconnection rights, and independent regulatory authority. China will also phase out all geographic restrictions on paging and value-added services in two years, on mobile/cellular services in five years, and on domestic wireline services in six years. China will also allow a 49 percent foreign ownership share in all telecom services and a 50 percent share in value-added paging services in two years. Finally, China will allow foreigners to invest in China's growing Internet service provider industry.
- *Insurance:* Currently, China allows foreign companies to operate only in Guangzhou and Shanghai. Under the new agreement, China will permit foreign property insurance and casualty insurance firms to insure large-scale risks nationwide immediately and will eliminate all geographic restrictions in three years. China will also expand the scope of activities of foreign insurers to include group, health, and pension lines of insurance, which represent about 85 percent of total premiums. China has agreed to allow 50 percent foreign ownership of life insurance firms; for non-life-insurance firms, China will allow branching or a 51 percent foreign ownership share on accession and the formation of wholly owned subsidiaries in two years.
- *Banking:* At this time, foreign banks are not permitted to conduct business in the local currency with Chinese clients. China also now imposes severe geographic restrictions on the establishment of foreign banks. Under the agreement, China will allow full market access for foreign banks in five years, and foreign banks will be able to conduct local currency business with Chinese businesses in two years and with Chinese citizens five years after accession.
- *Trading:* Foreign firms will have, for the first time, trading and distribution rights for most products, to be phased in over three years.
- *Services:* China will eliminate most foreign equity restrictions and allow greater access for professional services such as foreign law and accounting firms. In travel

and tourism, China will allow unrestricted access to the Chinese market for hotel operators and the establishment of 100 percent foreign-owned hotels in three years. Foreign travel operators will be able to provide the full range of travel agency services.

- *Movies:* Before the agreement, China permitted a maximum of 10 foreign films to be shown each year. After accession, China will allow 40 foreign films to be shown per year.
- *SOEs:* China has agreed that state-owned and state-invested enterprises will make purchases and sales based solely on commercial considerations. The government has agreed that it will not influence commercial decisions except in a WTO-consistent manner.

Note that those commitments are contained in the bilateral agreement between the United States and China. Additional bilateral agreements with other WTO members (for example, the European Union) can only expand the range and depth of China's commitments.

WTO Entry a Boost to Reform

Given the magnitude of China's economic problems, membership in the WTO alone cannot be expected to ensure the success of China's continued transition to a full-fledged market economy. It is entirely possible that economic or political upheavals will derail China's progress. Nevertheless, entering the WTO will significantly increase the chances for success.

WTO membership will promote growth and development in China by expanding the opportunities for Chinese businesses, mostly non-state-owned, that export to foreign markets. As noted above, government officials in China report that roughly three-quarters of export growth over the past two decades has been in the nonstate sector. It is true that China already largely enjoys full market access to the United States and its other major markets, so the immediate expansion of exports from China will be limited. Still, exports in some key labor-intensive sectors, such as textiles, would expand. Overall, in light of long-term dynamic effects, the Chinese government predicts that China's accession to the WTO would increase GDP by 95.5 billion yuan (U.S. $23.64 billion), or 1.5 percent, by 2005.[22]

While Chinese economists acknowledge that a staggering 10 million jobs will be lost in the agriculture, automobile, and machinery sectors, they predict that WTO membership will create as many as 12 million new jobs in sectors such as textiles, toys, and footwear.[23] Chinese firms will also face a more stable export environment, as their access to foreign markets will be protected by WTO rules. As Yang Donghui, secretary-general of the China National Federation of Textile Industries, points out, one of the primary benefits of WTO membership, "especially in the long-run . . . is that the country will be able to enjoy stable multilateral preferential trade polices in a rules-based market."[24]

Improving China's export opportunities will give the economy additional resilience to absorb the shock of needed reforms. Opening China's market to foreign competition will substantially increase the likelihood that the shock is actually administered. To quote one top Chinese official, "The blow will not be light . . . [and] pain is unavoidable."[25] If implemented successfully, China's WTO commitments will either require or catalyze dramatic pro-market reforms throughout the Chinese economy.

Slashing industrial tariffs and expanding foreign distribution rights will force rationalization of the bloated and chronically loss-making SOEs. China's industrial landscape is littered with so-called empty-shell enterprises (*kongqiao qiye*); it is estimated that half of all SOEs are losing money.[26] Those firms have managed to survive in the absence of outside competition; when markets are opened to foreign participation, though, closing down some factories and upgrading others will become unavoidable. Take the example of automobiles.

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It is widely recognized that there will be a sharp consolidation of China's 120 auto producers after tariffs are reduced from the current 80 to 100 percent to 25 percent. Chinese markets were quick to perceive the threat of WTO membership, with automotive listings plummeting on the Shanghai and Shenzhen stock exchanges the day after the signing of the U.S.-Chinese bilateral agreement.[27]

At the same time China is being forced to address its failed state-owned sector, the prospect of entering the WTO is also creating new opportunities for private enterprises in China. It is noteworthy that, just after China signed its bilateral agreement with the United States, it took the unprecedented step of elevating the importance of the private sector in official economic policy. State Development Planning Commission chairman Zeng Peiyan announced that the government would "actively guide and encourage private investment" and would "eliminate all restrictive and discriminatory regulations that are not friendly toward private investment and private economic development in taxes, land use, business start-up and import and export."[28] Just as important, Zeng declared that more private firms would have access to China's fledgling stock markets in Shanghai and Shenzhen, which are currently restricted almost exclusively to SOEs.

One of the linchpins of continuing China's economic transition is the overhaul of its financial sector. Historically, Chinese banks acted simply as funnels of resources into the SOE sector. China's banks today are in a precarious position, given declining capital adequacy, mounting problem loans, and continued reliance on "policy-based lending" to SOEs. If China is to develop a genuine market economy, it will require healthy financial intermediaries that link savers and investors according to market criteria.[29]

WTO membership will promote financial-sector reform by granting unprecedented market access to foreign financial institutions. Increasing the market share of foreign institutions will have a direct and immediate positive impact on the allocation of capital, providing new sources of capital for Chinese enterprises previously neglected by the state banking sector. Furthermore, foreign institutions will subject Chinese banks to intense competitive pressure, thereby forcing them to modernize their operations.

Just the prospect of foreign competition is already shaking up the Chinese financial sector. Top executives in China's state-owned banks are considering ownership changes to help brace the industry for change, particularly two years after WTO entry when all banks will be permitted to do business with Chinese companies in the local currency.[30] Meanwhile, China's central bank governor, Dai Xianglong, has announced a series of banking reforms including gradual interest rate liberalization and expansion of the band within which the bank allows its lending and deposit rates to fluctuate.[31]

Along related lines, China is breaking up its reinsurance market monopoly in preparation for WTO entry. Dai Fengju, head of the state-run monopoly, indicated that the reason for doing so is that the entrance of foreign business rivals will bring competition as well as advanced management technology, which will compel the Chinese firm to further improve its management and service.[32]

China's WTO commitments lay the groundwork for explosive growth of the Internet in China—a development with potentially enormous economic, social, and even political implications. Most obvious, China has agreed to allow 50 percent foreign ownership of Internet service providers, with some possibility of a higher number on a case-by-case basis, according to China's minister of information industry, Wu Jichuan. In addition, though, Chinese market access commitments in telecommunications, information technology products, and express delivery services will all feed growth of the Internet and electronic commerce. Already, China has 6.5 million Internet users, and e-commerce is set to explode. In 1999 the country's volume of online shopping reached $96.7 million, and it is expected to grow to $1.2 billion by 2002. While China had only 100 online stores at the beginning of 1999, it has more than 600 today and is adding two new online stores every day.[33]

Continued growth of the Internet will not only facilitate economic growth; it will provide a major boost to civil society as well. Although Chinese authorities announced new regulatory and privacy measures designed to keep a lid on the Internet's potential for political subversion in late 1999, they recognized the negative impact those measures would have on business development in the country and reversed course in March 2000.[34] The effects of those measures and similar ones in the future are unclear, but what is clear is that China's WTO commitments on Internet-related issues push hard in the other direction. Those commitments increase the odds that the Internet in China will become too big and too firmly entrenched for the authorities to control.

More broadly, China's accession to the WTO will help promote the development of the rule of law. Throughout China's history there has been a strong tradition of subordinating law to policy—using the law as a means of achieving the goals of the state. It is noteworthy that there is no distinction in the Chinese language between rule of law and rule by law—both are translated as *fazhi*. In a rule-of-law system, the state and the political elite (even the Communist Party) would be subject to the same laws. In a rule-by-law system, the law is an instrument to be used by the state to achieve its leadership's goals.

Accession to the WTO will force China to revise and streamline its administrative and contract laws, a process that it has already begun.[35] Currently, overlapping jurisdictions in China, a problem the Chinese refer to as "too many mothers-in-law," create a confusing regulatory environment that is susceptible to corruption. It was with that in mind that Martin Lee, chairman of the Democratic Party of Hong Kong and an ardent defender of human rights, wrote a letter to President Clinton in November 1999, stating, "The participation of China in the WTO would not only have economic and political benefits, but would also serve to bolster those in China who understand that the country must embrace the rule of law."[36]

In sum, China's WTO commitments represent a major victory for pro-market reformers in the Chinese leadership. In this regard, it is essential to recognize that those reformers face stiff internal opposition. One of the primary reasons China has not moved more quickly down the reform path is the divisive political battles currently fracturing the government. Different factions have markedly different attitudes toward economic policy.[37] In the words of Zhou Mingwei, head of the Foreign Affairs Bureau in Shanghai, "The WTO has been the most hotly debated political topic in China since 1989."[38] Leaders such as Premier Zhu Rongji are widely credited with pushing China to deepen its reform effort and integrate more with the global trading community. Others, such as Li Peng, former premier and now head of the National People's Congress, are fearful of the inherent instability that reforms entail and are a powerful force preventing China from reforming more quickly.

While no panacea, membership in the WTO would clearly strengthen the position of the pro-reform elements in the Chinese leadership. In particular, it would give them the political cover of saying that their hands were tied by international commitments. The merger of the domestic reform agenda with those international commitments, and the prestige of membership and participation in an important international body, would help legitimize the undoubtedly painful restructuring that China will have to undertake if it is to continue its transition toward a true market economy.

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Economic Reform and Political Freedom

Thus far this paper has concentrated on the effects of Chinese entry into the WTO on economic reform. But also of crucial significance in any consideration of U.S.-Chinese relations is the issue of political reform in China—namely, the spread of democratic institutions and protection of human rights. Here the impact of WTO membership is admittedly much less clear, since WTO rules do not require China to make any changes in its current repressive political system. Nevertheless, there are good reasons for believing that entry into the WTO, by encouraging continued market-oriented reform in China, will also encourage democratic change over time.

The relationship between economic and political freedom is hotly contested. It is a subject that has featured prominently in the annual debates in Congress over extending NTR with China, and doubtless it will be just as prominent in the PNTR debate. Some observers argue: "In the life of the ordinary Chinese citizen, there is more freedom in the economic realm than any other. Trade can help maintain that freedom, and help to expand that freedom to other realms of China's culture and society."[39] Others disagree, lamenting that "our China policy is the extreme case of the 'free trade solves all problems' school."[40] According to this view, "wealth alone does not drive the passion for democracy. If it did, the oil-rich Middle Eastern countries, along with Nigeria and Angola, would be flourishing democracies instead of corrupt tyrannies."[41]

One way to help resolve this debate is to pose the right question. The wrong question is, Do wealth and economic growth lead to democracy? The right question is, Does a market economy foster the growth of autonomous groups outside the state?

In the case of oil-rich Middle Eastern states, for example, most of the money flows directly into the state hands that control the state-owned oil enterprises. The states then *distribute* this wealth to their citizenry in the form of government handouts. As Samuel Huntington observes:

> Oil revenues accrue to the state: they therefore increase the power of the state bureaucracy and, because they reduce or eliminate the need for taxation, they also reduce the need for the government to solicit the acquiescence of its subjects to taxation. The lower the level of taxation, the less reason for publics to demand representation. "No taxation without representation" was a political demand; "no representation without taxation" is a political reality.[42]

The growth of wealth outside state control, a trend that WTO membership will only accelerate, challenges the power of the Beijing leadership at its root.

At issue here is the power of the purse. A society may have middle classes and growing affluence, but if the state is responsible for channeling resources to the citizenry, there is little reason for the citizenry to articulate demands that would oppose or run counter to state interests.

Accordingly, in evaluating the effect of WTO membership on China's political situation, what really matters is the degree to which trade with China helps generate wealth *outside state control*. In China today, such wealth creation is already well under way. Roughly one-third of the urban industrial workforce is employed in the nonstate sector. In rural areas the proportion is even higher; close to 50 percent of rural industrial workers (nonfarmers) are employed in the nonstate sector.[43] More than 200,000 enterprises can now import and export directly through the world market and by so doing bypass the foreign trade corporations that used to be controlled exclusively by the state. Moreover, the State Statistical Bureau of China reported that nonsalary income from savings interest and revenue from securities investments or inheritance as well as certain illegal activities accounted for 32.8 percent of urban citizens' total income in 1997, compared to 12.7 percent in 1981.[44]

The growth of wealth outside state control, a trend that WTO membership will only accelerate, challenges the power of the Beijing leadership at its root. For the first time since it was founded, the Maoist state must support itself by taxing resources it does not own. Not surprisingly, the state is finding this difficult and costly to do. According to officials at the State Administration of Taxation, outstanding unpaid taxes topped U.S. $5.25 billion in early 1998.[45] In July 1999 SAT officials were forced to remind local officials who were independently writing new tax codes, which lowered taxes for China's citizenry and enterprises, that "it is illegal for local governments to amend tax laws."[46]

Beijing's inability to control resources is becoming increasingly apparent in the case of local government employees as well. One 1993 report found that one-third of the 103 million government employees in China had outside employment. In the words of one Yantai city official, "From top to bottom, the Government is encouraging us to do business."[47] Local governments are affected by changes in the control of resources. The vibrant region located next to Hong Kong, Guangdong province, once received 80 percent of its annual budget directly from the central leadership in Beijing; today, it receives less than 2 percent.[48]

The shift of control of resources away from central state coffers has allowed the growth of a number of different types of independent groups in China. To be sure, it is still too soon to say that there is a vibrant or strong civil society in China; moreover, all groups are supposed to register with the state. Still, China's nascent civil society is certainly far stronger than it was in 1978.[49] Independent groups are finding it increasingly possible to criticize the state because they are now independently financed and receive no funds from the government.

The recent crackdown on Falun Gong, while it highlights how repressive the Beijing regime remains, also shows how dramatically things have changed since Mao's death. That a group with millions of adherents could form and organize outside the state, and that such a group could continue to survive even in the face of determined and brutal state opposition, would have been unthinkable 20 years ago.

More broadly, recent years have witnessed the emergence of a dizzying variety of interest groups formed around such issues as ethnicity; religion; the rights of women, particularly divorced and battered women; and children's rights. In what must be seen as a favorable development, many of those institutions are private or only semiofficial in nature. As Pei Minxin observes, "A notable feature of the growth of associations in the 1980s and early 1990s is that an overwhelming majority of them were semiofficial and private (compared with the dominance of fully official associations prior to 1978)."[50]

Any casual observer will notice the increased willingness of the Chinese press to criticize government policies, albeit to this day mostly in the economic realm. Industrial interest groups and trade associations have also sprouted up throughout the country. Those groups are lobbying to reform contract law and to develop independent judicial systems capable of addressing complex issues such as intellectual property rights law.[51] On other rule-of-law issues, a number of groups are calling for greater transparency in economic laws and administrative changes that prohibit the imposition of excess levies. Citizens' groups are now organizing to challenge unforeseen, illegal fees in areas such as housing as well.

Some recent events in China even point to the development of fledgling democratic political institutions. China has been experimenting with local village elections. To be sure, China's leadership is far from embracing full-fledged democratic institutions such as those in the West. Still, China recently completed another round of village elections and the Ministry of Civil Affairs allowed a team from the Carter Center in Atlanta to observe the elections and to help formulate uniform elections procedures. The delegation found that despite "procedural problems in several of the villages . . . the elections provided the voters a reasonably free choice." The delegation further observed that "most impressive . . . was the openness and candor of Ministry, provincial, and county officials in acknowledging problems and seeking advice on ways to resolve them."[52]

China's National People's Congress has also been taking a more active role in shaping policy, albeit in a still limited fashion.[53] The NPC is a massive organization with just under 3,000 deputies.[54] While it has a limited legislative role, the NPC does vote on appointments to certain governing bodies. It is noteworthy, for example, that pro-reform Zhu Rongji received a higher percentage of votes supporting his nomination as premier than did anti-reform Li Peng when he was nominated to head the NPC itself. This helps send a signal to China's leaders that many citizens support and back China's reformers.

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It bears repeating that the evolution of civil society in China is a slow process and not irreversible. Still, a variety of economic, social, and even political indicators suggests an ongoing process of transferring power from the state to the citizenry. Economically, as noted above, non-state-owned enterprises are the driving engines of growth in China. Socially, we have observed the spontaneous emergence of a variety of groups that receive no funds from the state.

To be sure, the growth of civil society does not automatically translate into expanding political liberties. After all, China's growing civil society exists alongside a still repressive and unaccountable regime. But the emergence of social power centers that rival the state does increase the likelihood that, over time, the state will be forced to concede political rights to those new power centers. Accordingly, civil society is a precursor of democracy. East Asia offers numerous examples of this dynamic in action. In South Korea, Taiwan, the Philippines, and Thailand, economic development laid the foundations for eventual political liberalization.

China's nascent civil society is still weak. As Gordon White points out, "This relative weakness of 'civil society' must be situated in the context of a semi-reformed command economy in which the state retains its dominant position in the economy."[55] But people who argue that nothing has changed in China, that 20 years of economic development have had no effect on political conditions, are badly mistaken. Chinese society is dramatically different from what it was two decades ago; the state's control over the populace has been substantially reduced. WTO membership, by strengthening civil society in China, can accelerate this process. Whether or when full-fledged democracy will come to China cannot be known, but it is clear that facilitating China's entry into the WTO is a step in the right direction.

What the United States Must Do

It is important to recognize that Congress does not get to vote on whether China enters the WTO. Two-thirds of WTO members must approve a new member's application, but the administration, not Congress, will cast the U.S. vote. Dozens of countries have joined the WTO since it was formally established in January 1995, and not once has Congress had a say in the matter—nor has it even paid particular attention.

Nevertheless, Congress does have the power to hinder and complicate China's accession to the WTO. In return for all its sweeping market access commitments, China expects the United States to make one commitment: to grant China PNTR. For the United States to live up to its side of the bargain, Congress must change the Jackson-Vanik amendment that currently subjects NTR status for China to annual review.

It is unclear what will happen if Congress refuses to grant China PNTR status. It is possible that China will refuse to enter the WTO, and all its pledges to open its markets will be set aside. Alternatively, China could decide to enter the WTO and refuse to extend its market access commitments to the United States. In that event, other countries would reap the benefits of China's newly opened markets, but the United States would not. As a consequence, the benefits of WTO membership, both to the United States and to China, would be severely compromised. Recent evidence suggests that this is the most likely outcome. China's foreign trade minister, Shi Guangsheng, declared in Beijing that China will likely seek WTO accession even if Congress does not pass PNTR and that "if the United States misses this opportunity, it will actually lose the tremendous market of China and will be giving away the opportunity for participating in this market to its competitors."[56]

The PNTR issue presents the following choice: The United States can act to encourage and facilitate pro-market reform in China, or it can act to block such reform. The correct choice is obvious.

Jackson-Vanik: Relic of the Cold War

The Jackson-Vanik amendment is a relic of Cold War–era tensions between the United States and the Soviet Union. An amendment to the Trade Act of 1974, Jackson-Vanik reflected congressional concern over Soviet restrictions on Jewish emigration. It permits the president to grant conditional "most favored nation" (now NTR) trading status to a "non-market economy" if the president determines that the subject country permits free and unrestricted emigration. The latter condition is subject to a waiver for 12 months if the president determines that such a waiver will promote the objective of free emigration.[57]

The president may renew the Jackson-Vanik waiver for another year by notifying Congress by June 3 of each year. While the president can extend NTR and waive the revocation without consulting Congress, Congress has 60 days after July 3 to overturn the president's decision by issuing a Joint Resolution of Disapproval with a straight up or down vote. Should this happen, the president can veto the resolution and Congress can then attempt to override the veto within specified time limits.[58]

After the normalization of relations between the People's Republic of China and the United States in 1979, the two countries concluded a bilateral trade agreement that went into effect on February 1, 1980. President Carter, however, was unable to determine whether China fully abided by Jackson-Vanik's freedom of emigration requirement; therefore, he opted for the annual waiver process. Every year since 1980, even in the aftermath of the Tiananmen Square incident in 1989, the United States has reextended NTR status to China.

Although the old term "most favored nation" suggests special or preferential treatment, the fact is that the United States currently grants NTR tariff status to more than 160 nations including Iran, Iraq, and Libya. Only Afghanistan, Cuba, Laos, North Korea, Yugoslavia, and Vietnam do not have NTR status under U.S. law.

Here then are the questions that should be considered in deciding whether to amend Jackson-Vanik to exempt China permanently: Should the United States grant the same trade status to China that it does to 160 other countries—and that it has granted to China every year for the past two decades? Or should the United States continue to single out China for special and differential unfavorable treatment under a Cold War law designed to help Jews emigrate from a country that no longer exists? The correct option is clear.

Some groups that oppose WTO membership for China have claimed that the United States would not have any WTO obligation to grant PNTR to China. For example, Lori Wallach of Public Citizen's Global Trade Watch has argued that "the WTO is silent on the duration of MFN grants, requiring only that MFN not be conditioned on any extraneous factor. . . . As long as the U.S. provides continuous MFN, action by China to limit U.S. WTO benefits in retaliation for the U.S. not providing permanent MFN would constitute a Chinese violation of its WTO commitments."[59]

That position is flatly incorrect. Article I, Section I, of the General Agreement on Tariffs and Trade, the WTO's founding document, stipulates that MFN or NTR status "shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties."[60] Under current U.S. law, however, China's NTR status is conditioned on an annual presidential waiver on the ground that such review furthers the objective of free emigration. NTR status is further conditioned on a vote in Congress to sustain or reverse that waiver. At present, then, China's NTR status is clearly conditioned on "extraneous factors," to use Wallach's own language, in violation of GATT requirements.

In this regard, Secretary of Commerce William Daley noted: "I want to clearly reaffirm the need to grant permanent Normal Trade Relations (PNTR) to China in order to obtain the full market-opening benefits negotiated last fall. Opponents of PNTR have tried to confuse the issue by falsely claiming that some form of periodic review of NTR status would be consistent with our WTO obligations. That is simply not the case."[61] In agreement, U.S. Trade Representative Charlene Barshefsky remarked, "There's really no legal question about it in the WTO."[62]

It is also misleading to claim, as Public Citizen does, that, in light of the bilateral trade agreement between the United States and

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China, "the U.S. could obtain all of the tariff cuts China would be required to make upon entry into the WTO even if the Congress did not grant Permanent Most Favored Nation (PMFN) status."[63] In the first place, the bilateral agreement does not cover certain sectors, particularly in services.[64] The United States would thus be excluded from a whole range of market access commitments that China has made. Second, the United States cannot assert whatever rights it enjoys under its bilateral agreement under the WTO's dispute settlement procedures. The WTO protects only those rights granted under WTO agreements. Ambassador Barshefsky has repeatedly made her position clear in stating that "we must grant China permanent NTR or risk losing the full benefits of the agreement we negotiated, including special import protections, and rights to enforce China's commitments through WTO dispute settlement."[65]

Loss of Jobs

Old-fashioned protectionists oppose PNTR for China for the simple reason that they oppose expanded trade with China. They point to the $71.2 billion in annual imports from China and the bilateral trade deficit with China of $56.9 billion.[66] Those figures, they claim, mean a loss of U.S. jobs. In particular, lobbyists for the textile industry fear the competitive challenge of Chinese imports once quotas are eliminated under WTO agreements.

However, PNTR by itself does not expand China's access to the U.S. market. All it does is to make permanent the status quo that has prevailed every year for the past 20 years. Accordingly, U.S. industries that face import competition from China will not be exposed to any additional competition simply as a result of changing China's NTR status from annually renewable to permanent.

It is true, though, that PNTR facilitates China's entry into the WTO and that WTO membership for China will require the United States to eventually remove some of the trade barriers it currently maintains against China—in particular, its restrictive textile quotas. Trade in textiles and clothing is subject to the WTO Agreement on Textiles and Clothing. Under that agreement, all countries are required to eliminate quotas in this industry by the year 2005. The United States, however, negotiated in the bilateral agreement with China a provision that would enable the United States to invoke additional protection against import surges through the use of a textile safeguard provision that expires at the end of 2008.[67] Despite this additional protection, the U.S. International Trade Commission is likely correct that, "although much of this increase in China's exports of textiles and apparel comes at the expense of other suppliers to the U.S. market, the U.S. textile and apparel industries could also be affected, with U.S. apparel producers and workers experiencing the more adverse effects."[68]

So WTO membership for China will adversely affect some U.S. interests through increased imports. Those increased imports, however, will benefit other U.S. interests: businesses that can reduce costs with Chinese inputs and equipment and consumers who enjoy the low prices and variety offered by Chinese clothing, toys, and other products. As to the overall effect on the U.S. economy, economists since Adam Smith have known that increased openness to foreign competition is a net benefit for countries that make that wise policy choice.

Meanwhile, on the other side of the ledger, WTO membership for China will open enormous new opportunities for U.S. exports and investment. One study by the Institute for International Economics estimates that "the induced increase in world exports of goods and services to China can be estimated at U.S. $21.3 billion. The immediate increase in U.S. exports of goods and services to China can be estimated at U.S. $3.1 billion."[69] Other studies, which take into account the potential dynamic gains of increased competition, estimate even higher benefits. Fred Hu of Goldman Sachs, for example, estimates that China's accession to the WTO would lead to an additional $13 billion in U.S. exports by 2005.[70]

The protectionist argument against PNTR thus comes down to the assertion that the commercial interests of textile producers and a few other import-competing industries are more important than the interests of import-using businesses and consumers, more important than the interests of U.S. exporters with a huge stake in improved access to the Chinese market, and more important even than the U.S. national interest in encouraging market-oriented reform in the world's most populous country. That kind of naked special pleading must be rejected.

The Need for Leverage

A common objection to PNTR is that granting it would be tantamount to rewarding a "rogue" nation for bad behavior. Critics of China's entry into the WTO point to a whole panoply of nontrade behavior by the Chinese government that offends core American values and runs counter to U.S. national interests. A short list of issues includes human rights abuses, technology transfers, nuclear espionage, missile proliferation, Asian security, campaign finance scandals, and China's handling of demonstrations in the aftermath of the accidental U.S. bombing of the Chinese embassy in Belgrade.

It is important to note, however, that critics of granting China PNTR status span the entire political spectrum and are concerned about different aspects of the Sino-U.S. relationship. Regardless of ideological stripe, the critics raise important concerns that should be part of the bilateral relationship between the United States and China. There are several reasons, though, why hindering China's entry into the WTO (which the U.S. Congress could do by not amending Jackson-Vanik) is not the proper way to resolve the outstanding issues.

One reason is that the status quo of conditional NTR is an empty cannon. Andrew Nathan, professor of political science at Columbia University, suggests that, "except for the post-Tiananmen sanctions, no policy has been as effective in achieving modifications of Chinese human rights policy as the threat of MFN [NTR] withdrawal."[71] It is true that, before the annual debates on the extension of NTR in the past, China would engage in a widespread publicity campaign and sometimes release a high-profile dissident. Those short-term efforts, however, did little to change government attitudes or promote long-term change.

Indeed, the annual threats to remove NTR have actually weakened U.S. credibility. Former U.S. ambassador to China James Lilley's words about the debates on NTR in the mid-1990s remain true today: "The fundamental issue for China policy makers is that if the United States is to brandish MFN [NTR] as a weapon, we must be prepared to use it or our opponents will treat us with contempt. If we are not ready to revoke MFN for China, and clearly we are not, the president should . . . deemphasize the issue."[72] With Sino-U.S. relations at a particularly low ebb in 1999, it is reasonable to ask what the point was of the annual debate on the floor of the House, when Senate majority leader Trent Lott had already announced that the Senate would not take up the issue. Moreover, the House of Representatives garnered only 170 votes in favor of revoking the NTR status of China in 1998, even in the face of the Cox Committee's espionage charges and the furor over illegal campaign contributions. The experience of recent years shows that the prospect that any circumstances short of outright military conflict would ever provoke Congress to revoke NTR is remote at best.

Furthermore, revoking China's NTR status would fail for the same reason that unilateral trade sanctions fail generally.[73] It is true that the United States is the sole superpower in the world today, but that does not mean that we live in a unipolar world where we can impose our will on other countries. If the United States were to revoke NTR status for China and raise tariffs accordingly, other countries would "free ride" on U.S. actions and continue to trade with China. People who oppose China's entry into the WTO for fear of high-tech exports going to China would also find their efforts stymied. Other countries are quite explicit about the fact that they will continue to give China their most advanced technology. Christian Pierret, the French junior industrial minister, for example, publicly declared in Beijing in 1998: "We [the French government] are playing to the

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fullest the game of technology transfers."[74]

Finally, in the event China's non-trade-related behavior becomes truly egregious (hostility toward Taiwan, for example), WTO obligations do not prevent the United States from taking appropriate actions. Article XXI(b)(iii) of the GATT explicitly states that "nothing in this Agreement shall be construed to prevent any contracting party from taking any action which it considers necessary for the protection of its essential security interests taken in time of war or other emergency in international relations."[75]

Implementation

A number of serious critics of China's entry into the WTO point out that the promised benefits of WTO membership will materialize only if China abides by its commitments. Moreover, they point out the possibility of severe disruptions to the WTO process should China become a member and not play by the rules. Even if China's leaders are intent on implementing the agreement, it is not lost upon the world trading community that some local bureaucrats will be resistant to change. Moreover, there is a lack of transparency in the rule-making process in China, a problem that hinders foreign access to China's market.

To be sure, these are legitimate concerns. Two mitigating factors, however, should be mentioned. First, the current Chinese leadership is at least aware of the problem. Top trade and foreign investment officials forthrightly acknowledge that "laws that were made during the 1970s or 1980s did not take into consideration international regulations. There are even conflicts between them and some recently-made laws, such as the Contract Law and the Corporate Law."[76] Trade officials have also been more forceful in pushing through laws and regulations "to conform to the requirement of WTO rules" and in acknowledging that "the government's project-review and decision-making processes should be more transparent."[77]

The second mitigating factor is the strength of the WTO dispute settlement process. Should China, as a member of the WTO, not open its market, the United States and other countries would have a better forum in which to air their grievances than they would if China remained outside the WTO. China would be forced to blame the entire world trading community and the WTO should it lose a case—something China would find difficult to do if it was intent on becoming a respected global leader in its own right. Already, there is evidence that China makes a concerted effort to play by the rules with international economic institutions such as the World Bank and the International Monetary Fund. Moreover, there is evidence, as Margaret Pearson observes, that

> [f]ar from resenting these foreign institutions, Chinese reformers often have benefited from China's participation in them. In domestic debates in particular, Chinese officials were able to use World Bank and IMF standards in conjunction with China's desire to be an accepted member of global organizations as an impetus for economic liberalization.[78]

Currently, while trade disputes between the United States and China remain purely bilateral, anti-reform elements in China often claim that the U.S. position stems from either the desire to protect failing U.S. industries or a fear of China's emergence as a regional hegemon. China's accession to the WTO would blunt such arguments. In so doing, it would also allow U.S. policymakers to more effectively address other, non-trade-related aspects of the Sino-U.S. relationship.

In the end, while concerns about China's implementation of WTO commitments are legitimate, they do not provide the basis for opposing WTO entry. Indeed, the strongest argument for bringing China into the WTO rests precisely on the recognition of the obstacles that currently hinder continued market-oriented reform in China. WTO membership can help to overcome those obstacles by imposing on China's leadership the additional constraint of pro-market international obligations.

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Conclusion

We return to the question posed at the beginning: *Is it in the U.S. national interest to encourage China to liberalize and reform its economy in a more market-oriented direction?*

The answer is a resounding yes. WTO membership is no panacea for China's economic problems, a vast majority of which are the consequence of China's disastrous socialist legacy. WTO membership is no guarantee that China will continue on the reform path and successfully make the transition to a full-fledged market economy, and it is no guarantee that China will embrace democracy and protect human rights. But it does push in the right direction.

We should not deceive ourselves about the influence of U.S. policies, wise or unwise, on China's future. China is the most populous country on earth, and Chinese civilization has existed continuously for thousands of years. China's future is largely up to China. But by taking advantage of China's offer to open its market, we can do what is in our power to exert a positive influence. Encouraging and facilitating China's entry into the WTO are quite simply our best chance to improve the odds for market-oriented reform—and, by extension, political reform—in that great and ancient nation. It is a chance we should not miss.

Notes

1. It is often forgotten that the world's worst famine took place in the People's Republic of China during a period known as the Great Leap Forward (1959–61). Estimates of the famine's death toll hover between 15 million and 20 million. Of significance here is the overwhelming evidence that the famine had virtually nothing to do with environmental factors but was, rather, the direct consequence of state policy. Mao Zedong, in an effort to achieve a Great Leap Forward in industry, extracted enormous resources from agriculture, which led to tremendous food shortages. China is not alone in this respect among communist regimes, as the modern-day case of North Korea suggests. Similarly, despite differences between Soviet and Chinese communism, the famine of 1932–33 in the Soviet Union resulted largely from Stalin's extraction program that fostered great discontent among the peasantry. For an analysis of similarities between the Soviet and Chinese cases, see Thomas P. Bernstein, "Stalinism, Famine, and Chinese Peasants," *Theory and Society* 13, no. 3 (May 1984): 339–71.

2. Internal government memo, quoted in Carl Riskin, *China's Political Economy* (Oxford: Oxford University Press, 1987), p. 237. To be sure, this evaluation had a political rationale as well. Newly established leaders often are quick to point out that the ancien régime performed miserably. China is no exception.

3. Dorothy Solinger, *China's Transition from Socialism* (Armonk, N.Y.: M. E. Sharpe, 1993).

4. See Victor Nee, "Organizational Dynamics of Market Transition: Hybrid Forms, Property Rights, and Mixed Economy in China," *Administrative Science Quarterly* 37 (1992): 1–27.

5. People's Republic of China, State Statistical Bureau, *1998 China Statistical Yearbook* (Beijing: China Statistical Publishing House, 1998), "Monthly Statistics."

6. "Unfinished Business," *Far Eastern Economic Review*, December 17, 1998, p. 22.

7. See Thomas W. Robinson, "Interdependence in China's Foreign Relations," in *China and the World*, 3d ed., ed. Samuel S. Kim (Boulder, Colo.: Westview, 1994), p. 193.

8. Mark A. Groombridge, "Is the Asian Flu Still Infectious? The Case of China," *Looking Ahead*, August 1998, pp. 21–24.

9. Australian Department of Foreign Affairs and Trade, East Asia Analytical Unit, *China Embraces the Market* (Barton, Australia: Commonwealth of Australia, 1997), p. 10.

10. The most dramatic improvements were made in rural areas. Between 1986 and 1993, 45 million rural poor were officially removed from the poverty list, an average of about 6.4 million a year; from 1994 to 1996, another 5 million rose above the poverty line. Zhao Huanxin, "Poverty Relief Work to Intensify," *China Daily*, April 8, 1999.

11. Peter Harrold, "China: Foreign Trade Reform—Now for the Hard Part," *Oxford Review of Economic Policy* 11 (1995): 135.

12. Yu Shuning, "China's Poverty Program," Letter to the editor, *Washington Post*, July 17, 1999, p. A18.

13. Nicholas Lardy, *China's Unfinished Revolution*

Encouraging and facilitating China's entry into the WTO are quite simply our best chance to improve the odds for market-oriented reform—and, by extension, political reform—in that great and ancient nation.

(Washington: Brookings Institution Press, 1998), pp. 115–20.

14. James Kynge, "China: A Fraught Fiscal Future," *Financial Times*, January 11, 2000.

15. For a broader discussion of this point, see Groombridge, "Is the Asian Financial Flu Still Infectious?"

16. Ian Johnson and Owen Brown, "China's Economic Growth Slows to 7.1% Despite Export Rebound," *Wall Street Journal*, December 30, 1999, p. A9.

17. "China: Big Boost for Economy Next Year," *Financial Times*, December 10, 1999.

18. See quotations from Li Jiange, deputy director, Chinese State Council for Restructuring Economic Systems, in "China: Big Boost for Economy Next Year," *Financial Times*, December 10, 1999.

19. For a more detailed discussion of this point, see Harold K. Jacobson and Michael Oksenberg, *China's Participation in the IMF, the World Bank, and GATT* (Ann Arbor: University of Michigan Press, 1990).

20. The accession of a country to the WTO is a three-step process. The first substantive step toward membership consists of a memorandum from the applicant describing all laws, regulations, and policies affecting trade and investment. At this point the process divides into two tracks. The WTO General Council appoints a working party composed of trade negotiators from WTO members to bargain with the applicant over bringing its domestic laws and regulations into compliance with the WTO. The second step is that the potential new member-state undertakes a series of bilateral negotiations with individual WTO members on reciprocal tariff reductions and—of equal importance in recent years—other market access issues covering agriculture, industrial goods, and services. After the successful conclusion of the bilateral discussions, the working party may submit an Accession Protocol for approval by the WTO's top governing body, the Ministerial Conference. At that time, the various bilateral agreements become "multilateralized," and an agreement is drawn up to be extended to all WTO members on an MFN basis. At this final stage, a vote will take place among WTO members, two-thirds of whom must vote in favor of the applicant's accession. At the time this paper goes to press, China has completed most of the necessary bilateral agreements, although negotiations with the European Union have still not been completed. Also, the formal Accession Protocol has yet to be drafted.

21. What follows is based on *Summary of U.S.-China Bilateral WTO Agreement*, White House Office of Public Liaison, November 17, 1999, www.uschina.org.

22. "China's WTO Entry to Boost GDP 1.5%, Report," *China Online*, November 18, 1999, www.chinaonline.com.

23. "China WTO Entry Could Spur Jobs," Associated Press, December 12, 1999.

24. Quoted in Meng Yan, "Riding High on the WTO Wave," *China Daily Business Weekly*, December 26, 1999, p. 1.

25. Unidentified official quoted in "China Bracing for Membership in WTO," Associated Press, January 11, 2000.

26. For a more thorough discussion of this point, see Mark A. Groombridge, "Dragon Droop: Why China's Economic Future May Be Less Spectacular Than You Think," *American Enterprise*, July–August 1998, pp. 34–39.

27. "GM China and the WTO," *China Online*, December 8, 1999, www.chinaonline.com.

28. Quoted in John Pomfret, "China Gives Broad Rein to Economy's Private Sector," *Washington Post*, January 5, 2000., p. A1. To be sure, there are some sectors that will be limited. Zeng is quoted further in the same article: "Except for the areas that are related to national security and those that must be monopolized by the state, all the rest of the areas should allow private capital to enter."

29. A thorough discussion of the banking situation is offered in Lardy.

30. James Kynge, "China: WTO Entry May Force Banks to Go Public," *Financial Times*, December 13, 1999.

31. James Kynge, "China: Financial Reforms to Accelerate," *Financial Times*, January 21, 2000.

32. "China Reinsurance: Beijing Prepares to Open Market," *Journal of Commerce*, February 10, 2000, p. 10.

33. "China Ecommerce Doubled Last Year, Up 12 Times by 2002," *China Online*, March 10, 2000, www.chinaonline.com.

34. Matt Forney, "China Reverses Harsh Internet Rules, Easing Threat to Trade," *Wall Street Journal*, March 13, 2000, p. A21.

35. For a broader discussion of this point, see Mark A. Groombridge and Claude E. Barfield, *Tiger by the Tail: China and the World Trade*

Organization (Washington: AEI Press, 1999).

36. This letter is available at http://www.business 4chinatrade.org.

37. See Andrew Nathan, "Factionalism and the Limits of Reform," in *China's Crisis* (New York: Columbia University Press, 1990), pp. 21–68.

38. Quoted in John Pomfret, "Chinese Are Split over WTO Entry," *Washington Post,* March 13, 2000, p. A1.

39. Jeane Kirkpatrick, Jack Kemp, Lamar Alexander, Steve Forbes and Donald Rumsfeld, "The Eagle and the Dragon," *Wall Street Journal*, June 23, 1997, p. A14.

40. Michael Ledeen, "The Trade Weapon and Other Myths," *American Spectator,* February 1998, p. 24.

41. Ibid., p. 26.

42. Samuel Huntington, *The Third Wave* (Norman: Oklahoma University Press, 1991), p. 65.

43. Fan Gang, "Development of the Nonstate Sector and Reform of State Enterprises in China," in *China in the New Millennium: Market Reforms and Social Development,* ed. James A. Dorn (Washington: Cato Institute, 1998), pp. 76–81.

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49. Pei Minxin, "The Growth of Civil Society in China," in *China in the New Millennium,* pp. 245–66.

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51. For further discussion of this point, see Mark A. Groombridge, "The Political Economy of Intellectual Property Rights Protection in the People's Republic of China," in *Intellectual Property in Emerging Markets,* ed. Clarisa Long (Washington: AEI Press, 2000), pp. 11–46.

52. Carter Center Delegation, "Village Election in China," Working Paper Series, March 25, 1998, p. 1.

53. Wang Juntao, "A Gray Transformation," *Journal of Democracy* 9, no. 1 (January 1998): pp. 48–54.

54. Of the 2,978 deputies to the Eighth National People's Congress elected to serve from 1993 to 1998, 332, or 11.15 percent, are workers; 280, or 9.4 percent, are farmers; 649, or 21.79 percent, are intellectuals; 842, or 28.27 percent, are Communist Party cadre members; 572, or 19.21 percent, are representatives of the various democratic parties and those with no party affiliation; 267, or 8.97 percent, are from the People's Liberation Army; and 36, or 1.21 percent, are returned overseas Chinese. Of these deputies 626, or 21.02 percent, are women. Representing all the 55 national minorities are 439 deputies, who make up 14.74 percent of the whole assembly. See the Web page of China's Consular Office in New York, http://www.nyconsulate.prchina.org/news/PeoplesCongressSystem.html.

55. Gordon White, "Prospects for Civil Society in China," *Australian Journal of Chinese Affairs* 29 (January 1993): 86.

56. Quoted in "China Resolved to Enter WTO," Associated Press Newswire, March 13, 2000, http://www.washington post.com/wp-srv/aponline.

57. Section 402 of the Trade Act of 1974, 19 U.S.C. § 2432. The waiver process only makes a nonmarket economy eligible for NTR treatment. To actually grant such treatment, the president must then conclude a bilateral trade agreement with the subject country that provides for (a) reciprocal NTR treatment, (b) safeguard measures against disruptive import surges, and (c) the protection of intellectual property rights. This agreement is limited to an initial three-year period but subject to additional three-year renewals. Section 405 of the Trade Act of 1974, 19 U.S.C. § 2435.

58. For a more thorough discussion of the historical background of NTR (MFN) doctrine in the United States, see Alan S. Alexandroff, "Concluding China's Accession to the WTO: The United States Congress and Permanent Most-Favored Nation Status for China," *Journal of International Law and Foreign Affairs* 3, no. 1 (Spring–Summer 1998). pp. 23–42.

59. Lori Wallach, Public Citizen Global Trade Watch Web site, http://www.citizen.org/ pctrade/China/WTOMEMO.htm#N_1_.

60. "With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with

respect to all rules and formalities in connection with importation and exportation, . . . any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties." *The General Agreement on Tariffs and Trade,* Article I, Section I, (1947), http://www.wto.org/wto/legal/gatt47.pdf.

61. "Correcting the Record on China Trade Issues," Business Coalition on U.S.-China Trade, FactWatch, February 16, 2000, http://www.uschina .org/public/wto/factwatch.html.

62. Quoted in "USTR Says Reviewing NTR for China on Annual Basis Would Violate WTO Rules," *Inside U.S. Trade* 17, no. 6 (February 10, 2000): 218.

63. http://www.citizen.org/pctrade/media/021600.htm.

64. See Charlene Barshefsky's March 8, 2000, letter to Rep. Charles Rangel (D-N.Y.), www.insidetrade.com.

65. See, for example, Charlene Barshefsky, Speech to the National Conference of State Legislators, Washington, February 4, 2000, www.ustr.gov/speeches.

66. Figures from the U.S. International Trade Administration, http://www.ita.doc.gov/industry/otea/usfth/aggregate/Hl98t10.txt.

67. The United States also negotiated other special protections against Chinese imports: a 15-year extension of the unfavorable "nonmarket economy" status under the U.S. antidumping law and a country-specific safeguard provision. By blocking freedom of trade between the United States and China, those protectionist provisions reduce the total value of China's WTO entry. Nevertheless, they further weaken the claim by protectionists that PNTR will cause U.S. industries to be overwhelmed by cheap Chinese imports.

68. U.S. International Trade Commission, "Assessment of the Economic Effects on the United States of China's Accession to the WTO," publication 3228, August 1999, p. xv.

69. Daniel H. Rosen, "China and the World Trade Organization: An Economic Balance Sheet," Institute for International Economics International Economic Policy Brief no. 99-6, June 1999, p. 2.

70. Fred Hu, "WTO Membership: What This Means for Greater China," Goldman Sachs Global Economics Paper no. 14, April 1999.

71. Andrew Nathan, "Influencing Human Rights in China," in *Beyond MFN: Trade with China and American Interests,* ed. James R. Lilley and Wendell L. Willkie II (Washington: AEI Press, 1994), p. 88.

72. James R. Lilley, "Trade and the Waking Giant," in ibid., p. 54.

73. For a more thorough discussion of this point, see Claude E. Barfield and Mark A. Groombridge, "Unilateral Sanctions Undermine U.S. Interests," *The World & I,* December 1998, pp. 92–97.

74. Quoted in "France Ready to Transfer Technology to China," Reuters, June 15, 1998.

75. *The General Agreement on Tariffs and Trade,* http://www.wto.org/wto/legal/gatt47.pdf.

76. Zhang Yan, "Shi: Trade Rules to Be Reviewed," *China Daily Business Weekly,* January 9, 2000, p. 2.

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