U.S.–China Trade Relations: The Best of Both Worlds

THIS YEAR'S BIGGEST trade battle so far has been over permanent normal trade relations between the United States and China. The U.S. House of Representatives voted in May to permanently normalize trade relations, paving the way for China's membership in the World Trade Organization. The issue is now before the U.S. Senate. The vote has sparked controversy, perhaps because the details of the WTO accession agreement are not well understood. The most striking detail of the agreement, which is essentially a work in progress, is that the United States does very little in exchange for much reduction in China's protectionism.

This one-sided liberalization is not unusual. In trade agreements between the United States and developing countries, the latter do most of the liberalizing. The reason is simple. The United States is already more open to imports, foreign investment and international trade in services than many other countries, especially developing ones. In the China–U.S. agreement, U.S. tariffs do not go down, and other types of trade protectionism are generally not reduced either. Important from the Chinese perspective, however, is the United States' commitment to make permanent the trade privileges it has been extending to China one year at a time.

Chinese tariffs do come down. Chinese industrial tariffs are at an average ad valorem value of 24.6 percent. The average will fall to 9.4 percent. Despite this large reduction, average Chinese tariffs are markedly higher than those of industrial countries. According to some estimates, the average industrial tariff among the WTO member nations is under 4 percent. While China's trade reduction is important, it is not NAFTA. The WTO is not a free trade organization.

In addition to tariff reductions, China will reduce nontariff barriers. Import quotas will be phased out. Import licensing will ebb. Government monopolies on the importation of some products will fade, as will government decrees that only certain enterprises may import products the government itself doesn't monopolize. Arcane government purchasing programs—essentially "buy China" programs—will be made transparent and opened to foreigners.

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Foreign investment rules will also change. Foreign firms will not have to agree to local content requirements, technology transfer requirements or minimum export requirements. Some of the biggest openings involve trade in services rather than in goods. Retailing and wholesaling, from which foreigners have been excluded up to now, will be opened. Foreign firms will be permitted to hold up to 50 percent interest in telecommunications operations. Right now in China, foreign banking operations can only do business with foreign firms and in designated locations. By the time the accession is five years old, foreign banks will be able to do business in Chinese currency with both Chinese companies and individual customers at any geographic location. This is a significant opening.

The results of the U.S.–China negotiations last November are only part of a larger agreement—China's accession to the WTO. WTO membership means not only trade openings for China but also access to the organization's dispute settlement mechanisms. China will no longer be subjected to arbitrary unilateral decisions involving so-called administrative protectionism, such as antidumping. Administrative protectionism exists within the WTO framework, but this protectionism is more fully rationalized than that experienced by countries in some bilateral relationships.

The WTO agreement includes tariff and nontariff reductions that will be "multilateralized." This means each of the bilateral agreements reached between China and every other country in the WTO will be merged. The best deal that China gives to any particular country will, in the merged agreement, be extended to all the WTO countries. Thus, the agreement between the United States and China can only get better.

—William C. Gruben

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