U.S.-CHINA TRADE ISSUES AFTER THE WTO AND THE PNTR DEAL

A Chinese Perspective

After thirteen years of hard bargains and dashed hopes, China and the United States finally reached a trade agreement in mid-November 1999. American companies would not get the full benefits, however, until the U.S. Congress agreed to make China's normal trade relations permanent. Half a year later, on May 24, 2000, the U.S. House of Representatives approved historic legislation granting China permanent normal trade relations (PNTR), which is a prerequisite for implementing the U.S.-China trade deal of last November. Both measures would pave the way for China's entry into the World Trade Organization (WTO). The new U.S.-China trade deal, described by government officials of both countries as mutually beneficial, should resolve many of China's market access and other bilateral economic issues from the past in a positive way.

In terms of bilateral trade relations, however, this accord has not resolved all problems. Because of the differences of both countries in social system, ideology, culture, and, particularly, worsening bilateral political relations, Sino-U.S. trade relations have been fraught with frictions and disputes in the past decade. Even after China's formal entry

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into the World Trade Organization and the United States' granting PNTR status to China, these problems will remain. From the Chinese perspective, there are four major issues: dispute over the trade imbalance derived from different methods of calculating trade figures; U.S. economic sanctions against China and U.S. technology export control; alleged "currency manipulation"; and human rights linked to trade relations. Thus, China-U.S. trade could remain a hot political issue in the United States and continue to strain bilateral relations. This essay intends to provide a Chinese perspective on these issues to the American public. Hopefully, this would facilitate mutual understanding, encouraging both countries to settle them at the working level, and finally defusing the trade issues and taking them out of the overall China-U.S. relationship.

Benefit Distribution

Although China's entry into the WTO signifies that "a historic door has been opened," as Mike Moore, director-general of the WTO, put it, no one expects immediate economic consequences from the deal. But the long-term benefits for both China and the United States are indisputable. For China, as many observers noted, this accord will integrate China with the world marketplace, give new impetus to its current sluggish domestic demand, restructure its economy toward becoming market oriented, and reinforce the rule of law. For the United States, it has achieved the long-sought goal of entering the last huge market in the world.

In the beginning, the economic benefits might be unevenly distributed among different industries of both countries. Since the United States has long complained about the alleged huge trade deficit with China, this accord should improve the bilateral trade balance in favor of the United States.

The major gains for the United States involve market access and tariff reduction. Overall, the Chinese tariff level will decline from an

average of 24.6 percent to 9.4 percent. As a result, U.S. exports to China are likely to grow faster, in percentage terms, than imports. The U.S. International Trade Commission estimated that reducing the Chinese tariff would boost U.S. exports by about 10 percent and its imports from China by about 6.9 percent. It would also create more U.S. high-paying export-related jobs in such fields as aerospace and the automobile industry.

More favorable terms in the deal are in the U.S. agriculture sector, where the Chinese tariff will drop from 22 percent to 14.5–15 percent, or even lower, by 2004. Thus U.S. cotton, wheat, corn, and soybeans will see a big surge in exports to China. In the meantime, China has committed to eliminate all quantitative restriction and adopt tariff-rate quotas (TRQ, i.e., a system in which imports up to the quota level are charged a minimal tariff—usually 1–3 percent—and above that level a high tariff). This system provides a strong incentive for state enterprises to purchase bulk commodities at world market rates. In addition, China will end export subsidies of agriculture commodities. This should be regarded as a major concession from the Chinese side given that total elimination of agricultural export subsidies will not be discussed until the next WTO round after 2000. Overall, the U.S. Department of Agriculture estimated that American farm exports to China would rise by $2 billion within five years.

Another important beneficiary is the U.S. automobile sector. In a separate package, China agreed to phase down its tariff from 80–100 percent to 25 percent on cars, from 50 percent to 10 percent on parts by 2006 and to grant foreign car manufacturers the authority to provide financing for car purchases from the date of China's WTO accession. In addition, foreign auto companies are given full distribution rights and trading rights, which means that foreign companies will be able to import and export without Chinese middlemen and provide after-sale repair and maintenance.

Probably the biggest winners are American telecommunications and Internet companies, which can finally exploit the Chinese telecom

and Internet market, as well as financial services. China will end all geographic restrictions for paging, Internet service, mobile, voice, and data services within the country. Foreigners may invest in Chinese Internet businesses and own up to 50 percent of Chinese telecom ventures in two years. Foreign banks also may offer services to Chinese customers in two years and own 33 percent of other financial services providers (later increased to 49 percent). These changes will finally open a vast consumer and commercial market in the Chinese finance industry.

The gains in the above sectors, however, will substantially expand U.S. services trade with China in which the United States has already enjoyed a surplus and may have less impact on improving the merchandise trade balance with China in the near future.

The only loser seems to be the U.S. textile industry. According to the agreement, the United States will abandon quotas on Chinese textile imports in 2005. But many analysts contend that fears about a big surge of Chinese textile imports to the United States are overstated and that this agreement will not change the picture all that much. The vast majority of Chinese exports to the United States basically come at the expenses of other foreign suppliers, and so one wouldn't expect significant additional pressure from this deal.[1]

To be sure, China's entry into the WTO could boost China's overall exports, including exports to the United States. But these exports usually contain some imported components, thus increasing China's demand for U.S. merchandise. As many analysts pointed out, the PNTR will not set off a new import surge because the United States is already open to most imports from China. The new deal would ease only the entry of U.S. exports to China, not the other way around.

What is more, under the agreement, the United States also managed to put a series of special rules in place to protect against the possible sudden influx of Chinese imports using so-called safeguards. Under current WTO rules, nations can institute safeguards for a four-year period, renewable once. They cannot single out individual nations for

special action, and they must gradually phase out the protection. Under the U.S.-China deal, however, the United States forced China to accept this highly protectionist action for twelve years (in the textile sector for nine years).

In addition, the U.S. negotiators have succeeded in blocking Chinese imports to the United States through the application of antidumping methodology. As the recent WTO meeting in Seattle demonstrated, most developing as well as developed countries condemn antidumping actions as a protectionist front for uncompetitive domestic industries. The Clinton administration continued to define China as a "nonmarket economy" for fifteen years, thereby perpetuating an even more arbitrary methodology to determine whether Chinese exports are "selling below costs." Using nonmarket criteria allows the complainant to ignore local Chinese prices and use surrogate or constructed prices. The U.S. Commerce Department repeatedly used this practice to manipulate data and ably blocked Chinese exports over the years. Although U.S. law and regulations provide for graduation of sectors or an economy as a whole, as Charlene Barshefsky, the U.S. trade representative, stated, from nonmarket rules, in practice U.S. government agencies in recent years have always succumbed to interest groups' pressure against such graduation. Therefore, China will receive antidumping treatment for the full fifteen years.

From the above overview we can see that the terms of the new deal would, at least in theory, boost U.S. exports to China and reduce Chinese imports to the United States, thus improving the bilateral trade imbalance about which the U.S. government and public always complained. But there is no guarantee that this will happen unless both countries resolve the above-mentioned long-standing disputes.

The U.S.-China Trade Imbalance

China and the United States have totally different official estimates of the bilateral trade imbalance. According to U.S. official data, the

Table 1 Chinese and U.S. Trade Data (in billions of U.S. dollars)

	DATA FROM CHINESE CUSTOMS				DATA FROM U.S. CUSTOMS			
Year	*Total Trade Value*	*Exports to the United States*	*Imports from the United States*	*Trade Balance*	*Total Trade Value*	*Imports from China*	*Exports to China*	*Trade Balance*
1990	$11.77	$5.19	$6.58	$−1.39	$20.03	$15.22	$4.81	$−10.47
1991	14.20	6.19	8.0	−1.81	25.26	18.98	6.28	−18.26
1992	17.50	8.59	8.90	−0.31	33.20	25.73	7.47	−18.26
1993	27.65	16.96	10.69	6.28	40.30	31.53	8.77	−22.77
1994	35.43	21.46	13.97	7.49	48.07	38.78	9.29	−29.49
1995	40.83	24.71	16.12	8.59	57.30	45.55	11.77	−33.78
1996	42.84	26.68	16.15	10.53	63.36	51.49	11.99	−39.50
1997	48.99	32.69	16.30	16.40	75.36	62.52	12.80	−49.75
1998	54.94	37.98	16.96	21.01	85.41	71.16	14.26	−56.90
1999	61.47	41.94	19.53	22.41	94.91	81.79	13.12	−68.67

Sources: *United States Foreign Trade Highlights*, U.S. Department of Commerce, various years; *China Customs Statistics*, various years.

United States ran a merchandise trade deficit of $68.6 billion with China in 1999, whereas the Chinese statistics put this figure at $22.4 billion—a difference of $46.2 billion (see table 1). If China and the United States cannot agree on a fair, scientific, and mutually accepted method of calculation, the U.S. deficit in dollar terms will continue to widen. The U.S. media even spread a sensational story that the U.S. trade deficit with China could soon exceed the U.S. deficit with Japan.

The main reason for this big discrepancy between Chinese and U.S. data seems to be the different methods used to calculate Chinese exports via Hong Kong. The United States uses a country of origin principle that records Chinese goods reexported by Hong Kong to the United States as Chinese exports. The PRC, using a country of destination principle, excludes those goods exported to Hong Kong and reexported to the United States from Chinese exports to the United States for the following reasons:

1. The export value data are compiled from Chinese Customs, which has no specific knowledge of the ultimate disposition of those goods exported to Hong Kong, whether consumed in Hong Kong or reexported to third countries. This is why China has incurred a huge trade surplus with Hong Kong for decades.
2. The goods exported by China to Hong Kong may be reexported to many countries, not only the United States. So Chinese Customs finds it difficult to determine the value of the reexported goods to the United States unless it gets prior information of that value.
3. The reexports of Chinese goods from Hong Kong to the United States have contained value added by Hong Kong firms, which may include Hong Kong's profits from marketing, product development, banking and insurance services, transportation, and storage. Chinese Customs has no way to calculate such values.

What makes the bilateral trade picture more complex and unfair is that the U.S. Customs, which counts Chinese exports to Hong Kong that are then reexported to the United States as Chinese exports to the United States, does not treat U.S. goods that are first shipped to Hong Kong and then reexported to China as U.S. exports to China. This grossly understates the real value of U.S. exports to China, distorts the bilateral trade balance, and swells the U.S. trade deficit with China.

Since 1993, Chinese Customs has improved the data-compiling method by trying to differentiate between goods exported to Hong Kong that are reexported to the United States and goods that are consumed in Hong Kong or reexported to third countries. Those that are reexported to the United States are recorded as Chinese exports to the United States. So, in my view, from 1993 onward the Chinese data on Sino-U.S. trade are more reliable. Because the reexported goods in Hong Kong change ownership, however, it is difficult for Chinese Customs to

know their final destinations. As we can see in table 1, Chinese data show a significant surge in China's trade surplus vis-à-vis the United States.

If the reexports were only a small part of Sino-U.S. trade, we could just ignore them. But Hong Kong is playing an increasingly important role in the marketing of Chinese goods in the United States. These reexports, then, are a large portion of Sino-U.S. trade. According to Chinese data, total exports to the United States in 1998 amounted to $38 billion. Reexports from China via Hong Kong to the United States amounted to $31 billion, or 81.5 percent of the total exports to the United States. Hence, any estimates of the Sino-U.S. bilateral trade balance that do not adjust for reexports will be totally inaccurate.

Many economists in the United States, China, and Hong Kong have made efforts for years to adjust Sino-U.S. trade figures. Nicholas Lardy, for example, used the method of taking into account the U.S. goods sold initially to Hong Kong and then reexported to China that are omitted from U.S. Department of Commerce data, as well as subtracting the value added by Hong Kong firms to imports from the PRC to the United States via Hong Kong. He concluded that the U.S. trade deficit with China in 1997 was $36.15 billion instead of $49.74 billion. From 1988 to 1997, he estimated that the United States overstated its trade deficit with China by anywhere from 37 to 126 percent.[2]

In K. C. Fung and Lawrence Lau's more comprehensive study, they first adjusted official U.S. trade data (deficit of $56.9 billion with China in 1998) on a free on board (FOB) basis rather than on a cost, insurance, and freight (CIF) basis, which may be 10 percent above the FOB cost. Furthermore, they adjusted the exports of both countries to each other for reexport via Hong Kong that are not calculated in U.S. official data. The results decrease the U.S. trade deficit with China by another $11 billion. Finally, the two scholars point out that U.S. imports from China via Hong Kong contain Hong Kong markups, which are estimated at about 25 percent of the cost of the reexport goods. By subtracting those markups, they concluded that the U.S. merchandise trade deficit with

China in 1998 was $36.9 billion instead of $56.9 billion.[3] Fung and Lau's findings, however, missed part of the issue, which is that outward processing accounts for a large proportion of Chinese exports to the United States. China has argued that the valued-added content of Chinese exports to the United States is low. Fung and Lau admitted that "there is some truth in the Chinese arguments" but that "additional research is required to resolve this interesting question."

Again, if China's processing part in Sino-U.S. trade is small, we can ignore it. The fact is, however, it is a large proportion, accounting for 72 percent of China's exports to the United States in 1997 and 71 percent in 1999.[4] Indeed, since China's opening up and economic reforms, more and more foreign, including American and overseas, manufacturers have shifted their production and assembly lines to China, especially those from Hong Kong and Taiwan. Final products of these ventures are exported to the United States or other countries. Two major categories of such kind of production are contractual processing and ordinary processing. *Contractual processing* refers to processing and assembling raw materials or components supplied by foreign firms for a fee. The processed outputs belong to the foreign firms and are exported by them. *Ordinary processing*, on the other hand, refers to processing with imported materials. Most of these businesses are fully foreign-owned enterprises, equity joint ventures, and contractual joint ventures. Instead of earning a processing fee, as in the case of contractual processing, foreign firms sell the processed exports for a profit. Most returns to capital generated by these enterprises do not accrue to the Chinese government. The processing margin rate, which is quite low, can be simply represented in the following formula,

$$M = \frac{(E - I)}{E}$$

where M is the processing margin rate, E is the exports value, and I is the imported material value.

Chinese scholar Y. W. Sung, using Chinese Customs and Hong Kong statistics, estimated the Chinese processing margin rate for Hong Kong–owned enterprises over the period 1992–1997 at 23.9 percent.[5] Professors Kueh and Voon of Hong Kong concluded that, in Hong Kong– and Taiwan-owned firms in China making export products, China contributed on average only about 27.2 percent to the total cost of processing goods.[6] The reason China value-added content is so low is that foreign (including American) and overseas (mainly Hong Kong and Taiwanese) partners play a major role in the value-added process. They perform substantial initial and final value-adding services for processing operations in China, including product design, production technology, production management, marketing, raw material sourcing, quality control, financing, shipping, and so forth, whereas China performs only the functions of assembly or fabrication.

For labor-intensive goods, the Chinese processing margin rate is even lower. Take the Barbie doll made in China as an example.

Retail price in U.S. toy store	$9.99
China's export price	$2.00
Raw materials (Middle East)	
Processed into semiproduct (Taiwan)	
Wigs (Japan)	$1.00
Packing materials (U.S.)	
Transportation and management fee	$0.65
China's processing fee	$0.35
China's processing margin rate	17.5%

A foreign-owned firm in China produces the Barbie doll. As we can see from above, most of its profit goes to Middle East, Taiwan, Japan, and the United States. China earns only a paltry $0.35 as processing fee. Under the country-of-origin rule, the $2 unit price was added to China's export value to the United States, which in no way reflects the real trade balance between the two countries.

As the above example shows, the existing single-country-of-origin (SCO) rules simply do not reflect the origin of production. Using these rules, the importing country often regards the outward-processing country as the origin of its imports, though the latter's value added could be very small by proportion. SCO rules also do not take into account the multiple flows of processing goods between importing and processing countries prior to exporting to a third country. As more and more labor-intensive goods have been shipped to China for processing and assembling, China has been mistakenly treated as the origin of production. The SCO rules "punish" the country to which goods are sent for processing and assembling.

Thus, a multiple-country-of-origin (MCO) rule appears conceptually to be more fair and appropriate. Unlike SCO, MCO facilitates the measurement of value-added contribution by two or more partner countries in their processing production and export. It allows each country's current account to be compiled using the value-added export and import figures.

J. P. Voon and Y. Y. Kueh, adjusting Chinese exports to the United States on a MCO basis, reported an even lower U.S. trade deficit with China in 1997, only $14.12 billion, rather than $49.74 billion as the United States claimed. They stated that the unadjusted statistics were inflated in all cases by about 250 percent relative to the adjusted ones.[7]

In summary, if we take into account China's processing content of its exports to the United States that was omitted in both Lardy's and Fung and Lau's estimates, and assume that more than 70 percent of Sino-U.S. trade is processing at around 27 percent of China's processing margin rate, the U.S. trade deficit with China adjusted by Lardy and Lau should be scaled down substantially, perhaps close to Voon and Kueh's estimates. Thus, in my view, the Chinese official data are more accurate and reliable. That is, the U.S. deficit with China in 1997 was around $16 billion and in 1998, $21 billion (see table 2).

To be sure, the United States still incurred a trade deficit with China. But if we consider three more factors, the deficit seems not so

Table 2 Comparative Estimates of U.S. Trade Deficits with China (in billions of U.S. dollars)

	U.S. Official Data	*Chinese Official Data*	*Lardy's Estimates*	*Fung and Lau's Estimates*	*Voon and Kueh's Estimates*
1997	$49.7	$16.4	$36.1	$29.8	$14.1
1998	56.9	21.0	—	36.9	—

serious. First, there is a "trade transfer effect" between the United States and its Asian trading partners. As mentioned above, China's foreign partners, particularly Hong Kong, Taiwan, and other Asian countries, have successfully exported to the United States by outward processing in China. China's trade surplus with the United States is largely a mirror image of the shrinking trade surplus of the Asian partners vis-à-vis the United States. The U.S. trade deficit with China must therefore be looked at in a regional context, not in isolation. Second, by the end of 1998, American direct investment in China had reached $21.4 billion. For example, Motorola set up factories in China, sold products in the Chinese market, and remitted profit back to the United States. It actually substituted China's import of mobile phones from the United States, and its profit offset part of the U.S. merchandise trade deficit with China. Third, the U.S. trade deficit we are talking about refers to merchandise trade. But the United States strength is in the service sector in which it had a $1.6 billion surplus with China in 1998. It is predicted that that could grow substantially under the WTO deal, by $3 billion, to $5 billion a year.[8] Indeed, since 1990, sales by U.S. firms to China have more than tripled, making China the most rapidly expanding of the top ten U.S. foreign markets (see table 3).

By any measurement, the U.S. trade imbalance with China is significantly smaller compared to that with Japan. There is no reason to make the trade issue a hostage in the U.S. domestic partisan struggle and thus poison Sino-U.S. political relations. The issue of the calculat-

Table 3 Largest U.S. Export Markets (ranked by export growth)

		VOLUME (IN U.S.$ BILLION)		AVERAGE GROWTH (IN %)
Rank	*Country*	*1990*	*1997*	*1990–1997*
1	China*	$5.978	$18.386	17.41%
2	Mexico	28.375	71.378	14.09
3	Singapore	8.019	17.727	12.00
4	Canada	82.957	150.12	8.84
5	Taiwan	11.482	20.388	8.55
6	South Korea	14.399	25.067	8.24
7	United Kingdom	23.484	36.435	6.48
8	Netherlands	13.016	19.822	4.40
9	Japan	48.585	65.673	4.40
10	Germany	4.807	12.805	3.92

*Adjusted for U.S. goods initially sold to Hong Kong and then reexported to China. If using unadjusted (i.e., U.S. Department of Commerce) data, the growth rate would be 15.02 percent, still the fastest among the top ten. See Lardy, statement to the Senate Committee on Foreign Relations.

ing methodology is complex. Both China and the United States can talk on how to unify the two different principles in calculating bilateral trade flows. A multilateral negotiation is under way within the framework of the WTO on the "Harmonized Rules of Origin" but is yet to be completed. Any unilateral overstatement and politicizing of this issue would not be conducive to resolving the bilateral trade problems.

Technology Transfer and U.S. Sanctions

The most important factor for the Sino-U.S. trade imbalance appears to be the U.S. economic sanctions and high-technology export control to China. The Sino-U.S. WTO accord has not resolved this issue.

If the United States intends to expand its exports to China, it should pay attention to the changes of demand in Chinese market. Traditional U.S. export goods to China such as wheat, fertilizer, steel, and so on no

longer appeal to Chinese customers because China can now export these products. At present, China is speeding up its modernization programs, needing to import advanced technology and equipment worth tens of billions of U.S. dollars each year. If the United States cannot adjust its structure of export goods to cater to the new market needs, its export volume will not increase.

In 1983, the Reagan administration decided to move China from Group P (most restrictive in export control) to Group V (less restrictive involving such non-ally but U.S.-friendly countries as Yugoslavia and Egypt) in the list of countries under export control, then extended its "green area" of technology transfer to China to thirty-two categories. That easing of controls led to a fast growth in U.S. exports to China. In early 1989, the U.S. Department of Commerce further relaxed its restriction on technology exports to China in thirteen categories. And the United States basically maintained a trade surplus with China until the early 1990s, when it started to impose economic sanctions against China.

The U.S. sanctions against China are comprehensive and cover a broad range of technology and equipment. Among others, the export of satellites is prohibited; nuclear trade and cooperation are suspended; the control of "dual-use" technologies has been tightened, including that of high-performance computers, machine tools, telecommunication equipment with encryption capability, mobile phone technology known as CDMA (code division multiple access); export licenses for crime control and detection equipment are prohibited; and Overseas Private Investment Corporation and Trade and Development Program activities have been suspended.

In the early 1980s, Chinese firms began to talk with Westinghouse and General Electric about purchasing nuclear power plant equipment for Qinshan (300,000 kilowatts) and Daiya (900,000 kilowatts). Due to U.S. export controls, however, these long talks ended in failure. Despite China and the United States concluding an agreement on peaceful utilization of nuclear energy in 1985, the U.S. Congress refused to ratify

it until early 1998. This agreement has never been implemented due to the political furor in the United States about so-called Chinese espionage. In fact, the potential of the Chinese nuclear power market is huge. At present, there are only three nuclear power stations in operation. It is estimated that, before 2020, China will increase its nuclear power capacity by at least 50 million kilowatts. American nuclear power equipment suppliers' exports to China could reach $1.6 billion annually, which could create 25,000 high-paying jobs.

China and the United States may also have an opportunity to cooperate in the area of space programs. In fact, using a Chinese rocket to launch an American commercial satellite (such as it did in Loral's case) saved at least $50 million for U.S. space companies. Cooperation between the two countries in this area could bring tremendous benefits to American businesspeople. For political reasons, however, the U.S. government has banned such cooperation in the future. In early 1999, Washington denied export of a satellite to China worth $450 million.

As China begins to upgrade its industrial structure, it needs to import machine tools, computer chips and parts, and telecommunication equipment, but the U.S. government has barred almost all these items. Pentium III computers can be purchased in every computer store or from on-line dealers all around the world, but the sale of such microprocessors by U.S. firms to China requires U.S. government special approval. The U.S. government has put China in a Tier III category, meaning that computers which have speeds of 2,000 MTOPS (millions of theoretical operations per second) cannot be exported, despite the fact that current speeds have long exceeded 2,000, reaching 10,000 to 30,000 MTOPS. Again, the long review process cost U.S. businesspeople billions of dollars.

The U.S. economic sanctions against China have proved counterproductive in terms of expanding U.S. exports to China; other developed countries have used the opportunity to grab lucrative Chinese markets from American companies. When the U.S. government denied Westinghouse's sale to China in the 1980s, European and Japanese

companies sold $15 billion in nuclear power technology to China. As a result, Westinghouse has reportedly been forced to lay off 3,500 workers. As many American business leaders pointed out, the recent restriction of CDMA equipment able to be exported to China could cost U.S. firms such as Motorola and Lucent billions of dollars. Continuing the existing export control would hurt American companies more than it would hurt China, they stated, because Chinese customers can go elsewhere to buy advanced technology from licensed dealers.

Although the United States is the most advanced country in the world in terms of science and technology, it accounts for only a relatively small share of China's technology imports. At American expense, Japan and the European Union have steadily increased their market share in the Chinese technology market. In 1998, the United States contracts for technology transfer to China were valued at only $3 billion, amounting to 18.3 percent of all foreign technology transfer to China. In the same year, the United States exported to China machinery and electronic products worth only $8.9 billion, while Japan's value of the same exported products to China was $15.1 billion, and the European Union's, $14.8 billion. Whereas the United States still maintains the economic sanctions it imposed against China after the spring of 1989, Japan and the European Union lifted theirs within a few months and have since incurred surpluses in their trade with China. In 1990, U.S., European, and Japanese exports to China were roughly equal. Since that time, European exports have grown 1.5 times faster than U.S. exports, and Japanese exports have grown twice as fast. Meanwhile, these countries also aggressively and generously extended export financing and aid programs to China that the United States has barred.

It is contradictory that the United States, on the one hand, underscores its trade deficit with China but, on the other hand, does not want to lift export restrictions on China. This has become the main obstacle in developing and expanding Sino-U.S. trade and economic ties. Both Chinese and American business circles call for relaxation of export

control, restoration of the Trade and Development Program, and Export-Import Bank's credit.

Imposing sanctions or threatening retaliation is not a solution. Both violate the principle of multilateral trade system, work against effective settlement of disputes, and make the issue even more complicated.

Alleged Currency Manipulation

Another Sino-U.S. economic issue has been U.S. charges of China's allegedly manipulating its exchange rate. According to the 1988 Trade Act, the U.S. government assesses annually whether its trading partners manipulate their exchange rates in order to gain unfair competitive advantage in their trade with the United States. Since 1992, the U.S. Treasury Department concluded, and reiterated in the following years, that China was manipulating its exchange rate and currency reserves and thus impeding U.S. exports to China.

At the height of the Asian financial crisis in the second half of 1997 through 2000, however, the United States applauded this "manipulation." President Clinton, Treasury secretary Robert Rubin, Federal Reserve chairman Alan Greenspan, and Secretary of State Madeleine Albright have lavishly praised China for holding its exchange rate constant in the face of massive devaluation in other Asian countries.

Paradoxically, the United States has insisted on its long-standing demand for a rapid opening of China's financial market and set it as a condition for China's entry into the WTO. Does not the United States know that liberalization of financial systems would certainly lead to a real devaluation of China's currency?

How to interpret these inconsistent, conflicting attitudes toward China's exchange rate system? Apparently, the groundless charges of China's manipulation of currency were used to press China to reduce its trade surplus with the United States. The current U.S. urge to hold Chinese currency stable may also derive from self-interest. According

to some estimates, a devaluation of the renminbi by 5 percent would add $4.3 billion to the U.S. trade deficit with China.[9]

The fact is that when the U.S. Treasury Department charged in the early 1990s that the renminbi's exchange rate was manipulated and devalued by the Chinese authorities, China was then running a global trade deficit. It is hard to sustain an argument that a currency is undervalued while the country is running a trade deficit.

Moreover, the renminbi's value has experienced an upward trend after the exchange rate reform in 1994. Since supply of foreign exchange was higher than demand in the market, some modest appreciation was subsequently recorded, leaving the renminbi's value change from 8.7:1 in 1994 to 8.27:1 in 1998 and 1999, a 4.8 percent appreciation (see table 4).

Several factors seemed to determine the upward movement of the renminbi's value. The new rule of buying and conditionally selling foreign exchanges by banks has brought most foreign exchange enterprise income into the market. In the meantime, demand for foreign exchanges has been restricted in scope and quantity. In addition, since 1994 China has run a trade surplus, reaching $4.3 billion in that year and $19.5 billion in 1996; thus supply of foreign exchange in the market was significantly augmented. The country has also recorded a surplus in its capital account, reaching $32.6 billion in 1994 and $22.9 billion in 1997; this is the major reason for the renminbi's appreciation. When China formally joins the WTO and the commodity and capital markets are liberalized, however, the current renminbi's exchange rate might change.

Lower tariffs will mean a steep rise in imports, which will put pressure on China's current account balance. In 1999, China enjoyed a trade surplus of $29.1 billion. But it is predicted that this surplus will gradually decline and reach a break-even point five years from now. In the meantime, foreign debt will be due incrementally during this period. Repaying the bulk of foreign debt may turn the current account to a deficit. Although the capital account might still keep a positive balance

Table 4 Renminbi's Exchange Rate (1 U.S. dollar vs. yuan)

Jan. 1, 1994	Dec. 31, 1994	Dec. 31, 1995	Dec. 31, 1996	Dec. 31, 1997	Dec. 31, 1999
8.7000	8.4462	8.3174	8.2984	8.2798	8.2799

Sources: China Statistic Yearbook; midpoint exchange rate published by People's Bank of China each day.

largely due to increased foreign direct investment, possibly no less than $40 billion a year, the profits of foreign investors could reach $100 billion. Should all these proceeds remit from China, the foreign exchange reserve, which now stands at $158 billion, could be drained. Then the renminbi's exchange rate will face pressure of devaluation.

If a more flexible, floating foreign exchange rate arrangement could be adopted, it should be regarded as a consequence and cost of China's WTO accession, not a so-called currency manipulation by the Chinese government. But more likely, for the time being, in the light of huge foreign exchange reserves, the Chinese central bank will liberalize the currency regime by allowing the renminbi to move in a slightly wider trading band in line with market demand.

Human Rights and Trade

The U.S. Congress has no power to approve or deny China's accession into the WTO; it can only decide whether to extend permanent most favored nation (MFN) (now PNTR) status to China. According to general WTO requirements, any WTO member should extend to all other members permanent and unconditional MFN. But the U.S. Congress, using the excuse of the so-called human rights conditions in China, decided to extend MFN on the basis of an annual review. Every year, from 1990 to 1999, a heated debate on China's MFN treatment among different parties and interest groups has wasted much political energy and the money of American taxpayers.

On May 24, 2000, the U.S. House of Representatives finally voted, by a majority of 237 to 197, to grant PNTR to China. Under the legislation, the United States would eliminate the annual congressional review of China's trade status, thus removing the largest barrier to the implementation of the U.S.-China trade agreement reached last November. However, the bill also contains provisions on creating a new congressional commission to monitor human rights in China. This precedent—linking major trade legislation to human rights—will cause friction in future U.S. trade relations with China, as well as with other nations.

Linking human rights with MFN not only conflicts with the fundamental principles of GATT and WTO, it also lacks a legal source. The Jackson-Vanik Amendment to the Trade Act of 1974 conditioned freedom of emigration to the MFN. A legacy of the cold war, it was aimed at the free emigration of Soviet Jews from the former Soviet Union. There is not a single word in this law about human rights as stipulated in President Clinton's May 1993 executive order. As for China's emigration policy, Deng Xiaoping once offered to allow as many as ten million Chinese to emigrate to the United States annually. Will the United States accept?

The MFN treatment has become a global standard for normal trade. It does not render a favor but assumes reciprocal obligations. More than 120 countries now have lower tariff rates than those under MFN; every country enjoys the Generalized System of Preferences (GSP). Only eight countries do not have MFN. Trade is trade. It should not be linked with noneconomic issues. Although many ordinary Chinese would agree that the human rights situation in China is far from perfect, they might question the human rights situation in the United States, too: its high crime rate, explicit racial discrimination, and many citizens living below the poverty line. All these point to the fact that at least two freedoms—freedom from want and freedom from fear—have not been completely realized in the United States. People might ask why doesn't

the United States improve its human rights first before trying to change other nations'?

No other nation would support the U.S. policy of linking trade preferences to human rights and follow the United States in its course of action. Many Asian leaders criticized America's "double standard" with respect to race, culture, and civilization and complained that the U.S. emphasis on human rights concentrated more on Asia than other parts of the world. In a WTO ministerial meeting in Seattle in late November 1999, the United States again tried to put a "human face" on the global trade issues and threatened to use sanctions if the WTO is not able to work out labor standards for wages, working conditions, and other labor issues. Delegates from developing countries were angered by the U.S. statement and warned that they could walk away from any agreement on a new round of talks.

Conclusion

The trade frictions and disputes between China and the United States mainly fall in the area of economic benefits distribution among certain industries and enterprises and are not related to the fundamental national interest of either country. They can be settled through negotiations on equal basis, which has been fully proved by past experience. Within the next six years, from 2000 to 2005, in order to meet the need of modernization programs, China's import value will exceed $1,300 billion. The year 1999 has already seen a significant increase in Chinese imports. If the United States can rid itself of the interference of noneconomic factors in its trade relations, lift the outdated sanctions against China, and relax its export control, American medium- and large-sized enterprises will be able to capture more Chinese market share. American capital, technology, and managerial skills combined with China's huge market, low-cost labor, and resources will bring tremendous benefits to the economic growth of both countries.