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*Instituto Universitario
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Universidad San Pablo



Documento de Trabajo
Serie Unión Europea
Número 44 / 2011

**China and the Global
Political Economy**

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China and the Global Political Economy

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CEU Ediciones

Julián Romea 18, 28003 Madrid

www.ceuediciones.es

Instituto Universitario de Estudios Europeos

Avda. del Valle 21, 28003 Madrid

www.idee.ceu.es

ISBN: 978-84-92989-82-9

Depósito legal: M-19752-2011

Maquetación: Servicios Gráficos Kenaf s.l.

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1. New Chinese Foreign Policy under the Hu Jintao Leadership

After end of the Cold War, Mr Deng Xiaoping, the Chinese leader, put forward the “24 Character Strategy” as the basic principles for Chinese foreign policy, which include “Observe calmly; secure our position; cope with affairs calmly; hide our capacities and bide our time; be good at maintaining a low profile; and never claim leadership” (冷静观察, 稳住阵脚, 沉着应付, 韬光养晦, 善于守拙, 决不当头)¹. Another 4 characters were added later, “do something” (有所作为). The strategy is the guideline for Chinese foreign policy under the leadership of both Mr Jiang Zemin (1989-2002) and Mr Hu Jintao (2002-now).

Entering into the 21st Century, many Chinese government officials and scholars believed that China had a twenty-year “Strategic Opportunity”. This idea first appeared in the Political Report of the 16th National Congress of the Communist Party of China (CPC) in 2002 when Mr Hu Jintao replaced Mr Jiang Zemin as the Secretary General of the Party and then the President of the State in 2003. The assumption behind the “Strategic Opportunity” is that China has had a peaceful international and stable neighbouring environment due to China’s economic growth and more active international engagement.

In order to take advantage of this Strategic Opportunity, in October 2007 the 17th National Congress of the CPC highlighted certain new tendencies in Chinese foreign policy.

1.1. Strategic objectives of Chinese foreign policy and the harmonious world

The strategic objectives of Chinese foreign policy include three points. (1) Sharing opportunities for development; (2) Rising to challenges together; (3) Promoting the noble cause of peace and development of humanity. In order to reach these goals, the proposition of China is to join hands with the people of all countries and strive to build a harmonious world of lasting peace and common prosperity.

What is the real meaning of a harmonious world? There are two key words and five main elements. The two key words are *lasting peace*, and *common prosperity*. The five elements are: (1) Politically, all countries should respect each other and conduct consultations on an equal footing in a common endeavour to promote democracy in international relations. (2) Economically, they should cooperate with each other, draw on each

¹ The translation is according to the *Annual Report to Congress: Military Power of the People’s Republic of China, 2007* (Washington, DC: Office of Secretary of Defence, 2007, p.6)

other's strengths and work together to advance economic globalization in the direction of balanced development, shared benefits and win-win progress. (3) Culturally, they should learn from each other in the spirit of seeking common ground while shelving differences, respect the diversity of the world, and make joint efforts to advance human civilization. (4) In the area of security, they should trust each other, strengthen cooperation, settle international disputes by peaceful means rather than by war, and work together to safeguard peace and stability in the world. (5) On non-traditional security issues such as energy and climate change, they should assist and cooperate with each other in conservation efforts to take good care of the Earth, the only home of human beings.

Although many Chinese commentators have emphasized that the Harmonious World is the initiative of Mr Hu Jintao, if we look at the official documents of the Communist Party of China, there are some pre-conditions for attaining the ideal harmonious world, which include upholding the tenets and principles of the United Nations Charter, observing international law and universally recognized norms of international relations, and promoting democracy, harmony, collaboration and win-win solutions in international relations. In other words, the Chinese concept of the harmonious world is based upon universal norms that come from the Western tradition rather than the ancient Chinese cultural tradition.

1.2. China's relationships with the outside world

In the 16th National Congress of the Communist Party of China in 2002, the Chinese leadership started to rank the relationship with the developed countries, or Western countries, as its first priority. The ranking of Chinese foreign relations put developed countries first, neighbouring countries second, and third world countries or developing countries last. The 17th National Congress of the CPC kept the same ranking with different definitions or priorities.

Relationships with developed countries. In 2002 the emphasis was to improve and develop relations with the developed countries. Proceeding from the fundamental interests of the people of all countries concerned, we would broaden the converging points of common interests and properly settle differences on the basis of the Five Principles of Peaceful Coexistence, notwithstanding the differences in social system and ideology. In 2007 the focus was to continue to strengthen strategic dialogue, enhance mutual trust, deepen cooperation and properly manage differences to promote long-term, stable and sound development of bilateral relations. We can see that the Chinese leadership puts the relationship with developed countries as the most strategic one and would like to have a long-term, stable and sound bilateral relationship with them.

Relationships with neighbouring countries. In 2002, China would continue to cement our friendly ties with our neighbours and persist in building up a good-neighbourly relationship and partnership with them. We would step up regional cooperation and increase our exchanges and cooperation with our surrounding countries. In 2007, the emphasis was to follow the foreign policy of friendship and partnership, strengthen good-neighbourly relations and practical cooperation with them, and energetically engage in regional cooperation in order to jointly create a peaceful, stable regional environment featuring equality, mutual trust and win-win cooperation.

Relationships with developing countries. In 2002 what the Chinese leadership stressed was to enhance solidarity and cooperation with other third world countries, increase mutual understanding and trust and strengthen mutual help and support. We would enlarge the areas of cooperation and make it more fruitful. In 2007 China would like to continue to increase solidarity and cooperation with them, cement traditional

friendship, expand practical cooperation, provide assistance to them as far as we are able, and uphold the legitimate demands and common interests of developing countries. The key words here are traditional friendship, practical cooperation, assistance as far as we are able.

To summarise, China upgrades its relationship with developed countries to the level of a strategic relationship, and pays more attention to pragmatic cooperation with its neighbours and other developing countries.

Within the Chinese foreign policy agenda, the position of two major countries is not very clear, i.e. Japan and Russia. Japan should be part of the developed countries, as well as neighbouring countries. Russia is not one of the developed countries, and only a neighbouring country.

According to this agenda, the United States and the EU as well as the EU member states are the most important partners for China, and Japan and Russia are next. Other neighbouring countries such as ASEAN and the South and North Koreas are third. Developing countries in Africa and Latin America are at the lowest level.

1.3. Keeping a low profile in international affairs

There were big debates on the issues of the ‘peaceful rise’ several years ago in China, especially in 2003. The major argument regarding the concept of the peaceful rise was if China should continue to keep a low profile or it should take a more active role in global affairs. The Chinese leadership gave up the peaceful rise concept and changed it to the concept of peaceful development.

The 17th National Congress of the CPC emphasized very strongly that “China will unswervingly follow the path of peaceful development. This is a strategic choice the Chinese government and people have made in light of the development trend of the times and their own fundamental interests”. And at the same time, the major contribution of China to regional and global development is “through our own development, and effort in the areas where our interests meet with those of various parties”.

China’s low profile diplomacy can be reflected by some very important changes in its foreign policy statement in the 17th Party Congress.

First, there is no mentioning of setting up a new international order, a slogan China started to use from the 1970s. There is even no mentioning of reforming the old international order, but only an emphasis on “working to make the international order fairer and more equitable”. It seems that this is the first time that the Chinese leadership clearly recognizes the legitimacy of the current international order in an official document.

Secondly, there is no mention in the report of the so-called comprehensive national capabilities and China as a great power in world affairs. There is continued emphasis on China still being a developing country. There is also no word regarding China as a responsible power. The emphasis is on China being part of the interdependent world, and that China would like to work with everybody in the world. There is a mention that China will continue to take an active part in multilateral affairs and assume its due international obligations. In comparison with the 16th Party Congress in 2002 when the CPC stated that “we will continue to take an active part in multilateral diplomatic activities and play our role in the United Nations and other international or regional organizations”, this is a more active stance.

1.4. Multilateralism and responsible power

Before 2000 what China always emphasized was multipolarity, which has been the official discourse for many years, rather than multilateralism. Some Chinese scholars started to challenge the concept of multipolarity in the later 1990s, advocating pluralism as its replacement, and arguing that the tendency in the post-cold war international system was non-polarity instead of multipolarity². In July 2001, Chinese scholars discussed multilateralism and multilateral diplomacy during a workshop in Beijing and 8 papers were published by *World Economics and Politics*, a very influential academic journal on international studies in China, in October 2001³. It was the first time that Chinese scholars looked at multilateralism from both theoretical and policy perspectives. The main Chinese understanding of multilateralism in early 2000s was very much the same as balance of powers and multipolarity. As some of them argued, multilateral diplomacy was the appropriate approach to the multi-polar world⁴.

The Chinese government started to change the discourse from multipolarity to multilateralism after 2003. Several very important events that may had an influence on the change include, (1) China's accession to the WTO which is regarded as one of the most important global multilateral regimes. China needed to learn and play the multilateral game in international trade regimes. (2) The agenda of UN reform. Chinese emphasized very strongly that the United Nations is the best platform to practice multilateralism, and the UN reforms should be in the interest of multilateralism, and enhance the UN's authority and efficiency, as well as its capacity to deal with new threats and challenges⁵. (3) The promotion of "Effective Multilateralism" by the European Union through the 2003 Solana Report in which the European Union also defined China as the strategic partner of the EU, which was warmly welcomed by the Chinese government⁶. (4) The international, especially the European and trans-Atlantic, debates on unilateralism and multilateralism after the Iraqi War in 2003.

From late 2003, many Chinese leaders and governmental officials started to talk more about multilateralism, rather than multipolarity⁷. Multilateralism was firstly regarded as one of the most important areas of common ground between China and the European Union for constructing the EU-China strategic partnership⁸. Later, multilateralism, especially regional-multilateralism, became the new choice for China's foreign policy in general⁹. In April 2004 during the Foreign Ministerial Meeting of the Asia-Europe Meeting (ASEM) Mr Li Zhaoxing, the Chinese Foreign Minister, used "effective multilateralism" officially for the first time in his speech. "Reality has proven that multilateralism is the effective way to deal with the common challenges we are facing, the appropriate measure to settle international disputes, a safeguard to healthy development of globalization, and the best way to promote democratization and legalization of international relations. The key element for establishing an effective multilateralism is a global partnership guided by the new concepts of security, development and civilization, and based upon equality, mutual trust and cooperation¹⁰". Several

² Song Xinning and Chen Yue, *An Introduction to International Politics*, Beijing: Renmin University of China Press, 1999.

³ *World Economics and Politics*, 10 (2001), pp.1-44.

⁴ Shen Jiru, "Multilateral Diplomacy and Multipolar World", in *World Economics and Politics*, 10 (2001), pp.20-24.

⁵ *Position Paper of the People's Republic of China on the United Nations Reforms*, 2005/06/07. From: <http://www.fmprc.gov.cn/eng/zxxx/t199318.htm>

⁶ Song Xinning, "China's View of European Integration and Enlargement", David Shambaugh, Eberhard Sandschneider and Zhou Hong, eds., *China-Europe Relations: Perceptions, Policies and Prospects*, London: Routledge, 2008.

⁷ Song Xinning, "Multilateralism and Responsible Power: New Tendency of Chinese Foreign Policy", in Herausgeberin and Corinna Hauswedell, eds., *Chinas neue Rolle in der Welt: Machtrivalität oder Chancen für mehr Multilateralismus*, Rehburg-Loccum, 75/07, 2009, pp. 153-163.

⁸ Ministry of Foreign Affairs of People's Republic of China, 'Premier Wen Jiabao Meets with Javier Solana', 16 March 2004. From: <http://www.fmprc.gov.cn/eng/zxxx/t80256.htm>

⁹ Liu Changming and Pang Chunen, "From Bilateralism to Multilateralism: New Model for China-East Asia Relations", *Journal of Shandong University*, No. 5, 2007, pp.112-114. See also Jin Canrong, ed., *Multilateralism and east Asia Cooperation*, Beijing: Contemporary World Press, 2005.

¹⁰ Ministry of Foreign Affairs of People's Republic of China, 'Minister Li Zhaoxing's keynote speech on Multilateralism during the Foreign Minister Meeting of ASEM', 17 April 2004. From: <http://www.fmprc.gov.cn/chn/wjdt/zjyh/t85514.htm>

months later Mr Wang Yi, the Vice Minister of Foreign Affairs talked again about multilateralism in his speech at the 14th Ministerial Meeting of the Non-Aligned Movement, regarding it as “the only choice to tackle globalization; and it is the tendency of the new era”. He also gave a new definition of multipolarity. “The multipolarity we proposed is not that which contends for hegemony among great powers in history, but the harmonious co-existence and balanced development of the many forces in order to maintain the stability of the international community¹¹”.

As many people argued, the Chinese understanding of multilateralism is very much different from the European one¹². For the Chinese, multilateralism is a kind of inter-governmental arrangement to deal with common issues. With the regime, every sovereign state is equal and the main principal is non-intervention in other's internal affairs. For China, multilateralism is more like a kind of diplomatic tool rather than a mechanism for international order. So the most popular concept in China is multilateral diplomacy¹³.

The Chinese always have big debates on China's role in world affairs. The official definition of China's position is China as a socialist and developing country. The outside world always mentions China as an emerging power or even an emerging superpower. But most Chinese do not accept this definition. For many of them, China is still a regional power instead of a global power. China has been trying to be a normal member of the international community. But it has not reached that position entirely, because China is still regarded as an OTHER, similar to a rogue state, by many Western people and even governments. China is always put in the same list together with North Korea, Cuba, Iran and Iraq. It is always difficult for Chinese people to travel abroad due to visa restrictions.

Thus, the argument of the Chinese is that, if China is not regarded as a normal member of the international community by the Western states, why should it always be required to bear the obligations of a normal member? The Chinese government has mentioned many times that China would like to be a responsible country within the world community. The concept of stakeholder advocated by the Americans is also well accepted by Chinese officials and scholars. But many ordinary Chinese people do not care very much about this. What they care about is how China is treated by the outside world, especially by the Western countries, i.e. the United States and Europe.

The 17th Party Congress did not mention anything about China as a responsible power. The reasons could be two: Firstly, China has not regarded itself as a global power or even a POWER. In Chinese language “power” has both positive and negative connotations. Secondly, China still believes that the peaceful, stable and sustainable development of China itself, economically, politically and socially, is the greatest contribution to the regional and global development. To be a responsible member of the international community, China should pay more attention to its own domestic affairs instead of external ones. Chinese foreign policy should serve China's domestic development. Because of this inward tendency of Chinese foreign policy, China focuses more on regional multilateral affairs rather than global ones.

¹¹ Ministry of Foreign Affairs of People's Republic of China, 'Promoting Development of Multilateralism and Advancing the Process of World Multipolarity, Speech of Vice Minister Wang Yi at the 14th Ministerial Meeting of the Non-Aligned Movement', 20 August 2004. From: <http://www.fmprc.gov.cn/chn/zxxx/t151070.htm>

¹² Gudrun Wacker, “Same Bed, Different or Compatible Dreams? Commonalities and Differences”, in Stanley Crossick and Etienne Reuter, eds., *China-EU: A Common Future*, Singapore: World Scientific Press, 2007, pp.207-214.

¹³ Shen Jiru, “Multilateral Diplomacy and Multipolar World”, *World Economics and Politics* 10 (2001), pp. 20-24. Liu Changming and Pang Chunen, “From Bilateralism to Multilateralism: New Model for China-East Asia Relations”, *Journal of Shandong University*, No. 5, 2007, p.113.

2. Priorities in Chinese Foreign Policy

The Chinese strongly believe that foreign policy is the continuation of domestic politics and it must serve the national development strategy and domestic politics. The priorities of Chinese foreign policy can be divided into different levels such as domestic versus international, bilateralism versus multilateral, and regional versus global.

2.1. Domestic versus international

After 60 years of the People's Republic of China, especially the opening-up and reform in the last 30 years, China has achieved a great deal in economic development and external relations. But the most important domestic issue is still troublesome to Chinese Communist Party leaders, i.e. the political legitimacy of the Party.

Many Chinese believe that the major challenge to the Communist Party of China nowadays is the legitimacy of the ruling position of the CPC. In the first 40 years of the People's Republic of China, the basis of the legitimacy of the CPC was neither public participation nor social or economic welfare, but the charisma of personal leadership such as Mao Zedong and Deng Xiaoping, the ideology of Communism plus nationalism, and the centralized political system. After 30-year domestic reform and opening up to the outside world, the ideology of Communism has lost its base. Very few people in China care about a Communist future. Nationalism is still a force because of the Sino-US, Sino-Japanese and Sino-European disputes in various fields. But it is also a challenge to the current leadership. Along with the market economy system, decentralization has become the common demand from local levels. Mr Jiang Zemin came into power in very special circumstances. He had no choice but to follow the direction pursued by Mr Deng Xiaoping. His reputation as a Chinese leader is not so strong among ordinary Chinese people. Mr Hu Jintao was actually nominated by Mr Deng Xiaoping as the 4th generation of Communist leader.

Although the Chinese Communist leadership is facing a big challenge, most Chinese still believe that no other political force can and should replace its ruling position because it was the Communist Party of China that started the process of reform and opening-up policy and has provided more economic benefits and a better living standard to Chinese people. This also means that the only legitimacy of the CPC is economic welfare. For the Communist Party of China, the only way to keep its ruling position is to keep the Chinese economy developing constantly.

In order to maintain and strengthen the legitimacy of the CPC the Communist leadership of China put forward so-called "Socialism with Chinese Characteristics". The major feature of this slogan is to put economic development instead of the class struggle as the priority of the CPC. The essence of the so-called "Deng Xiaoping Theory" is that everything should be based around the core of economic development. After Mr Deng Xiaoping, both Mr Jiang Zemin and Hu Jintao continue this strategy and go even further. Jiang Zemin put forward the so-called "Three Representations" and Mr Hu Jintao has put forward the so-called "Scientific Development" and "Harmonious Society".

For the Chinese leadership, foreign policy is determined by domestic politics and should serve domestic politics and economics. Because of the legitimacy problem of the Communist Party in China, political stability

is regarded as the most important issue in China. But how to maintain political stability is the question: to strengthen the so-called “People’s Democratic Dictatorship”, or go through economic development and economic welfare? The answer is the latter. Economic development is not only a matter of strengthening China’s national capabilities, but is also a matter of maintaining the ruling position of the Communist Party in China. This is the most important domestic policy in China. The major task for Chinese foreign policy is to pursue a peaceful international environment for China’s economic development¹⁴.

2.2. Bilateralism versus multilateralism

Many countries pursued bilateralism or unilateralism as the main approach in their foreign policy for a long period of time after World War II, with the exception of the Western European countries. The special international circumstance giving rise to this was US foreign policy after World War II, although the United States was the major initiator of the global economic multilateral regimes. It was also US foreign policy that forced many countries to pursue either multilateralism or bilateralism in their regional foreign policy. In Asia, the United States put forward a bilateral approach by the establishment of bilateral military alliances with various individual Asian countries such as Japan, South Korea, Philippines, etc. In contrast, the United States put into practice a multilateral approach in Western Europe within the framework of the Marshall Plan and forced the Western European countries to work together as a group in order to receive Marshall Plan assistance, even though the initial objective of the Plan was not to support European integration.

The Chinese Communist Party emphasized an independent foreign policy even before it came into power in 1949 because it did not want to rely too much upon the Communist Party of the Soviet Union. The People’s Republic of China was forced to carry out a so-called “lean to one side” foreign policy and it became the member of the Socialist Camp led by the Soviet Union because of the Korean War which began in 1950. The Socialist Camp and the Warsaw Pact Organization could be regarded as a multilateral arrangement among the Socialist countries in the 1950s and 1960s. It was also because of the bad experience with the Socialist Camp, where the multilateral approach was regarded by Chinese as a kind of hegemonic system, that China finally broke with the Soviet Union, dropped out of the Socialist Camp and put into practice the so-called independent and self-determinate foreign policy. Both the United States and the Soviet Union were defined in terms of a hegemony, in a very negative way. From the late 1950s to the 1980s, China kept its posture of unilateralism and bilateralism in foreign relations, and strongly supported the non-alignment movement¹⁵.

After 2003, China started to talk about multilateralism and looked upon it as one of the strategic tools to deal with international affairs, especially its neighbourhood policy.

China has the most complicated surrounding environment in the world. Traditionally, the main approach for China in dealing with its neighbours was bilateralism. The major concern was to resolve or put to one side historical and current bilateral problems. After the Cold War, there has been little possibility of China having any direct military confrontation with the neighbours. The security threat for China has never been just bilateral with its neighbours. The political and economic instability within certain neighbouring countries as well as in the Asian region become the new threats to China’s national security¹⁶.

¹⁴ See Song Xinning, “Domestic Politics and its Impact on Chinese Foreign Policy”, in Weixing Chen and Yang Zhong, eds. *Leadership in a Changing China*, New York: Palgrave Macmillan, 2005, and “China’s View of European Integration and Enlargement”, in David Shambaugh, Eberhard Sandschneider and Zhou Hong, eds., *China-Europe Relations: Perceptions, Policies and Prospects*, London: Routledge, 2008.

¹⁵ Zhao Kejin, “Hard Diplomacy and Soft Landing: Creation and Influence of Chinese New Thinking on Diplomacy”, *International Perspectives*, No. 5, 2005.

¹⁶ Meng Xiangqing, ‘More Stability from Surroundings, More Security for China’, *Global Times*, 4 April 2007, p.11.

Bilateralism was the traditional approach for China in dealing with its neighbours. One of the reasons was because China was worried about a multilateral arrangement being the tool of others to constrain China, as the United States and the Soviet Union did in the 1950s and 1960s. Another reason was that most of China's neighbours were allies of either the United States or the Soviet Union during the Cold War era. China had a strong sense of being threatened by neighbours that were influenced by the two hegemonic superpowers¹⁷.

After the cold war, China started to participate in the regional arrangements in the Asian Pacific such as Asia-Pacific Economic Cooperation (APEC) in 1991 and the ASEAN Regional Forum (ARF) in 1994. But the main dynamics of Chinese involvement was to use the regional platform to deal with bilateral issues and to counteract the influence of Western sanctions after the 1989 event. A good example was the importance of the bilateral meetings with the major counterparts in the region, especially the United States and Japan, during the annual APEC informal Summit. These meetings were more important for China than any regional agenda within the APEC framework¹⁸.

China started its new "Good Neighbourhood Policy" from the early 1990s. The main content of the policy was "to act appropriately towards neighbours and to be a partner with neighbours". Since the second half of the 1990s, Asian regional cooperation has developed smoothly on the one hand, and the sensation of the "China Threat" on the part of China's neighbours increased on the other hand. China's economic and military capabilities were regarded as the major reasons for the China Threat. China's traditional way of dealing with neighbours faced great challenges because it is more difficult for it to deal with all its neighbours separately. It is easy for China "to act appropriately towards" its neighbours. But it is very difficult for China "to be a partner with" all its neighbours separately. The best way is to have a partnership with all its neighbours through certain regional-multilateral mechanisms.

In October 2003 Mr Wen Jiabao, the Chinese Premier, put forward a new conception of China's neighbourhood policy, i.e. "to build an amicable, tranquil and prosperous neighbourhood in the region" According to Mr Wen, to build an amicable neighbourhood means benevolence, good neighbourliness and harmony; to build a tranquil neighbourhood is to actively maintain peace and stability in the region; to build a prosperous neighbourhood is to step up mutually beneficial cooperation with the neighbouring countries, deepen regional and sub-regional cooperation, and vigorously facilitate economic integration in the region, thus achieving common development with other Asian countries¹⁹.

The new strategy is to move away from the traditional "bilateral plus regional" approach, i.e. using a regional platform just to deal with bilateral relations, to a new "regional-multilateral plus bilateral" approach, i.e. to engage in more regional cooperation and work with neighbouring countries together within the regional-multilateral arrangement in order to resolve bilateral problems. Bilateral issues, especially border issues with different neighbours, can be easily resolved or put on ice at the same time.

China's regional-multilateral approach to deal with regional issues and neighbouring countries can be regarded as part of China's neighbourhood policy, as well as its global strategy. In terms of China's neighbourhood policy, bilateralism is not enough to safeguard China's national security and economic

¹⁷ Liu Changming and Pang Chunen, "From Bilateralism to Multilateralism: New Model for China-East Asia Relations", *Journal of Shandong University*, No. 5, 2007, p.112.

¹⁸ Song Xinning, 'China's View on Asian Regionalism', in Wolfgang Pape, *Models of Integration in Asia and Europe*, Luxembourg: Office of Official Publication of the European Union, 2000)

¹⁹ "China's Development and Asia's Rejuvenation", Speech at ASEAN Business & Investment Summit by Mr Wen Jiabao, Premier of the State Council of the People's Republic of China, 7 October 2003. From: <http://www.fmprc.gov.cn/eng/topics/zgcydyhz/dqc/t27711.htm>

interests. In terms of global strategy, China would like to play a more important role in global affairs with the condition of a stable and secure regional environment.

But China's regional-multilateral approach or efforts to engage in regional cooperation is not to pursue an EU-style regional integration. Many scholars have argued that there has been no real regional integration in Asia because 'integration' has a very special meaning and is strongly related to institutionalization and legalization²⁰. The dynamics of China's regional approach include two challenges. The first is to resolve the bilateral problems with the neighbours. As mentioned it is very difficult for China to be partner with its neighbours separately. The main objective is to keep a good relationship with all the neighbours through different regional arrangement such as ASEAN plus one, the Shanghai Cooperation Organization, East Asia Summit, and Northeast Asia-3 Summit. The second is that, in order to play a more active role in global affairs, China needs a stable, prosperous and secure regional environment.

China's multilateralist strategy is mainly for regional affairs rather than global affairs. Globally, the Chinese focus on multilateralism relates to the United Nations and global economic institutions such as the WTO and IMF. With regard to the responsible power argument (see part one of this paper), China pays more attention to the bilateral relationship with the major powers in the world, rather than global multilateral regimes, because the IMF and World Bank are still regarded as Western-dominated regimes by many Chinese. Even in the United Nations, for China, the relationship with the other four permanent members of the Security Council is always the priority.

Four more principles of Chinese diplomacy established after 2002, i.e. "great power as the key, periphery as the core, developing world as the foundation, multilateralism as the stage" (大国是关键, 周边是首要, 发展中国家是基础, 多边是舞台) show that China still pays more attention to the bilateral relationship with the major powers. Some people have also argued that the Chinese multilateralist strategy is actually a selective multilateralism²¹.

2.3. Regional versus global

Most Chinese still regard China as a regional power rather than a global power, or regional power with the characteristics of the global power. There are several reasons for this. Firstly, China's economic development level is still very low and GDP per capita is at a very low level in international terms, although total GDP has reached number two in the world. Secondly, China's economy is very much dependent upon the global market, especially the Western economies. Thirdly, and most importantly, China's national interests, especially its national security interest, is more regional than global.

When China negotiates with other major powers such as the United States, the EU, Russia and Japan it always talks about mutual respect for each other's vital interests. The vital interests of China are related to sovereignty, territorial integrity and national security, with real issues such as Taiwan, Tibet, Xinjiang, and the North Korean nuclear programme. All of these are regional. Although the Middle East and Africa are becoming increasingly important for China, they have not been priority issues for China, and will not become so in the near future.

²⁰ Xinning Song, "Political Economy Approach to European Studies", *International Perspectives*, no.4, 2005.

²¹ Song Xinning, "China and Regional Integration: From Bilateralism to Regional-Multilateralism", in *The IUP Journal of International Relations*, Vol. IV, 1 & 2, 2010, and "Bilateralism and Multilateralism in Chinese Foreign Policy", in José Luis de Sales Marques, Reimund Seidelmann and Andreas Vasilache (eds.), *States, Regions, and the Global System: Northern Asia Pacific and Today's Globalisation*, Baden-Baden: Nomos Publishing House, 2010.

Economically, the major economic partners of China are three, the United States, the EU and East Asia. The EU (EU-25 and now EU-27) has been the number one trade partner of China since 2004 and has always been the most important provider of technology. The United States ranks as number two. But actually, China has more trade with East Asia (Northeast Asia and Southeast Asia) than the EU and the US together. In 2008, China's trade with Asia was 1365.95 billion US\$ (53.32% of China's total trade), including 1016.90 billion US\$ with East Asia (39.70% of China's total) and trade with the EU-27 was 425.57 billion US\$ (16.61% of China's total) and 333.74 billion US\$ with the United States (13.03% of China's total). In 2009 with a very significant decrease of foreign trade, China's trade with Asia was 1172.05 billion US\$ (53.10% of the total) and 879.26 billion US\$ with East Asia (39.84% of the total). China's trade with the EU-27 was 364.04 billion US\$ (16.49% of the total), and with the United States it was 298.26 billion US\$ (13.51% of the total)²². Some people have even argued that if one takes APEC as a whole, it will account for more than 70% of China's total foreign trade.

Table 1. China's Foreign Trade in 2008 (billion of US\$)

	Total trade	%	Export	%	Import	%
China	2561.632	100%	1428.546	100%	1133.086	100%
Asia	1365.952	53.32%	663.295	46.43%	702.657	62.01%
Japan	266.785	10.41%	116.134	8.13%	150.651	13.30%
South Korea	186.113	7.27%	73.951	5.18%	112.162	9.90%
Hong Kong	203.666	7.95%	190.743	13.35%	12.923	1.14%
Taiwan	129.217	5.04%	25.878	1.81%	103.340	9.12%
ASEAN	231.117	9.02%	114.142	7.99%	116.974	10.32%
East Asia	1016.898	39.70%	520.848	36.46%	496.050	43.78%
EU-27	425.577	16.61%	292.878	20.50%	132.699	11.71%
USA	333.738	13.03%	252.297	17.66%	81.440	7.19%
Canada	34.520	1.35%	21.789	1.53%	12.731	1.12%

Table 2. China's Foreign Trade in 2009 (billion of US\$)

	Total trade	%	Export	%	Import	%
China	2207.219	100%	1201.663	100%	1005.555	100%
Asia	1172.049	53.10%	568.597	47.32%	603.452	60.01%
Japan	228.848	10.37%	97.911	8.15%	130.938	13.02%
South Korea	156.232	7.08%	53.68	4.47%	102.552	10.20%
Hong Kong	174.945	7.93%	166.233	13.83%	8.712	0.87%
Taiwan	106.228	4.81%	20.505	1.71%	85.723	8.52%
ASEAN	213.011	9.65%	106.297	8.85%	106.714	10.61%
East Asia	879.264	39.84%	444.626	37.00%	434.639	43.22%
EU-27	364.042	16.49%	236.284	19.66%	127.758	12.71%
USA	298.259	13.51%	220.816	18.38%	77.443	7.70%
Canada	29.701	1.35%	17.675	1.47%	12.026	1.20%

²² Resources from General Administration of Customs of the People's Republic of China, www.ChinaCustomsStat.com. See also Song Xinning, "The EU-China Relations in Transition: Challenges and Opportunities", in Roland Vogt, ed., *Europe and China: The Implications of Changing Global Roles*, Hong Kong: Hong Kong University Press, 2010.

Resources: General Administration of Customs of the People's Republic of China, www.ChinaCustomsStat.com.

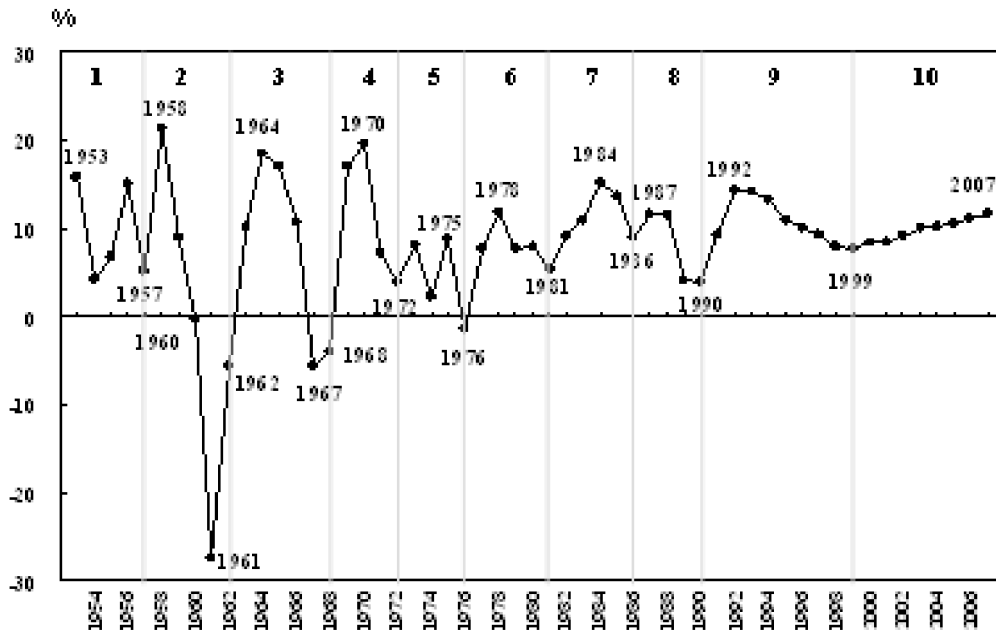
3. China's Economic Development Strategy

Between 1947 and 1948, just before founding of the new Republic, China could only produce 1/87th of America's steel production and 1/8th of Japan's; 1/9th of American's coal production, but the same as Japan's; and 1/35th of America's electricity production and 1/6th of that in Japan. Since 1998, China has already risen to first in steel, coal, cement, cloth, TV sets, motorcycles, tape recorders, washing machines, grain, cotton, meat, seafood, egg production; and power and crude oil production are already ranked 2nd and 4th and also with a production capacity for TV sets, refrigerators and washing machines that accounts for the 1/3rd of the worldwide total today. There seems to be no doubt that the industrial production of China today ranks between 4th and 3rd worldwide.

In 1994, using the PPP approach, estimated by the World Bank, was the first time that China's economic size ranked second in the world, 20% larger than Japan. In 2009 the global economic growth rate was about -2.2%, -2.4% in USA, but 8.7% in China. Although, as the largest developing country, with a large economy and rapid economic development, China has made a strong impression on the world's people even during the international financial crisis. In August 1994, in a survey by the famous Japanese magazine, Ashahi hinbun (Zhaori Xinwen), 44% of the Japanese asked during the survey believed that China would be the most influential country in the Asian-Pacific region in the year 2000, and 30% considered that the USA would be, but only 16% were still sure Japan would be; and because of the crisis this is not far off the mark. The growing economic power gives China the impetus to start to be a real partner with the USA, EU and Japan in the world economy. The economic crisis of 2008-2009 meant that Japan slowed down in terms of development, and China might catch up with Japan next year in GDP. Compared with the USA, Japan and EU, China's miracle of development in the region is not so bright looking forward, not because of the effects of the financial crisis, but due to China's so-called un-sustainable development model – with a clear business cycle (see Figure 1), serious pollution, low efficiency in use of natural resources, a big gap in income distribution, no self-sufficient supply of high tech, serious trade disputes with partners, manipulation of the RMB exchange rate, real estate and stock market bubbles, and so on, as well as a slowing down of the reform of the political system.

How to promote sustainable development, and what should be the main route for China's development in the near future, are the issues people should keep in mind. A group of indicators is given below to make it clear.

Figure 1. Growth rate in China 1953-2007



In the hope that China will be a real partner of the members of the global village in the world economy, China has to meet certain requirements or criteria in order to be one of the leading economies in the World, to give it the power that it needs to be able to take responsibility within the world economy, in case an economic crisis such as that of 2008-2009 has to be dealt with in the future:

- 1) It has to be a top economic power in the world, which means having a large GDP both in absolute terms and per capita (in 2009, the GDP of China reached \$4960 billion, but GDP per capita was \$3800);
- 2) With the largest population in the world, China needs a large proportion of highly qualified people, not only workforce, in the total population, or the cultural-educational level of people in China should be much higher than that of today in order to modernize the country;
- 3) An advanced industrial structure, especially leading advanced sectors in important industries (but without a dual structure in society, i.e. the existence of rich and poor, advancement and backwardness in the economy at the same time), and it has to be developing toward the future: the post – industrialized, or so-called information society;
- 4) A market oriented or market-driven economic structure, and rational allocation of different resources (production resources) with high economic efficiency, involving very significant technical and institutional progress in the economy;
- 5) Sufficient capital inflow and outflow, and currency should be convertible either in the current account and in the capital account of the balance of payments, at least, to be an 8th Clause nation of the IMF;
- 6) A huge market capacity, which means being able to absorb a large amount of domestic and foreign economic output, having the power to push development towards greater demand;

- 7) Effective power of control, especially the power of control over the flows of resources including high-tech equipment, workforce (qualified workforce), capital funds, information and other natural or non-natural resources;
- 8) A reasonable social structure, stable social system and pattern; social life should be institutionalized, and with a highly social civilization.
- 9) High living standards both in cities, towns, and also in rural areas, with safe food, water, and better environment.
- 10) A very significant contribution to, and interest in, world economic affairs, and with a great willingness to participate in worldwide economic and political affairs.

China wishes to meet the requirements mentioned above within the next 30 - 50 years, and become one of the rich countries in the world. In this case China would be friend of all the economies and would lay the foundation for exchange with the rest of the world including both rich and poor. To judge by economic history, I consider it to be certain that China will reach the goal of development by the middle of this century.

Although China is significantly richer than before, with \$3800 per capita in 2009, and has *pursued* the Millennium Development Goals (MDG) of halving poverty, universal primary education, and these Millennium Development Goals have been achieved ahead of schedule, China is still one of the largest developing economies in the World, and has had to fight serious poverty. After nearly 30 years of reform and opening up and rapid economic development, China's impoverished rural population has fallen from 250 million in 1978 to 21.48 million, and the rate of poverty has fallen from the original 30.7 per cent to 2.3 per cent, and the nine-year compulsory education population coverage has reached 98% (see Figures 2 and 3).

Statistics show, in 2007, that the poor population in rural areas decreased by 13.78 million. Per capita net income of 785 Yuan lower than the population living in absolute poverty, decreased from 21.48 million to 14.79 million, a decrease of 6.69 million per capita net income in 786 to 1,067 Yuan low-income poor population decreased to 35.5 million from 28.41 million, a decrease of 709 million. Key national poverty relief and development work in the per capita net income of farmers from 1,928 Yuan to 2,200 Yuan after deducting price factors 11.7 per cent growth over the previous year, higher than the country's average level of 2.2 rural percentage points. This is the "Outline of China's rural poverty alleviation and development (2001-2010)", the fastest since the implementation of the 2001 poverty reduction.

Figure 2. The change in China's rural poor (1978-2005)

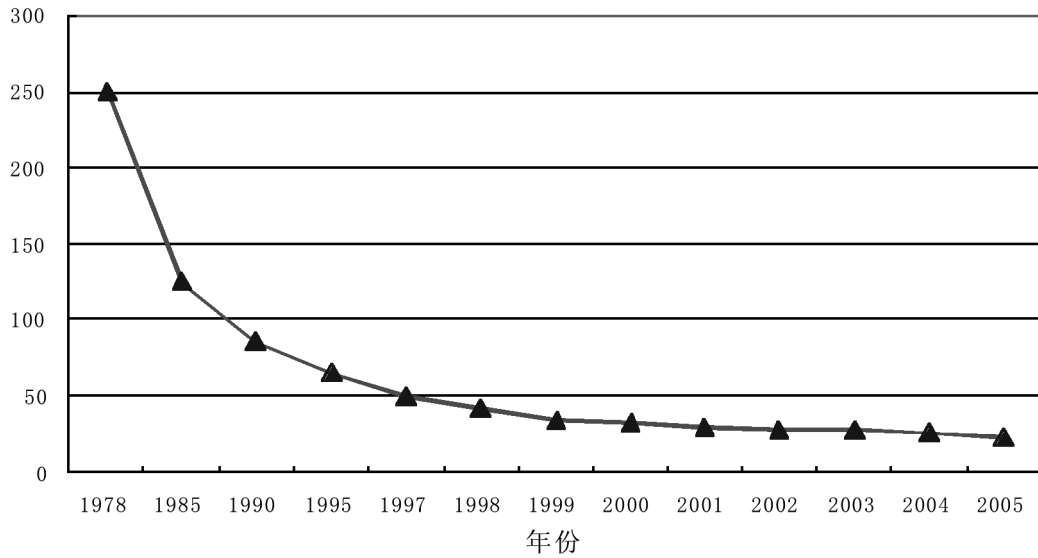
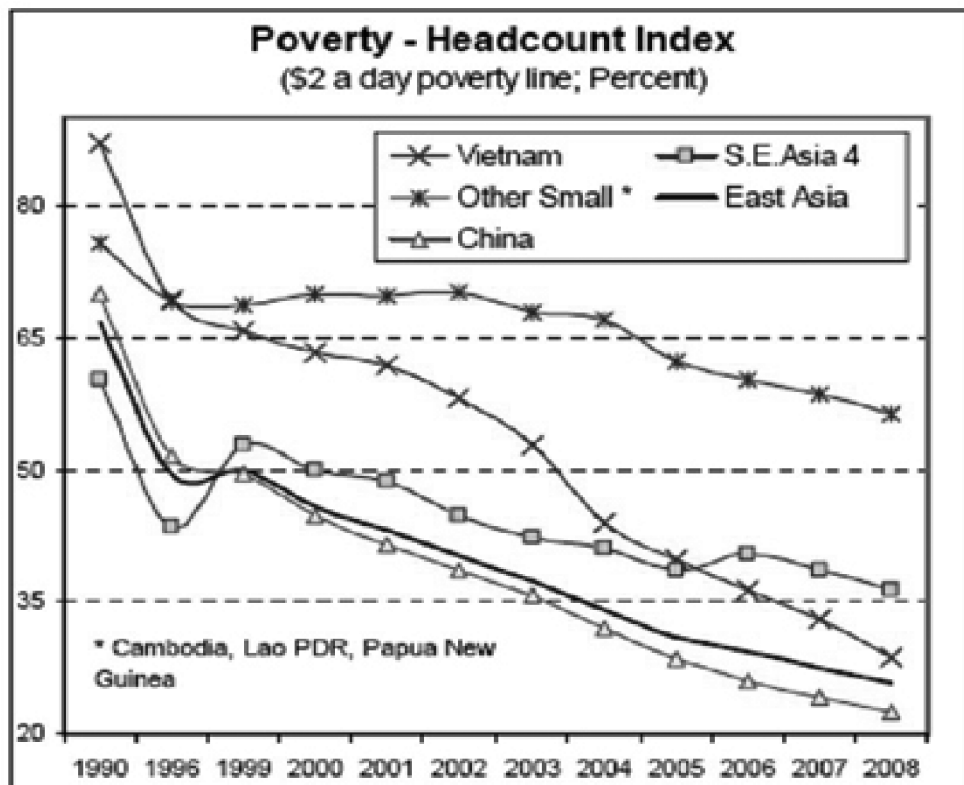


Figure 3. Poverty headcount index

Exhibit 3



To fight poverty in China, China should establish as anti-poverty policy in the near future:

- a) The establishment of a standard development poverty line, the long-term goal of poverty alleviation
- b) The establishment of a rational system of credit and poverty alleviation with financial sector participation

- c) The establishment and improvement of the urban and rural social security system
- d) The promotion of the process of urbanization, and provision of social security and public services to the floating population in cities
- e) The provision of more equal opportunities in education
- f) The expansion of rural labourers' occupational and skills training and labour export
- g) The improvement of the rural medical service
- h) The establishment of a rational public finance poverty alleviation mechanism, to strengthen the management of the government when dealing with poverty

Meanwhile, in the next decade, China's redistribution of income should be reformed; and the most efficient way of increasing the income of the poor is to promote a movement of labour from traditional industries into modern industries. Statistics show about 130 million people from the countryside have sought jobs in the country's urban areas since the late 1980s. Most of them work as construction workers, security guards and waiters, where they encounter low and often delayed pay, long working hours, poor safety conditions, lack of social security, inadequate schooling for their children and substandard living conditions.

4. Sino-US and Sino-EU Economic and Trade Relations

4.1. Historical Review

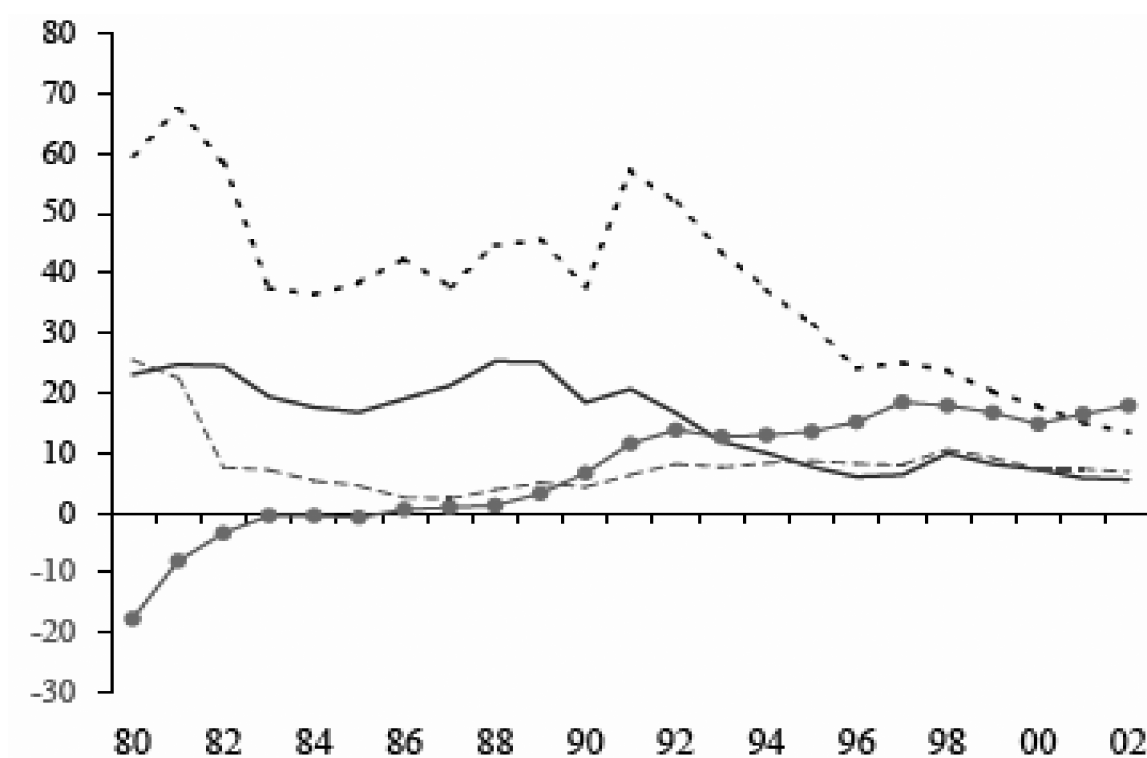
China's external trade in 1978 was ranked 32nd in the world and 11th in 1995, and 10th in 1998, 9th in 2000, and finally 2nd in 2009, which is really great progress in historic terms due to the modernization of its economy. External trade also contributed greatly to the increase of the foreign exchange reserve, which was USD 19.44 billion in 1992, USD 51.62 billion in 1994, and reached USD 144.9 billion in 1998 and USD 2390 billion in 2009. Meanwhile China's degree of dependence upon external trade increased year by year, which shows that China is deeply involved with and integrated into the world economy, and that the development of China is closely associated with global economic changes. Within economic globalization, China's progress has been impressive.

As we all know, every family in the US is able to buy Chinese products that are reasonable in price and good quality, every day. Both US enterprises and all commercial activities have benefited a lot from Chinese trade. The past 20 years have seen a faster growth period than ever for Sino-US trade. According to China's statistics²³, total trade with the US has reached US\$169.6 billion in 2004 at an annual growth rate of 34 percent, with China's exports to the US up 35 percent to US\$124.9 billion, imports from the US up 32 percent to US\$44.7

²³ Ministry of Commerce, http://www.mofcom.gov.cn/article/200501/20050100333447_1.xml.

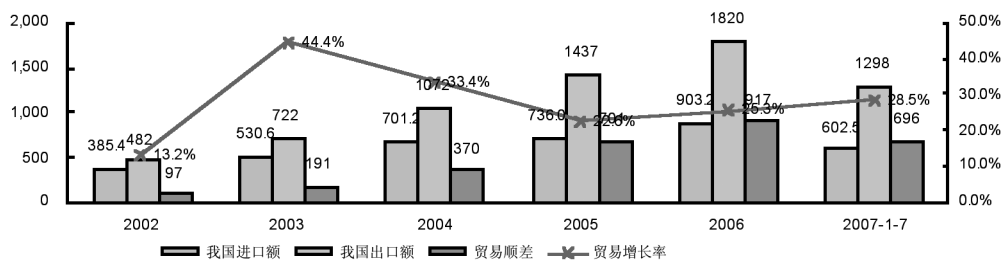
billion, and total trade at US\$ 333.74 billion in 2008. Accordingly, the strong growth has made the US China's second largest trade partner, its second largest export market, the 6th import market in 2008. Meanwhile, US investment in China has also surged in recent years. There are over 58362 US-invested companies operating in China, with US\$ 63 billion capital investment by 2008. Based on the US Census Bureau's statistics²⁴, China was the second largest import and 3rd largest export trade partner of the US In view of the trade relationship between the two countries, there is a serious trade imbalance between China and the US, which, in fact, has soared year after year to a new record. In accordance with China's data, the US trade deficit with China reached US\$170.1 billion in 2008, while it was more than US\$266.3 billion based on US statistics. All in all, China is now the biggest contributor to the US trade deficit, and 73% of total China's trade surplus comes from the US In 2009, the two sides' trade decreased 10.2% to US\$ 360 billion, US exports were US\$ 69.6 billion, a decrease of 0.2%, imports decreased 12.3% to US\$ 296.4 billion, and the trade deficit decreased 15.4% to US\$ 226.8 billion. China is the US's 3rd ranked export partner and first ranked import partner, according to US Department of Commerce. Although there are conflicts in the two countries' bilateral economic and trade activities, somehow trade has continuously developed despite the disputes.

Figure 4. Percentage of Trade Deficit in US Total; red is China's contribution, black is Japan's, blue is the Four Tigers' and green is ASEAN's



²⁴ <http://www.census.gov/foreign-trade/>

Figure 5. EU Trade with China – blue is import, green is trade surplus, orange is export by China, %, and in US\$ 100 million.



The Sino-EU trade relation developed rapidly (see Figure 5). In 2000, Sino-EU trade was US\$ 69 billion, and the trade deficit on the EU side was US\$ 7.3 billion. In 2008, Sino-EU (27 member countries) trade was US\$ 425.6 billion, increased by 19.5%, the EU's exports were US\$ 132.7 billion, increased by 19.6%, the EU's imports from China were US\$ 292.9 billion, increased by 19.6%, compared with the previous year. The trade deficit on the EU side was about US\$ 160 billion. In 2009, the two sides' trade decreased 13.5% to US\$ 412.6 billion, EU exports were 113.1, decreased by 1.5%, imports decreased by 17.3% to US\$ 299.4 billion, and the trade deficit decreased 24.6% to US\$ 186.3 billion. China is the EU's 3rd export partner and first import partner, according to the EU Statistic Bureau.

In fact, trade disputes between China and the US and the EU, apart from the trade surplus, have always been a long-standing issue. They were becoming more and more important before China's WTO accession, and even affected China's accession process. This is shown by the requests made and opinions expressed by the US and EU during the current trade dispute negotiations:

Import Policy

China started to lower import tariffs before its entry into the WTO. In 1996 China lowered its average import tariff from 42.1 percent to 23 percent, and further lowered the average import tariff to 17 percent on 1 October 1997. On 6 January 1999, the Minister of Finance announced that there would be further import tariff cuts for 1,014 products in the textile and toy sectors. So by the end of 1999, the average tariff level was down to 15 percent, which is the same as that in most of the developing countries.

The US and the EU still complained that China restricts imports by a variety of means, including prohibitively high tariffs and domestic tax on imported products, non-tariff-related measures, restrictions on Chinese enterprises' import licenses and other trade barriers. For example: for some motor vehicles, the tariff could be as high as 25 percent. In addition, the tariff might vary for the same product depending on places of entry. Sometimes additional domestic tariffs might be added, or some local restrictive rules might apply. Moreover, imports may also be subject to value-added tax and other duties. The current value-added tax system (VAT), usually at 13 or 17 percent, was also complained about by US and EU trade partners because if a product was subject to a 10 percent import tariff and a further 17 percent VAT, the total consumption tax would be at a rate in excess of 27 percent.

As to China's non-tariff trade barriers, there are also some issues to resolve. For example, although China Customs announced on 1 January 1999 that the number of products requiring export licenses was cut from 707 to 395, there being a 44 percent reduction, the US and EU trade partners still complained that many

products are subject to both quota and import licensing requirements. For such products, after permission has been granted by other administrations for import, MOFCOM still has the right to decide whether a licence should be issued.

Transparency

Although in recent year China's trading system has become significantly more transparent, the US and EU trade partners suggested that they sometimes encountered difficulties in learning which rules and regulations apply to their operations in China.

Trading Rights

Before China's entry to the WTO, there were some 25,000 companies involved with external trade, but the Chinese government still restricted the types and numbers of entities that have a legal right to engage in trading business, forcing US trade counter partners to do business with those with import licences. In the context of China's WTO negotiations, China had pledged to open up the availability of trading rights, such as the rights to import and export. At the end of the transition period, all foreign and domestic enterprises should have trading rights, but the truth is that some restriction persisted, such as on iron ore imports.

Issue of Standards

China retains a statutory inspection requirement for about 780 imported goods and several hundred exported products. The US and EU trade partners complain about the problems of the standards system in China, which include a lack of transparency, difficulty in determining appropriate standards, use of different standards on imports from different countries and domestic goods. For example, US traders are not sure which Chinese standards apply to their goods. Sometimes a particular good of the same type imported from the US and from the EU are inspected in accordance with different standards when they are imported to China. American trade partners also complain that China's sanitary and phytosanitary "import quarantine standards are often overly strict, unevenly applied," and not the same as those used for domestic trade, "and not backed up by modern laboratory techniques."

Government Procurement

China's US and EU trade partners complain that government procurement practices are unclear and there is a lack of transparency. Although China committed to announcing all related laws and regulations, China did not publish any specific rules and regulations on government procurement practices before its accession to the WTO. Moreover, competitive bids for tenders were not allowed for most government procurements in China for the Government investment in the financial crisis during 2008-2009.

Export Subsidies

China's US trade partners complain that although the Chinese government claims that direct financial subsidies on all exports including agricultural goods had ended on 1 January 1991, Chinese exporters could still benefit from loan policies (non-commercial terms loan), export tax rebate (rebate on value-added tax), preferential tax policies (reduced income taxes), and preferential energy and raw material, as well as land

supply policies. The US partner treats all these as discriminatory measures in trade, which today contributes most of the trade disputes between China and US

Lack of Intellectual Property Protection

China's US and EU trade partners complain that the end user piracy of business software is widespread. One can easily find unauthorized copies of pirated software or audio and video products everywhere in China. US industry estimates of IP losses in China due to piracy have exceeded US\$2 billion. Although Chinese authorities have carried out a lot of investigations and has engaged in preventive work, serious problems still remain and the effectiveness of the actions has not been seen, causing a 337 investigation by the US side.

Barriers to Service Industries

To the US and EU, China's service industry market is so closed that the Chinese government only allows foreign services providers to operate under selective licences. This is reflected in restrictions to foreign enterprises' investments and operations in service industries in China. Lack of transparency in administrative procedures limits the exports of foreign companies' services and investments to China. Service trade opportunities, particularly those in financial services, telecommunications, audiovisual, transportation, distribution, professional services, legal services, accounting services, tourism, and so forth, have been affected by a variety of restrictions. Recently in 2010, a dispute arose relating to credit card issuing by the two sides, for example. The US traders think that obstacles such as labour employment, representative office establishment and joint-venture requirements make it very difficult for them to access China's market.

On the other hand, in terms of service provision, complaints showed that the area of information services in China remains a difficult and sensitive area for foreign firms to access. Foreign investors mention that in April 1996, for example, the State Council announced plans to apply severely restrictive regulations governing the activities of foreign information providers. The distribution services sector is another difficult issue, and foreign companies are again restricted in the scope of their activities. Business licences often do not allow firms to provide a full range of services, such as marketing, after-sales services and customer support. Foreign firms do not have access to transportation services on a reasonable and non-discriminatory basis and are required to use state-owned companies to distribute their goods.

Anti-competition Practices

Anti-competitive practices in China come in the form of industrial conglomerates created to improve the profitability of State-Owned Enterprises (SOEs) and to keep unemployment low. Some are even authorized to fix purchase prices and allocate contracts. US traders strongly criticize this.

Electronic Commerce

In fact, at present, sales and contracts executed through electronic commerce are not regulated under Chinese law, but Chinese officials are aware of the potential of e-commerce for promoting exports and increasing the international competitiveness of Chinese firms. China will complete its regulations. All foreign investors are aware that the lack of an effective legal framework poses a challenge to development of the e-commerce business in China.

Investment Barriers

Although China's official policy welcomes foreign investment, US and EU investors consider that the Chinese government has imposed investment barriers and control on foreign investment that could channel them to the areas that support China's economic development. China encourages foreign investment in priority infrastructure sectors such as agriculture and high-tech sectors. On the other hand, it restricts or even prohibits them in sectors where China wants to protect local industries. In addition, China bans investment in certain industries citing "national security interest", and forces foreign firms into joint venture arrangements, or insists on technology transfer from foreign companies.

Other Complains

China's US and EU trade partners complain that the following WTO requests are not fully carried out in order to deal with the issues mentioned:

Uniform Administration – In China there are four different levels of authorities from central government to township, all with laws, regulations, rules, directives, policies, standards, and so forth. All these criteria will affect trade in goods, services, trade-related aspects of intellectual property rights or the control of foreign exchange.

Transparency - All laws, regulations, rules and policies of China's trade should be published and readily available to other WTO members. Such publication is required to disclose in full all the things mentioned above, and China should offer its trade related data and information to other WTO members.

Non-discrimination - Foreign individuals and enterprises and foreign funded enterprises should be no less favoured than other individual and enterprises in respect of goods, service and other trade business either at nationwide or sub-nation level.

Foreign Exchange Control - China accepted Article VIII of the IMF's Articles of Agreement, which means the openness of free foreign exchange in the Current Account of the Balance of Payments, but today the pressure on the Capital Account is growing.

Subsidy - China should stop all export and import subsidies on goods, services and other trade transactions.

Taxes and Charges Levied on Imports and Exports - China should ensure that customs fees or charges applied or administered by national and sub-national authorities should be in conformity with the GATT 1994, and foreign funded enterprises should be on an equal footing.

In addition, for agricultural commodities and product standards, China should follow the regulations set forth by the GATT. Although many kinds of conflicts like those mentioned above remain, and a coexistence policy of encouragement and restrictions has been imposed on bilateral trade by both countries, Sino-US and Sino-EU economic and trade relations disputes have never been and will never be able to slow down the expansion, development and intensification of bilateral economic and trade activities.

5. Exchange of RMB to US Dollar: Manipulated?

The financial crisis in the US and other developed countries was the most significant event in the world economy during the period 2008-2009. This crisis adjusted the pattern and structure of the world economy and made financial issues headline news everywhere in the world, and will have an influence to the end of the first decade and even the beginning of the second decade of the 21st Century. During the crisis, caused by the economic difficulties, the currencies in various countries were seriously devaluated, for example, the Indonesian Rupiah, Thailand Baht and Korean Won, and some of the economies in the world suffered negative growth in 2009. In such a situation, China is almost the only economy in the world to be free from the shock because of its prudential and gradual opening of finance to the rest of the world.

Since China is one of the largest and most important economies in the World, its role in bringing stability to the economic situation in the world during the crisis is also very important. In this case there are many different comments and ideas regarding China's roles in different ways. The most popular two are set out here: first, whether RMB, the China's Currency, should be appreciated or not under pressure from other economies to reevaluate. The answer should be, in the short and middle term (for example by the middle of the year 2010), that there is no reason for the RMB, the Chinese currency, to be revaluated, and in the long run, there is no reason not to retain flexibility for the RMB, the Chinese currency, taking into account development and in the changing world economy. Second, whether or not China should pursue some new and different policies in coping with the difficult domestic economic performance affected by the world financial and economic crisis in 2010. The answer is that the Chinese Government has taken some positive steps in terms of fiscal expenditure policy to increase domestic consumption in order to deal with the effect of a drop in exports, although China's export performance is quite impressive worldwide, and there must be a slowdown in investment increase to avoid over-heating the economy.

Appreciation or depreciation would not hurt China's trade. Some economists consider, if the currency of China, the RMB, appreciated, that the Chinese economy will benefit due to an decrease in the cost of imports and the debt service of China, while exports cannot be promoted for different reasons. On the other hand, some other economists think that with the appreciation of the Chinese currency, China's economy would be hurt, and a new financial crisis would once again hit the world economy and cause a serious economic crisis again. With China insisting on non-appreciation of the currency, some economists of the world approve of the policy pursued by China but also believe that it will adversely affect Chinese economic development, China should pursue some new policies to cope with the problem. The following are the main points:

1. From the analysis of the supply and demand of foreign exchange in the Chinese market, the RMB, the currency of China, has a stable basis.
2. There is some possibility of a return of the financial crisis, and the impact of the crisis on the world economy is continuously developing, with unclear effects and results for China and the world economy.
3. Currently the exchange rate of the RMB is set by pegging it with the US dollar with the dynamic of the market, an artificial intervention which will produce the result of RMB appreciation in short term, but in the long run, the strength of the market would adjust the rate to make it effective.

4. A change of rate (appreciation or depreciation) of the RMB, the Chinese currency, will be following with the general direction of economic development, and reflecting the need of economic development of China first, with only secondary consideration of the effect of depreciation or appreciation on other economies.
5. Whether or not the RMB should be appreciated would be decided by China's political and economic needs; as a developing country, China neither has the need nor is qualified to maintain exchange rate unchanged forever under today's circumstances.

A depreciation of world economies' currencies would put pressure on China's exports, but the pressure would be far less than the shrinkage of import demand caused by the financial crisis. With the low inflation and worldwide growth rate recovering, the conditions of supply lay a very good foundation for China's export growth in 2010. China's recent policy alternatives will help in promoting imports. A negative impact of other economies' devaluation of their currencies upon Chinese exports mainly comes from the shrinkage of demand; and with the recovery of development in the world, China's exports will soar again.

Trade competition is a comprehensive term which is based on different factors and elements; despite the competitiveness of products from other economies being increased by depreciation, it is not so easy to drive out Chinese products from their traditional market, especially from the developed market. The reasons for this are:

- 1) Depreciation of other economies' currencies during the crisis was forced, and as the result of financial crisis, which would be different from a positive depreciation as a policy instrument to promote exports.
- 2) With the enclave feature, some the production chain was a part of the overall system of multinational corporations (MNCs); depreciation would not make MNCs redesign their strategy and shift more production from China.
- 3) Most of the comparative advantage of China is due to economy of scale and low labour costs, which could not be replaced in a short run by other economies.

The financial crisis combined with the changing situation of production have had a greater impact than domestic demand in China in recent years, and the uncertainty of the effects of the crisis has had a negative impact on the strategy of economic growth of China recently. The Chinese government has used both monetary and fiscal policy to cope with the economic difficulty, by increasing domestic demand while maintaining the increase in exports.

With all the measures of fiscal and monetary policies taken by the Chinese government, the budget deficit of China plus all levels of authorities' bonds issued in recent years will increase the percentage of the fiscal deficit of the GDP, but it will still be less than the same level in most of the economies in the world (3% of annual GDP is acceptable, and a total of less than 20% of annual GDP). By using expansionary monetary and fiscal policy (commonly used by other economies also) China hopes to avoid a more seriously negative impact on economic development, and reach the economic growth rate target. Obviously, the result of monetary (including appreciation or depreciation of the RMB, the Chinese currency) and fiscal policy might be revealed after a time lag of several months or years; in the meantime, the Chinese government is paying much attention to the effect of the acceleration of investment and the effect of crowding-out to avoid the negative impact of the bystander effect of fiscal policy. The Chinese also hope that the all the economies in the world will recover

soon, and has made a contribution to the world by maintaining or even revaluating the stable exchange rate of the RMB, the Chinese currency, although this may have adversely affected Chinese economic development in some aspects. When worldwide recovery arrives, China will have no pressure to adjust the exchange rate of the RMB independently of the dynamic of monetary market in China and leave the pegging system behind.

Avoiding a US-China currency war: the need for rational calculation to avoid labelling China as 'a currency manipulator'. Since July 2005, China's RMB has been revalued by 21 per cent. But this has neither significantly improved the US trade deficit, nor reduced China's trade surplus. Merely the prospect of a trade war, or a currency or exchange rate war, between the world's two largest economies would further delay the recovery of the world economy.

Figure 6, RMB Exchange Rate to US Dollar



Does China manipulate the RMB exchange rate? 'Yes' is the answer most widely accepted in the developed economies, but the basis for this is common sense, whereas the legal basis for this argument is unclear. What China adopted was fixed exchange rate policy in 1997-2005, a managed floating system in 2005-2008 and a soft pegging after August 2008. True, the People's Bank of China intervenes in the foreign exchange markets by purchasing US Dollars in order to maintain a stable exchange rate for the RMB. But can this be considered as 'currency manipulation'? A fixed exchange rate was the dominant regime under the Bretton Woods System (BWS), when the US Dollar was pegged to gold and all other currencies were pegged to the US Dollar. After President Nixon de-linked the USD from gold in 1971, the IMF started to encourage more flexible exchange rates from 1973. But the IMF never introduced any rules prohibiting any country adopting a fixed exchange rate. There are three official exchange rate systems accepted by the IMF and its member countries: fixed, floating and in-between - pegging. For example, in Asia, most economies use the pegging, Hong Kong has a currency board arrangement and Singapore has a crawling peg. Neither the US nor the IMF appears to have any problem with these two economies.

A revaluation of the RMB would not help rebalance the global economy. The reality is, as China's Premier Wen Jiabao pointed out, during 2005-2008, the RMB appreciated by 21 % against the US Dollar and by 16 % in real effective terms. But China's current account surpluses rose from 3.5 % of GDP in 2004 to 10.8 % in 2007, before moderating to 9.6 % of GDP in 2008 due to the global recession. In March 2010, China suddenly recorded a

trade deficit of \$7.2 billion, despite the continuation of the RMB's soft peg to US Dollar. It is unlikely that further RMB appreciation, as demanded by some US congress representatives and some famous scholars such as Prof. Paul Krugman, can basically change China's status as 'factory of the world' and substantially boost American exports by doubling volume in 5 years as US President Obama hoped. While the US could experience limited economic gains if any form of sanctions is enacted, the Chinese economy will suffer serious harm also. First, many workers in coastal export processing zones will lose jobs, resulting in a slowdown of economic growth and social unrest; secondly, a surcharge tariff of 20 per cent or more combined with some other tariff and non-tariff methods to attempt trade protection will drive a large proportion of Chinese exports out of the US markets, and will significantly reduce China's external demand; third, as more speculative capital enters China betting on RMB appreciation, the problem of an asset bubble in the Chinese economy will worsen and could spiral out of control.

Goods that are 'Made in China' actually involve a collective division of labour chain across East Asian economies. In the past two decades, East Asian economies including Japan, South Korea, Taiwan, Hong Kong and Singapore have invested and moved their assembly lines into mainland China to take advantage of its cheap labour and land costs; parts and modules come from ASEAN economies and are assembled in mainland China; and exports thereof continue to be targeted at the US and EU market. As a result, these economies have greatly reduced their trade surplus with the US, while increasing the surplus with China, and China is perceived as having the largest trade surplus. A trade and currency war between the US and China would trigger significant knock-on effects for the region as well as the world.

The trade deficit also creates jobs. People can see this from the following case studies. A Dutch intermediary company is processing 95% of its sales of women's shoes in China.

Value list for a pair of woman shoes: 1. Pre-manufacturing in EU (R&D: Euro 0.9, production and quality control: Euro 0.05); 2. Manufacturing process in China (Raw material: Euro 2.18, labour cost: Euro 0.93, Shipment: Euro 0.46, Insurance: Euro 0.04; Other costs -electronic power, water ,etc: Euro 0.44, Profit: Euro 0.37); 3. Post manufacturing in EU (Tariff: Euro 0.35, Logistics: Euro 0.22, Retail: Euro 0.67). Retail price: Euro 19.95 (in EU).

Cost in EU:

$0.9+0.05=\text{Euro } 0.95;$

$2.18+0.93+0.44+0.37+0.46+0.04=\text{Euro } 4.42$

$0.35+0.22+0.67=\text{Euro } 1.24$

Total: Euro 6.61 (Wholesale price: Euro 6.65)

Value in China: $0.93+0.44+0.37=\text{Euro } 1.74$

Value in EU: $19.95-1.74= \text{Euro } 18.21$

(Raw material imported from EU)

That is, Euro 18.21 remains in the EU. The trade deficit is the differential of the prices between China and EU, which could be considered as the GDP of the EU, and each unit of GDP could create certain jobs, which is common sense.

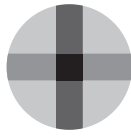
To avoid a trade and currency war, some suggestions have been made, for example, by Prof. Ronald I. McKinnon (William D. Eberle Professor of International Economics at Stanford University) who pointed out: "So here we have the makings of a deal. China agrees to a one-off modest appreciation of the RMB while continuing to reduce its net saving surplus (trade) by increasing consumption. The US agrees to the People's Bank of China stabilising the Yuan-dollar rate indefinitely while working on reducing America's huge net saving (trade) deficit. Both sides agree to stop the (incipient) trade war which has seen them imposing, or threatening to impose, tariffs or other restrictions on the other's goods²⁵".

The suggestion of this author is: if people cannot reach common agreement in relation to the RMB- US Dollar exchange rate, the best way to resolve this issue is to organize a team from the two sides, and allow the experts from the IMF and the World Bank to calculate the real value of the US Dollar and the RMB, the Chinese currency, and work out a central exchange rate accepted by China and the US. The result of this teamwork would be the basis for any future discussion about the economic relation between China and US, given that it is clear that any RMB exchange rate agreement is not just a domestic issue for China. As two of the largest economies in the world, any change to the US Dollar and China's currencies would have an impact on the world economy. If this suggestion could be accepted by the two sides, the RMB exchange issue could finally be resolved and the trade issue would also become less important.

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Resumen: Desde 2003, tanto líderes, como miembros del gobierno chino empezaron a hablar de multilateralismo en lugar de multipolaridad. En un principio el multilateralismo fue visto como una de las más importantes áreas en común entre China y la Unión Europea para construir la asociación estratégica UE-China; después el multilateralismo, especialmente el multilateralismo regional, se convirtió en la nueva elección de la política exterior china en general. El concepto chino de multilateralismo es muy diferente al europeo. Para China, el multilateralismo es un tipo de acuerdo intergubernamental para negociar ámbitos de interés común. Para el régimen chino, cada estado soberano es igual y el principio más importante es el de no intervención en los asuntos internos de cada Estado. Para China, el multilateralismo es un tipo de herramienta diplomática más que un mecanismo de orden internacional. Por ello China es más partidaria del concepto de diplomacia multilateral.

¿Cuál es el significado real de un mundo en armonía? Existen dos palabras clave y cinco elementos principales que son objeto de análisis en este documento.

Dentro de las relaciones económicas y comerciales Sino-UE se incluye un extenso ámbito de cuestiones: la política de importación, transparencia, derechos de comercio, subsidios a la exportación, falta de protección de los derechos de propiedad intelectual, barreras a la industria de servicios...Estas, entre otras cuestiones, son analizadas en este documento. Finalmente se incluye en este artículo el debate sobre si existe una manipulación del valor de cambio del RMB con respecto al dolar.

Palabras clave: Prioridades globales, política económica global, multilateralismo, paz duradera, prosperidad común, relaciones económicas y comerciales Sino-UE.

Abstract: Since 2003, many Chinese leaders and government officials have started to talk about multilateralism rather than multipolarity. At first, multilateralism was regarded as one of the most important areas of common ground between China and the European Union for constructing the EU-China strategic partnership; then multilateralism, especially regional-multilateralism, became the new choice for China's foreign policy in general. The Chinese understanding of multilateralism is very different from the European one. For the Chinese, multilateralism is a kind of inter-governmental arrangement to deal with common issues. For the regime, every sovereign state is equal and the main principal is non-intervention in others' internal affairs. For China, multilateralism is more like a kind of diplomatic tool rather than a mechanism for international order. So the more favoured concept in China is multilateral diplomacy.

What is the real meaning of a harmonious world? There are two key words and five main elements that are analysed in this paper.

Sino-EU economic and trade relations include an extensive number of issues: import policy, transparency, trading rights, export subsidies, lack of intellectual property protection, barriers to service industries...These are covered in this paper. Finally there is a discussion as to whether the RMB to US dollar exchange rate is manipulated.

Keywords: Global priorities, global political economy, multilateralism, lasting peace, common prosperity, Sino-EU economic and trade relations.

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ISBN: 978-84-92989-82-9

