Chapter-VI

CONCLUSION
Economics is where the interests of the United States and China intersect. Trade and business ties have moved from the margins to center stage in Sino-American relations over the past 25 years. But in the history of relations between the world's most developed country and the world's largest developing country, the one constant has been that political considerations have limited and shaped actions in the economic realm\(^1\). That is almost as true in the beginning of 21\(^{st}\) century it was when President Nixon made his historic visit to Beijing in 1972. However, this period has also witnessed the willingness and effort from both the sides to improve the bilateral trade and investment relations.

In the immediate aftermath of the 1979 normalisation, trade and business loomed small in the nascent Sino-American relationship. On both sides, strategic concerns dominated calculations. Over the longer run, President Nixon and his immediate successors nurtured the China tie as an integral part of a global strategy to counter the Soviet Union and its allies. This long-term strategy went along nicely with Chinese leader Mao Zedong's motivation to use the PRC opening to the United States as a counterweight to the Soviet military threat to China's north.

Though economic ties were viewed as a useful supplement to the strategic initiative, enormous hurdles blocked the realization of significant trade and business relations in the early years. For decades preceding the opening, the United States had led an international effort to isolate China economically, and in the process constructed an impressive array of laws and regulations to bar business

\(^1\) Kenneth Lieberthal *US-China relations have continued to affect commercial ties.htm* US-China Business Council Last Updated: 18-May-98
with Beijing. Similarly, PRC-imposed hurdles were equally large. Mao had sought for more than a decade to minimize China's economic ties abroad in the pursuit of national self-reliance. He feared dependence on any single foreign country for supplies of grain and other important goods and wanted to eliminate domestic knowledge of foreign lifestyles. Under Mao, China refused to assume foreign debt and lacked the legal infrastructure necessary to receive foreign investment.

The second chapter of the thesis analyses the trade and economic relations between the United States and China since the time the PRC came into existence in 1949 till 1978. The bilateral trade and investment was quite negligible given the fact that the political factors played heavily against such an engagement.

It is only in the early years after 1972 saw only limited Sino-US business ties develop even if the leaders of both sides had prioritized commercial relations. Trade levels in the 1970s remained very modest, with the balance tilted in favor of the United States (see Figure 2.1). Because of the overwhelming focus on the strategic importance of the relationship, this attenuated economic development caused little consternation.

The psychology of economic relations began changing rapidly, however, as Deng Xiaoping rose to prominence and began in earnest to formulate a reform agenda in 1978. Deng stressed the importance of "opening to the outside world," and the U.S. business leaders proved keenly attentive to this new message. The third chapter has described the continuing Chinese economic reforms and its ramifications for the United States trade and business interests.
In 1979, China began to lay the legal and policy groundwork for foreign trade and investment, and many American executives traveled to the PRC, with visions of a huge market in their mind's eye. The Carter Administration also worked to clear away the legal underbrush on the US side, winning Most Favored Nation (MFN) trade status for the PRC for the first time in 1980.

Despite such positive trends and high hopes the bilateral trade and investment grew slowly. Also, the strategic rationale behind the bilateral relationship remained fundamental for both Beijing and Washington. By the late 1980s, the cumulative effects of improved economic ties, substantial domestic reforms in the PRC, and an easing of Cold War tensions increased the momentum of US-China trade and investment activities.

In 1989, however, the bilateral political relationship, always an important factor in shaping economic ties, sustained serious damage. The events in Tiananmen Square in June severely frayed economic ties; the combination of moral revulsion in the United States and the resurgence of orthodox forces in the PRC quickly dealt a body blow to US trade with and investment in China. Further, the collapse of the Communist block during the last six months of 1989 virtually erased the strategic rationale for strong US-China political ties.

The changed political environment produced US sanctions against China, encouraged human rights and other activists to work with Congress to place MFN renewal in jeopardy each year, and made many US firms reticent when it came to defending strong economic ties with China in a hostile public arena. In addition, China's inflation-fighting policies threw the PRC domestic economy into recession, reducing both demand for American products and the ability to absorb US investment.
In sum, despite substantial hype at various points along the way, Sino-American trade and business ties remained modest for two decades after President Nixon's pathbreaking trip to Beijing. Strategic and political factors contoured the economic relationship, and the difficulties inherent in China's protracted effort to evolve toward a market economy limited successful business. During the 1980s, ethnic-Chinese entrepreneurs from Hong Kong and Southeast Asia, who tend to be more comfortable operating in an opaque market where personal ties and special favors count a great deal, proved far more adept than US firms at forging business ties with China. On the positive side, even taking the Tiananmen sanctions into account, the two governments made significant progress during these years in establishing the legal and policy frameworks necessary to develop substantial future business relations.

Deng Xiaoping's trip to southern China in early 1992 altered the dynamics of the relationship. The trip, during which Deng memorably urged the country to emulate the commercial success of the Shenzhen Special Economic Zone, jump-started rapid domestic growth and renewed efforts to reform the economic system. The 14th Party Congress in 1993 adopted a series of important measures to shift decisively toward a market economy. Suddenly, China's Gross Domestic Product (GDP) began to expand at annual rates of more than 13 percent, and the country started to attract levels of foreign direct investment (FDI) second only to those of the United States. American businesses took note and stepped up their China activities. Somewhat more slowly, the Clinton Administration, for which US economic growth based on development of the global economy was an article of faith, joined in the effort. The Administration became increasingly supportive of expanded bilateral business ties since mid-1994, though it has only recently begun
to secure a solid political footing for its policy of comprehensive engagement with China.

US-China trade and investment relations have expanded rapidly since 1993, achieving a size and maturity previously unmatched. Bilateral trade mushroomed to $81.8 billion in 1999, albeit with a US trade deficit that has reached politically sensitive dimensions. US direct investment in China has grown apace during 1994-99, totaling over $20 billion in utilized investment. China has also begun to play a direct role in the US economy. The PRC government now is second only to Japan in holdings of American government debt instruments. And many Chinese firms have invested directly in American operations.

An assessment of Sino-American trade and business ties over the two and half decades thus must conclude that a strong foundation has been laid. Both trade and investment have reached substantial levels, and business relationships have matured. The fourth chapter looks into this interesting aspect of Sino-U.S. bilateral diplomacy where the trade and economic interests have come to shape their overall relationship. There has been a continuous diplomatic effort by both the countries to maintain this increasing sphere of trade and economic relationship. American products in China hold significant market share in sectors ranging from primary foods and consumer goods to information technology and aircraft. And American firms are among the leading foreign players gaining access to China's gradually opening service sector. A substantial share of the products made in China by foreign-invested enterprises are competitive in a broad array of sectors in the United States. In 1999, roughly one-fifth of Chinese exports went to the American market, and nearly 40 percent of PRC exports were produced by foreign-invested enterprises.
Many trends in the Chinese economy provide grounds for optimism about future growth in US business activities in the PRC. Current efforts to restructure the State-owned enterprise (SOE) sector and to put the banking system on a sound footing promises an immediate need for US consulting and investment banking services and, eventually, a more market-driven economy that should foster the type of competition in which US firms thrive. Long-term changes in China have tended toward greater openness, transparency, and predictability, all of which are favorable developments from a US perspective. And China's GDP is reaching a level at which significant consumer dollars are available for the purchase of foreign products.

These strong, positive trends do not exist in a vacuum, however, and significant issues that have clouded the trade and investment relations are not hard to identify. The fact that each of these issues discussed in the fifth chapter has a political as well as an economic component highlights the important underlying reality that, even after two decades of the normalisation of their relationship, political issues still heavily shape the Sino-American business relationship. The most prominent issues are the following:

The US-China trade deficit: The US-China trade deficit ballooned to $68.7 billion in 1999. Though few economists are alarmed about this development--economists generally are reluctant to analyze trade in bilateral terms--politicians are deeply concerned. Devaluations in most of East Asia since the summer of 1997 have tilted trade balances throughout the region against the United States, potentially rubbing raw protectionist sentiment among the members of The U.S. Congress. In such circumstances, China yielded to the pressure to devalue the renminbi (RMB) to maintain export competitiveness. Beijing,
however, has taken care to maintain the value of the RMB, a stance applauded by the US government.

But the bilateral deficit issue is likely to prove difficult to resolve. China is reluctant to use its hard currency reserves to increase imports for fear it may need to call on these reserves for other reasons, such as helping to support the Hong Kong dollar or straightening out its own banking system. Further, China will need to maintain its export levels, since the PRC is already suffering from excess capacity and high inventories in the production of such items as bicycles, cars, televisions, and washing machines. In addition, China's exports to the United States currently far exceed its imports from the United States. Even if PRC imports were to grow in percentage terms more rapidly than exports, the US trade deficit with China likely would continue to expand.

**World Trade Organization (WTO) accession:** China's accession to the WTO has been important in several respects. While China and the United States both wanted to reach an agreement on the terms of China's entry, China will not gain membership over US objections. The two sides continued to disagree on the phase-in period for China's entry. The United States, viewing China as a highly successful export economy, called for full WTO compliance shortly after PRC accession. China, fearing overwhelming foreign competition in its home market, argued for a longer phase-in period. However, it took political courage on both sides to hammer out a workable compromise. They reached to an agreement on November 15, 1999.

This accession agreement stands to generate enormous benefits for the bilateral relationship. It will provide a quantum leap in the predictability of future Chinese economic reforms, which, in turn, would considerably improve the PRC
business climate. It was believed that an accession agreement almost certainly will take the MFN renewal issue off the table, stabilizing the relationship.

Yet the financial meltdown throughout much of East Asia, which started in the last half of 1997, had made an accession agreement between the United States and China more difficult to reach. WTO opponents in Beijing argued that much of the difficulty around Asia stemmed from the types of market opening that they oppose, including financial sector liberalization. Alternatively, reformers in China tried to use WTO membership conditions as political cover to make the changes that they felt were necessary for China to become globally competitive over the long term. They found it convenient to be able to blame the WTO for requiring such changes.

**Compliance to International agreements:** China's inconsistent implementation of international agreements also could remain a problem in US-China relations. China's failure to live up to international agreements inevitably stiffens the backs of US leaders who decided terms for China's WTO membership and whether to accept China's promises, such as those to restrict exports of nuclear technology. A poor PRC record in implementing international agreements in the future may risk the imposition of debilitating new US sanctions, which of course would increase political friction.

**China's domestic economic performance:** As China's economy matures, US producers can expect sharper competition from PRC firms for market share in China. The characteristics of the PRC market will challenge the formulas for success developed by US companies in China to date. Although China's middle class is growing rapidly, it does not resemble the middle classes of the advanced industrial democracies. US firms will have to tailor their products to be both
attractive and affordable for consumers whose incomes are low by American standards. The smartest US firms will use what they have learned in China to increase their competitiveness worldwide. Eventually, these companies will find Chinese firms—not just foreign-invested enterprises in China—competing in the US market.

China's domestic economic performance may have other spin-off effects that challenge US-China business ties. Restructuring the State-owned sector and related financial reforms should provide opportunities in both the short and long terms for US firms. But these initiatives also create considerable short-term risks of economic dislocation, high unemployment, slowed growth, and increased corruption. The economic earthquake in much of Asia has also made these initiatives more difficult to pursue. The Asian financial crisis has decreased the foreign investment capital available for restructuring SOEs and has increased export competition for the output of China's township and village enterprises and private sector, which in turn has decreased profit margins and job growth. In general, slower growth in China would reduce demand for American products and services.

Politicising economic issues affects the bilateral trade relationship: American politics could jeopardize the bilateral economic relationship. Ever since the 1989 Tiananmen incident, diverse American advocacy groups—for human rights, non-proliferation, the right to life, and fair trade, among other causes—have sought to link their agendas to alleged abuses in China, arguing that China is one of the world's greatest offender in each of these areas. Although Chinese behavior in each of these areas is, to some extent, offensive to American values and/or law, the claim that China stands out among global offenders is generally spurious. China has received this unwelcome attention, rather, because the events in
Tiananmen Square created a compellingly horrific set of images of the PRC that provides additional visibility, emotion, and fundraising capacity to any cause that can link its agenda to Chinese conditions.

However, in spite of all these conflicting issues hampering the bilateral relationship, there is more common ground between the two countries in trade and business relationship than in many other areas. Beijing’s leaders are interested for economic growth, because China’s stability and survival depend on it. The United Sates, at the same time, is trying to take advantage of the greatest commercial opportunity of the next century. China’s enormous need for investment and technology to fuel its growth coincides perfectly with America’s desire for exports and new markets to create profits and jobs. Normalizing U.S.-China trade and business relations, therefore ought to be a priority for both countries. It is in their mutual interest to do so.

**Prospects of U.S.-China Commercial Relations**

In U.S. foreign policy, economic interests have always been subordinated to geopolitical objectives. Until Tiananmen, the geopolitical consideration of using China as a counterbalance to former Soviet Union overshadowed human rights and economic concerns. Since Tiananmen, however, human rights concerns have dominated U.S. economic policy toward China, and without the Soviet threat, China has receded in importance in U.S. foreign policy. American attitudes toward China have also had their ups and downs over this period.

It is time for the United States and China to establish a framework for bilateral relations that removes the vicissitudes in their relationship. And, it is time, in this post-Cold war era when economics are increasingly in command in
international relations, for the United States to rethink the subordination of economics to political concerns in its foreign policy. There is no better place to start than normalizing U.S.-China commercial relations, an area where mutual interests outweigh differences.

**Options before the U.S. Government**

There is a growing trend of trade and commercial interests getting reflected in the foreign policy decision making of present day nations. The nations of the world are trying to be well equipped structurally to move accordingly with the changing international dynamics where trade and economics have come to the forefront. Like other nations the United States as well as China have revamped their foreign policy decision-making structure to accommodate and focus on the trade and business interests. Besides the government agencies, the views of other non-government agencies, academicians, public opinion regarding the Sino-U.S. diplomacy in trade and investment have been taken seriously. The recommendations of the U.S.-China Business Council, the Coalition of Business for U.S.-China Trade and the Business Roundtable are helpful. The following areas of U.S. government policy are most important.

Trade expansion is a critical factor in a comprehensive strategy toward China that can enhance America's ability to address a broad range of interests. The policy options before Washington to demonstrate its commitments to these goals, is as follows:

- **Granting of an unconditional extension of permanent normal trade relations to China.** Granting permanent NTR to China would allow America's strongest economic sectors, particularly the agricultural,
automobile, computer, financial services, and telecommunications industries, as well as Internet-related commerce, to compete in China's large market, which would help expand China's small but growing private sector. Greater private-sector employment will offer the Chinese people the wealth and freedom they need to choose private alternatives to government subsidies in education, health care, housing, and other basic needs that come with increased restrictions and regulation. The US congress after much deliberation has passed the permanent normal trade relations (PNTR) bill on May 24, 2000.

- **Seeking of the simultaneous entry of Taiwan and China into the WTO.**
WTO membership for China and Taiwan would increase U.S. access to their markets. By emphasizing the positive-sum benefits of trade liberalization as opposed to the zero-sum sovereignty disputes, the WTO also will provide an international forum through which cross-Strait economic relations can be enhanced and normalized.

**Human Rights:**

U.S. business recognizes that the human right is a core American value and an essential element of American global diplomacy. Moreover, the principle is a universal one and, therefore is conducive to multilateral action. Persuasion rather than sanctions, private negotiations rather than the public sermonizing are more likely to achieve the objective of improving human rights for the Chinese people. The U.S. government, therefore, should discontinue its policy of linking non-economic issues, such as human rights, to economic initiatives. It should return to the principle of pursuing trade and investment agreement to liberalise and further economic growth, while promoting human rights through independent cooperative efforts. The North American Agreement on Labour Cooperation and the North
American Agreement on Environmental Cooperation may serve as models for a similar cooperative effort on human rights with China.

Besides, the United States should explore new ways to monitor and address human rights concerns in China. The White House and Congress should review the lessons learned from the Helsinki Commission and consider their applicability to the challenge of human rights in China. The establishment of an executive-legislative commission, as proposed by Representative Sander Levin and Senator Spencer Abraham, merits Congress's thoughtful debate.

U.S. Trade restrictions and regulations:

In some significant instances, because foreign competitors are not encumbered by the same rules and regulations, restrictions imposed by the U.S. government seriously disadvantage U.S. companies' ability to compete in China. Although some restrictions may continue to be justified on national security or foreign policy grounds, many of them are left over from the cold war and are no longer needed. The regulations that most concern the U.S. companies operating in China concern export controls, embargoes, sanctions and restrictions on financing by the Overseas Private Investment Corporation (OPIC), the Export-Import Bank and the Trade and Development Agency (TDA). The U.S. government should:

(1) Reassess and rationalize the U.S. export control system. In general, unilateral export controls should be eliminated, the speed of licensing decisions should be increased, and predictability and accountability improved.

(2) Extend eligibility for OPIC insurance and Export-Import Bank and TDA financing to all countries in the Asia Pacific region, including China. The only effect of the six-year U.S. OPIC and TDA sanctions has been to restrict efforts by the U.S. companies to establish a presence in China, handicapping U.S. exports. Expanding Export-Import Bank export
financing and guarantees is essential for American companies to participate in major infrastructure projects in China and would boost U.S. companies’ competitiveness.

(3) Eliminate or rationalize country specific policies. As part of step-by-step normalization, Congress should revise trade law provisions that single out China for less favourable treatment, particularly in the areas of export controls, peaceful nuclear power plant construction, aerospace, and special import safeguards.

**Options before China:**

To maintain the growing bilateral trade and business relations is a two-way street. Policy priorities for China in part mirror those of the United States. The following points need urgent attention.

**Membership in the World Trade Organisation (WTO):** China, has every right to take its place among the trading partners of the world. Accession to the WTO, however, is a commitment to be bound by a set of rules. China needs to agree to a commercially acceptable protocol. Commitments should include eliminating the restrictions on foreign trade and investment contained in China’s industrial policies, extending full trading rights to foreign companies, and eliminating protectionist tariff and non-tariff barriers to trade.

**Market Access:** China needs to implement all phases of the 1992 bilateral agreement and phase out quotas, import licensing restrictions, and other administrative barriers that act as effective market barriers. Currently China, like many other Asian countries, maintains significant barriers to entry by foreign financial services providers and telecommunication companies. Given China’s
need for increasingly sophisticated financial services and telecommunications infrastructure, it is in the interest, when it joins the WTO, to work within the APEC framework and the General Agreement on Trade in Services (GATS) to remove market access barriers.

**Intellectual Property Rights:** Although the US and China have entered into agreements regarding IPR standards (1992) and enforcement (1995 and 1996), piracy of U.S. software, videos, and sound recordings remains a serious problem. China's credibility is on the line when it does not adhere to agreements that it signs. It must follow through on its IPR commitments, crack down on piracy, and vigorously enforce IPR regulations.

**Transparency:** Foreign corporations doing business in China overwhelmingly suggest the need for transparency, or openness, in Chinese regulations and laws. Lack of transparency involves the non-publication and non-availability of laws, regulations, and related measures and procedures, as well as the use of informal administrative “guidance” or “approval” as a form of rule making. Lack of transparency harms both foreign and domestic businesses by increasing uncertainty, complicating business planning, and facilitating corruption. Establishing greater transparency in regulations and laws not only would strengthen investor confidence but, would help China succeed in its anticorruption campaign.

China-US business relations have traversed a rocky path for a quarter century but have managed to grow substantially. Politics continually has influenced the economic relationship, and stable bilateral ties are just beginning to take root in the post-Cold War era. In this context, it is tempting, but dangerous, to make economic ties the central rationale for the relationship. Economic links,
while important, are vulnerable to attack from many angles, from efficacy in producing desired changes in China to morality.

Perhaps the most important accomplishment over the past two decades is that the overall China-US relationship is now both broad and deep enough to weather trying times in any single area. Today the depth and breadth of interaction between American and Chinese societies are quite extraordinary, whether it be among scholars, business executives, factory workers and managers, tourists, government officials, adoptive families, journalists, entertainers, or just friends. But healthy US-China business ties will require ongoing attention to the political as well as the economic challenges for a long time to come. American and Chinese leaders must demonstrate willingness and combined effort to bring a stable and productive Sino-American relations.

In the long run, facilitating people-to-people interaction through increased trade will benefit both America and China. It will help integrate China into the world's economic system and create the conditions that empower the people of China to seek additional freedom and democracy. A stable democracy and free market in China is vital to the peace and stability of the Asia-Pacific region, as well as to the whole world.