

What Commercial Policies Can Promote China's Sustainable Trade Strategy?

Li Jian
Academy of International Trade
and Economic Cooperation, China

Simon J. Evenett
University of St. Gallen and
International Trade and Regional
Economics Programme, Centre for
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International Institute for Sustainable Development
161 Portage Avenue East, 6th Floor
Winnipeg, Manitoba
Canada R3B 0Y4
Tel: +1 (204) 958-7700
Fax: +1 (204) 958-7710
Email: info@iisd.ca
Website: www.iisd.org

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List of acronyms

ASEAN	Association of Southeast Asian Nations
FTA	free trade agreement
G20	20-Nation Coordination Group
LDCs	least developed countries
WTO	World Trade Organization

1.0 Introduction

The purpose of this paper is to consider the implications for China's commercial policies of a decision to adopt a sustainable trade strategy, the motivation for which was described in Long (2010), the overview paper for the Sustainable China Trade Project. The assumptions underlying that strategy and its design, appear to take account of developments within the world economy, the reaction of trading partners, and the existing web of international trade agreements and related institutions. The implementation of such a strategy must do the same, and here we give due attention to the relevant developments. Overall, in this paper we seek to identify possible trade policy options that China may wish to consider as it pursues a sustainable trade strategy.

For the purposes of this project the following five objectives compose China's so-called sustainable trade strategy:

1. Promote the rebalancing of the Chinese economy away from its currently unsustainable path.
2. Promote added value in economic activities, not just sales.
3. Promote services, not just manufacturing.
4. Promote Chinese firms (including multinationals), brands and intellectual property rights. (Nationality matters.)
5. Support a harmonious, sustainable architecture for international trade.

These objectives represent an adaptation of the traditional notion of sustainable development to the current circumstances facing China, reflecting not just environmental notions of sustainability but also social and economic aspects. Not every reader may be comfortable with each of these five objectives, but we take them as parameters for the purposes of this paper. Moreover, the current global economic downturn, which has adversely affected Chinese exports, may influence the speed with which the country implements measures that seek to attain these five objectives.

The desire to shift away from low-value-added manufacturing exports, which are thought to offer limited prospects for long-term improvements in standards of living as seen in terms of wages and environmental quality, combined with the enduring need to create a large number of jobs every year for those entering the labour force and migrating toward urban and coastal areas, appears to have been an important motivation for the shift in Chinese thinking toward commercial policy-making. So has the recognition that existing export growth rates are provoking greater opposition to trade in China's trading partners. In this respect, the adoption of a sustainable trade strategy can be seen as an attempt to reorient China's domestic and international commercial trajectory.

Since this paper is part of a larger project and the contributions will be published together, we will not repeat material here that others have comprehensively covered. We have also mentioned Long's overview of a sustainable trade strategy for China (Long, 2010). That paper also provides an informative summary of the evolution of recent Chinese trade growth and its integration more generally into the world economy.

Likewise, Cosbey, Song and Savage's (2010) paper for this project describes the numerous connections among international trade and the environmental, social and economic aspects of the traditional concept of sustainable development. Cosbey et al. also draw on a wealth of China-related evidence in support of their argument that these connections are of importance to policy-making.

The focus, then, of this paper is specifically on the various commercial policy options that could advance the objectives of a Chinese sustainable trade strategy. The choice of the phrase "policy options" rather than "trade agreement" was deliberate, because the latter is only a subset of the former. Even so, much of the emphasis here is on what China can accomplish through traditional trade policy instruments and venues, such as the World Trade Organization. Moreover, as the scope of trade agreements, in particular regional or bilateral trade agreements, has grown over time, in some cases to include non-commercial matters, arguably the strict distinction between trade agreements and other international accords has diminished.

Throughout, this paper is informed by practice, not just principle or theory. The recent global economic downturn plus long-standing difficulties in concluding the Doha Round of multilateral trade negotiations must surely inform policy-makers' choices. The looming threat of a return to the protectionism of the 1930s, to an era of competitive devaluations of currencies, sharp falls in exports and imports, and the like, has no doubt influenced perceptions of national priorities and the appetite for international cooperation on commercial policy and other economic policy matters. In addition, the current crisis has brought to the fore a new forum, the Group of 20, where China has played an active and growing role. These considerations cannot be ignored, at least in terms of shorter-term prioritization of initiatives.

Moreover, countries' growing resort to bilateral and regional trade agreements implies that careful consideration must be given to such options too. As will become clear, there are differences in the speed with which progress is likely to be made in various forums where trade-related accords are negotiated, and this may call for different potential priorities in the near term as well as over the medium to longer term. Yet we recognize that the further into the future the analyst proceeds, the more qualification and circumspection any forward-looking assessment requires.

This paper is divided into six sections. Section 2 will briefly discuss what can be reasonably expected of traditional trade policy instruments, based as they are on reciprocity, non-discrimination and

rules, in contributing to the implementation of a sustainable trade strategy, a program with multiple objectives. Section 3 accounts for the adjustments and evolution of China's foreign trade policies after China's accession to the WTO and analyzes strategies that China has used to develop multilateral, regional and bilateral economic cooperation.

Section 4 discusses several of the major challenges facing China in terms of its sustainable development in foreign trade and coordination of relations with its trading partners. Section 5 studies the policy options for China to use to change its foreign trade development strategy and to strengthen trade cooperation. Section 6 contains a conclusion and summary remarks.

2.0 Commercial policies and the goals of a sustainable trade strategy

The five objectives of China's sustainable trade strategy, as outlined in the introduction to this paper, are broad and far-reaching. The question naturally arises as to what outcomes traditional trade policy instruments can realistically be expected to deliver, should China adopt this strategy. This question is not just of theoretical interest, as policy-makers driven by results need realistic assessments of what each type of tool can deliver.

Getting expectations wrong can do much to discredit an important initiative over the longer term. Arguably the adoption of the noble-sounding "development objectives" in the Doha Round has, because of their lack of specificity as well as doubts that many trade policies can make first-order contributions to macroeconomic aggregates, done much to discredit the WTO in recent years. It is important to resist the temptation to oversell what trade policy tools can deliver. Indeed, some commercial policy instruments may be better at attaining certain objectives than others, and some objectives are best met by state measures other than trade policies.

For the purposes of this discussion, the following instruments of Chinese commercial policy will be considered: reciprocity-based binding trade agreements in their various forms, non-binding (or soft-law) initiatives, state-to-state dialogues, and unilateral measures, which by definition do not require the agreement of a trading partner. Given the penchant of many trade negotiators and officials for reciprocal, binding trade agreements, the following discussion starts by assessing the potential contribution of this form of commercial policy.

The question, then, is in what ways traditional reciprocity-based trade agreements that contain so-called rules on non-discrimination and provisions on market access advance the five objectives of China's sustainable trade strategy. The first reason for asking this question is that some of the five objectives might best be dealt with by policy instruments other than reciprocal trade accords.

For example, if the rebalancing of the Chinese economy requires a shift from dependence on export-related sources of demand toward greater reliance on domestic consumption growth, then measures that reduce the need for Chinese households to save as much of their income as they currently do are likely to be far more effective than any single trade agreement. It is quite unclear how trade policy instruments can contribute in this regard, since savings decisions are driven by precautionary motives as well as expected rates of return, which are variables not typically affected by trade agreements.

Moreover, questions might arise as to whether trade accords have any further role in advancing some of the stated objectives. The desire to promote upgrading of Chinese firms into segments of markets where industrialized country firms currently dominate may be accomplished by lowering tariffs on higher-end products. If, however, these tariffs are already zero or close to zero, negotiated as they were as part of previous market-access exchanges among industrialized countries and then multilateralized through the most-favoured nations requirement, then few trade barriers may need to be removed in future negotiations.

Tariffs on manufacturing items of interest to industrialized countries tend to be lower than those on labour-intensive manufactured goods made in developing countries. The process of upgrading is likely to shift more Chinese exports into tariff lines that already have very favourable tariff treatment, in which case there may be few tariff barriers to negotiate away in the future. Of course, if foreign technical standards and associated qualification procedures remain an important barrier, then something to negotiate may still remain.

The presumption that all reciprocity-based trade agreements must advance these five objectives should be dispelled too, and the current disadvantageous tariff treatment afforded to low-end manufactured goods helps make this point. Should China negotiate a free trade agreement (FTA) or a multilateral trade accord that lowered or even eliminated the tariff peaks on low-end manufactured goods in a number of major export destinations, in effect the incentive to expand low-value-added manufacturing in China would be enhanced, which is directly at odds with the second objective of a sustainable trade strategy. This observation is significant, as the liberalization of manufactured (that is, non-agricultural) products is central to most bilateral, regional and free trade agreements. Moreover, since many industrialized countries are concerned about liberalizing tariffs on low-end manufactured products (to prevent inefficient firms from facing the full force of international competition), should China decide not to pursue the abolition of these tariffs in trade negotiations, it may find it easier to conclude the other, associated accords in the first place.

The service sector presents one area where seeking improvements in market access abroad is consistent with one objective of the sustainable trade strategy. To the extent that access to foreign markets is an important trigger of domestic service sector development, then the priority afforded to seeking market opening abroad for Chinese firms rises. Taking this observation about services together with the previous discussion on goods suggests that Chinese priorities concerning which market access concessions it seeks from trading partners may need to evolve from goods to services.

The last example of upgrading raises a further, distinct point. If the Chinese authorities are determined enough to create strong incentives to upgrade products, they could introduce a system of export taxes that are related to unit values of production¹. Leaving aside any problems that may

¹ One indicator could be average export revenue per unit sold.

well arise with falsification of unit values, a sliding scale of export taxes that is inversely proportional to unit value could substantially reduce the profitability of exporting low-end goods. The broader lesson here is that the Chinese government may well take some unilateral trade policy measures to attain some of the five objectives identified earlier. Arguably, the expansion of China's service sector may be facilitated by certain trade policy measures, but the policies with first-order effect are likely to be domestic ones, such as the removal of any barriers to entry or reviewing restrictions on land use, which tend to hold back retailing.

To the extent that the overseas expansion plans of Chinese firms or their intellectual property are compromised by foreign governmental practices, there may well be additional challenges that new reciprocity-based trade accords can tackle. Rules strengthening the transparency of foreign regulatory practices and obligations to provide national treatment would follow as negotiating priorities.

However, the requirement for reciprocity allows trading partners in the negotiations to make demands for the reform of comparable Chinese regulatory institutions. Of course, the negotiating clout of trading partners may vary considerably, and China could diplomatically rebut the demands of certain trading partners. Still, before putting new matters on the negotiating table, the Chinese authorities ought to consider carefully the extent to which it is prepared to alter its domestic regulatory regimes in response to foreign requests. In sum, reciprocity is a two-way street.

Acute concerns about infringements on domestic sovereignty may limit what China can reasonably accomplish for its internationally active firms through reciprocity-based trade accords. This in turn raises the alternative of supporting soft-law initiatives that seek to advance non-discrimination principles in national regulatory regimes. While these soft-law approaches may have the attraction of being non-binding, should China use them as a tool for advancing its interests abroad then Chinese regulators would be expected to adhere to the same international standards. Foreign criticism of lapses would not be avoided just because an international regulatory initiative is non-binding.

Consideration of what reciprocity-based trade accords can deliver requires examining the basis of any potential deal or agreement. The considerations above suggest that negotiations centred on improving market access in services and the extension of transparency and non-discrimination into regulatory areas are interests that follow from the five objectives of a Chinese sustainable trade strategy. What trading partners want in return for any concessions to their Chinese colleagues, and the sensitivity of those demands, will have to be taken into account as well. If foreign demands, in particular in the areas of agricultural trade liberalization and the opening up of financial services, are seen as too far-reaching, this will limit any realistic assessment of what reciprocity-based accords can contribute to China's sustainable trade strategy. As indicated earlier, the success of the latter strategy is, fortunately, not wholly contingent on traditional reciprocity-based trade agreements.

Trade accords could advance the objectives of China's sustainable trade strategy in two other ways. The first concerns improvements in environmental policy and the enforcement of environmental objectives. Whether included or not as part of a reciprocal FTA or multilateral trade accord, trade agreements can be used to entrench shared goals (such as the progressive improvement in environmental standards) and to commit to enforcement of associated laws and regulations. Precedents exist where nations have taken on commitments to enforce domestic regulatory laws in trade agreements and to appropriately fund enforcement bodies, posing the question of whether those precedents can be adapted to promoting sustainable development. We return to this matter in Section 5.

Because one of the objectives of China's sustainable trade strategy is to promote a harmonious, sustainable architecture for international trade, the question arises as to what stance China might take concerning the evolution of the multilateral trading system. This is not just a matter of completing the Doha Round and any other existing initiatives, though those may well be particularly important, especially as concluding the Doha Round would lock in many of the reforms that have taken place in many countries over the past fifteen years and discourage protectionism during the current global economic downturn. It will also be a matter of managing the disputes that will inevitably arise, as well as establishing future negotiating agendas, be they as part of any future multilateral trade round or, more likely, in the context of alternative plurilateral or "critical mass" accords.² Such accords can be used to address important sector initiatives, such as those relating to the environment. In addition, it may be possible to make more progress on the opening of service sector markets in WTO accords that do not require every WTO member to be a signatory.

A final important strategic consideration concerns the ongoing climate change negotiations and their relationship to the multilateral trading system. The potential for a climate change accord to induce significant restructuring of national economies raises the question of the relationship between any specific climate change proposals and the five objectives of China's sustainable trade strategy. Trade-offs among these objectives, and between these objectives and the goal of slowing climate change, may have to be considered. In short, international initiatives outside of the multilateral trading system may well implicate the manner in which trade policy instruments are used to advance China's sustainable trade strategy.

The purpose of the discussion in this section has been to highlight the manner in which several commercial policy tools available to the Chinese government vary and how that variation might

² A plurilateral accord is an accord between a subset of the WTO members concerning a matter of common interest. The benefits of membership of such an accord need not be shared with other members. A critical mass accord is an accord among a subset of the WTO membership that comes into effect when a pre-specified agreement threshold is met. A characteristic of critical mass accords is that the reforms undertaken as a result of them are shared with all WTO members, irrespective of whether a trading partner is a signatory to the critical mass accord.

influence the choice of which policy tools will best help attain the objectives of China's sustainable trade strategy. Certain deductions (such as promoting service sector market-opening objectives over goods market-negotiating objectives) follow from consideration of these objectives and the present state of the multilateral trading system.

Other deductions point to the fact that there may be limits to what can be achieved through reciprocity-based trade accords, unless China is in a position to deflect any awkward demands from trading partners. (China may be better positioned to do this in certain negotiations than in others.) Furthermore, some objectives may best be pursued by unilateral trade measures and even by state measures not typically associated with trade policy. Indeed, these observations suggest that trade policy should not be expected to contribute to each of the five objectives of China's sustainable trade strategy, or ultimately be judged by such contributions.

It is not a matter of whether a trade policy instrument can influence economic, social or environmental targets associated with any given objective, but whether the trade policy instrument is the best policy instrument available to attain that objective. In this regard, the first objective (rebalancing the Chinese economy) seems to be best accomplished with macroeconomic tools, not trade policy. Trade policy instruments are likely to make some contribution to the second through fourth objectives, but unilateral state measures may contribute more. Finally, trade policy initiatives will be at the centre of discussions for meeting the fifth objective (promoting a harmonious multilateral trading system) and will figure prominently in many discussions on other significant international initiatives, such as negotiations over an accord to slow climate change, that implicate the multilateral trading system and China's overseas commercial interests.

To better root suggestions and recommendations for Chinese policy-makers in the appropriate context, the next two sections consider at some length the objectives and recent experience of Chinese commercial policy-making.

3.0 China's trade strategy and policy since entering the WTO

The purpose of this section is to describe the factors underlying China's current trade strategy and the initiatives that have followed from that strategy. As will become clear, China has tailored its approaches to different matters and trading partners, assembling a wide portfolio of tools. This discussion provides the point of departure for suggestions for reorienting China's commercial policies to the objectives of a sustainable trade strategy, the subject of Section 5 of this paper.

3.1 The adjustment of China's foreign trade policy since entering the WTO

Some of the main factors influencing the formation and implementation of China's foreign trade and economic policy are as follows:

Political factors. The Communist Party of the People's Republic of China has put forward a "people-oriented" policy, which since the 16th National Congress has aimed to comprehensively implement a scientific outlook on development and build a "harmonious society." Compared with the traditional outlook on development, the scientific outlook on development is a step forward and sets new and higher standards for domestic development planning, opening to the outside world, promoting the coordinated development of the national economy and foreign trade, resolving all internal and external conflicts, and ensuring China's peaceful rise. Through this new outlook, China hopes to establish an "internal and external, interactive, mutually beneficial and win-win, safe and efficient open economic system and form new competitive advantages in participation in international cooperation and competition under the conditions of economic globalization" (Hu, 2007).

Economic factors. Since China's accession to the WTO, China's national economy and foreign trade have developed rapidly, and China has become the world's fourth-largest economy and third-largest trading country. At the same time, problems such as domestic and international economic imbalances, relatively weak domestic demand, extensive dependence on foreign trade growth, intensified constraints on foreign trade from resources and the environment, an excessive trade surplus, currency appreciation pressures and conflict with major trading partners have become increasingly prominent. Foreign economic and trade policies should be adjusted to take these issues into account; otherwise, the country's continuous growth in both imports and exports will not be sustained.

WTO rules. As a new member of the WTO, China needs to open up its domestic market in accordance with its commitments and WTO rules, clean up and revise laws and regulations that do not comply with WTO rules, and improve the transparency of policy formulation and

administration. The principles of market access, national treatment and transparency initiated by the WTO have become the consensus. At the same time, China hopes to make improvements and innovations in multilateral trade rules to better balance the interests of all parties and uphold fair international trade and competition.

International patterns. As China's international status improved, the international community became increasingly concerned about China's role in international affairs, including international economic relations, and hoped that China would assume more responsibilities. In this period, bilateral and regional cooperation of various kinds was actively carried forward. However, for various reasons, the Asia-Pacific region has not yet formed mature regional economic cooperation organizations like the European Union or the region covered under the North American Free Trade Agreement. China started by creating an external environment favourable to its own development, hoping to strengthen regional economic cooperation with surrounding areas and to strengthen bilateral economic and trade cooperation with more partners to seek common future development.

3.2 Trends in China's commercial policy strategy

China's accession to the WTO resulted from the country's implementation of reforms and opening policies, the establishment of the socialist market economic system and active integration into the world economy. After its accession to the WTO, China's foreign economic and trade policies placed more stress on opening up and cooperation and paid more attention to the coordination of growth. Opening up, cooperation, identifying win-win situations and sustainable development are China's long-term goals for the future development of its foreign trade.

More emphasis on opening up means that China is becoming increasingly aware of the fact that the world of today is an open world, economic globalization is developing rapidly, and the international division of labour has become deeper and more extensive. China's accession to the WTO makes its market more open, allowing it to merge with the world market into an organic whole. China must face up to more intense competition with foreign enterprises and commodities while at the same time, through integration into the global economy and through international industrial transfer, gaining more opportunities to give play to its own advantages and accelerate its own development.

More emphasis on cooperation means that China earnestly follows all the international trade rules in its foreign trade and economic activities, fulfills its obligations to expand market access, actively participates in and promotes bilateral, regional and multilateral cooperation, strives to achieve mutual benefits and win-win situations, and shares the development results with trade partners. China must take the interests of partners, particularly developing countries, into account while achieving national development. It must also consider all parties concerned in the face of various contradictions and conflicts and, as far as possible, find a way out through consultation and negotiation. China will never harm others to benefit itself.

More attention to the coordination of growth means that China has made the scientific outlook on development a guideline for economic work in the new era. In light of new problems concerning the internal and external economy, China will place more emphasis on balance and coordination among external and domestic demands, foreign and domestic capital and investments, imports and exports (including growth rates, quality and efficiency), the relationship between foreign trade and resources and the environment, and the relationship between foreign trade and the national economy. China is trying to realize comprehensive and coordinated sustainable development and develop resource-saving and environmentally friendly trade.

3.3 A new player in the multilateral trade regime

Over the six years since China's accession to the WTO, China has strictly abided by WTO rules and conscientiously fulfilled various obligations and commitments. First, China has significantly reduced its import tariffs, reducing the average tariff from 15.3 per cent in 2001 to 9.8 per cent at present. Of this, the average tariff on industrial products dropped from 14.8 per cent prior to accession to 8.9 per cent after; the average tariff on agricultural products decreased from 23.2 to 15.2 per cent, and both were much lower than those in Japan and the European Union.

Second, China has reduced non-tariff barriers and abolished import quotas, trade permits and other non-tariff measures, so enterprises no longer need government approval for getting engaged in foreign trade. Third, China has actively opened up its service trade market and made specific opening commitments in nine out of the 12 fields in the service trade and 102 of the 160 subfields, much higher than the commitment level of the general developing countries and actually higher than some developed countries for service areas such as banking, insurance, telecommunications and transportation. Fourth, China has strengthened the protection of intellectual property rights, setting up a two-pronged administrative and judicial protection system with Chinese characteristics, and has intensified law enforcement for the protection of intellectual property. The Chinese legal system for intellectual property rights has reached the protection standards required by the WTO council on trade-related aspects of intellectual property rights. Finally, China is improving a unified and transparent legal system in line with WTO requirements. The country has cleaned up or abolished 2,300 rules and regulations in its administrative departments.

From April 19 to 21, 2006, the WTO reviewed China's trade policies for the first time since China's accession to the WTO. In this deliberation, all the representatives of participating WTO members thought highly of China's performance on its commitments. They believed that China's accession to the WTO not only promoted China's reform and opening-up process but also brought opportunities to the world. They also believed that China's fully abiding by its commitments was a major contribution to the multilateral trading system. Of course, some members put forward

proposals on specific aspects of China's trade policies that need to be revised and improved, as well as on such issues as strict implementation, timely communication and transparency of policies. The Chinese government attached great importance to the views of members and made some improvements after the conference. Sun Zhenyu, Chinese ambassador to the WTO in Geneva, said, "Three Director-Generals of the WTO all fully affirmed China's great efforts and achievements, and the Director-General Pascal Lamy ranked China A-plus" (www.china.com.cn, January, 23, 2008).

From May 21 to 23, 2008, the WTO reviewed China's trade policies for the second time, in Geneva. Before the review, 19 parties, such as the United States, European Union, Brazil and India, put forward over 900 questions about specific aspects of China's trade policies. China gave printed answers to most of these. During the review, some parties raised more questions about the rising prices of grain, balance of international payments, transparency of the trade regime, technical barriers to trade, subsidies, limits to exports, law enforcement for intellectual property rights, industrial policies, governmental purchases and service sector opening. The Chinese delegates answered these questions. The chairman of the review meeting praised China for its efforts.

3.3.1 Participation in the Doha Round

China places great emphasis on participating in and promoting the Doha Round negotiations and has presented more than 40 proposals and position papers covering many areas of the negotiations. In the Cancún meeting, held in September 2003, China, together with 19 other members, including India and Brazil, jointly formed the famous "20-Nation Coordination Group" (G20), which played an important role in pushing the negotiations toward the direction of balanced development. In the WTO mini-ministerial meeting held in Dalian, China, in July 2005, China coordinated in-depth discussions on the difficult problems of the negotiations. During the WTO ministerial conference held in Hong Kong in December 2005, China addressed the general assembly as well as participating in all seven "green room meetings" with more than 30 major WTO members, conducting bilateral talks with 21 ministers of the member countries, and participating in dozens of senior official meetings and consultative group discussions. China played a positive role in promoting the meetings to achieve results in terms of reducing agricultural subsidies and providing the least developed countries (LDCs) with tariff- and quota-free treatment.

In late July 2008 the WTO held a mini-ministerial meeting, attended by major members in Geneva, to negotiate solutions to the last critical problems. Some members, including China, made certain compromises and concessions on issues such as reductions in overall trade-distorting domestic support for developed members, sensitive products, special safeguards and anti-concentration clauses. However, the negotiations broke down because of the differences between the United States and India over special safeguards for agricultural products. Chinese officials regard this as a serious setback to the Doha Round and fear the failure will have a serious negative impact on the fragile

multilateral trading system (Chen, D., 2008).

3.3.2 Resolution of disputes with main trading partners

With the rapid growth of foreign trade after joining the WTO, China's trade disputes and frictions with its major trading partners are increasing rapidly. The relatively well-known concerns are the Sino-EU and Sino-U.S. textile disputes, as well as disputes over such issues as steel products, intellectual property, trade balance, the yuan exchange rate, auto parts, food safety and Sino-Japanese agricultural products.

Objectively, the trade disputes facing China are to a certain degree inevitable and long-lasting. The rapid take-off of China and other emerging economies, and the dramatic changes in the pattern of international division of labour, will inevitably lead to changes in the distribution of interests, resulting in a game between the countries with vested interests and the large emerging countries. Therefore the current trade disputes are, in general, the product of global economic and trade development. As long as the established dispute settlement procedures are followed and the interests of all parties are taken into account, current disputes are not likely to lead to all-round confrontation and conflict.

The Chinese side has always believed that the best way to resolve various trade disputes is through consultations and negotiations within the WTO rules and system, with good intentions toward others, instead of through confrontation and sanctions. In 2005 China reached a textile trade memorandum of understanding with the United States and European Union. China has exchanged views on trade disputes with the United States, Europe, Japan and other major trading partners, reached understandings or consensus, and avoided the intensification of disputes using tools such as the Sino-U.S. strategic economic dialogue and U.S.-China Joint Economic Committee, the EU-China Joint Economic and Trade Committee, and high-level economic dialogue with Japan, as well as by strengthening high-level visits between the two sides concerned. China reformed its mechanism for setting the exchange rate, gave up the mechanism pegged to the U.S. dollar, and expanded the floating flexibility of the yuan according to market supply and demand. It also put in order the domestic market operations, intensified law enforcement for the protection of intellectual property rights, and severely cracked down on infringement and piracy acts. Finally, it actively adopted measures to curb excessive growth of exports and expand imports.

Naturally, not all the trade disputes between China and its trading partners can be resolved through consultations and negotiations. Many cases have been brought under the WTO dispute settlement mechanism. For example, in 2002 eight members, including China, the European Union and Japan, brought a case against the United States' protective tariffs on steel products. In 2004 the United States brought a case dealing with China's discrimination against imported semiconductor products.

In 2006 the European Union, the United States and Canada filed a case against China's tariff on imported auto parts. In 2007 the United States brought a case against China's trade subsidies and lodged a complaint against China's failure to crack down on copying and restrictions of U.S. movies, music, and books. In April 2009 China filed a case against the United States over Clause 727 of the 2009 General Finance Bill, which placed barriers on China's poultry exports to the United States. Some of these cases were settled because disputing parties made some compromise, and some were arbitrated by the WTO. On the whole this did not affect the overall development of economic and trade relations between China and its major trading partners. China has also learned lessons from these experiences. However, the Chinese government's stand is that "dialogue is better than confrontation, and cooperation is better than pressure" between governments, and that governments should make efforts to resolve conflicts through negotiations (www.people.com.cn, May 25, 2007).

3.3.3 China's position toward the multilateral trade regime and Doha round

China is a firm defender of the multilateral trade system. China introduced the policy of reform and opening up in 1978, and since then it has been rapidly integrated into the global economy. China went through 15 years of tough negotiations before formally entering the world's multilateral trade system. After its accession to the WTO, China strictly fulfilled its commitments, fully demonstrating China's persistence and seriousness under the system. Currently, economic globalization is deepening, but it is raising various new contradictions for economics and trade. These must be settled within the framework of the multilateral trading system. A reasonable and effective multilateral trading system is conducive to the sustained and stable growth of the world's economy and trade, as well as to China's peaceful rise and its sustainable development of foreign trade.

China respects the results achieved so far by the negotiations within the multilateral trading system, and it complies with WTO rules. At the same time, Chinese officials believe that the WTO needs reform and improvement, and they advocate the establishment of a more equitable, secure and non-discriminatory multilateral trading system. The new round of multilateral trade negotiations must take into account the balance of interests among countries at different levels of development and respect the economic development objectives and opening-up modes of developing countries. Without the full participation of developing countries, economic globalization is unfair and incomplete.

At the very beginning of the Doha negotiations, China put forward the proposal of "four musts": any new trade agreement must:

1. Give full consideration to the development levels of the relevant industries in the developing countries and give special treatment in terms of the degree and speed with which those sectors are expected to open up.
2. Take practical and effective measures to ensure the implementation of the Uruguay Round agreements.
3. Ensure the full and effective participation of the developing members and that negotiations be conducted on the basis of equal consultations.
4. Negotiate in a balanced and coordinated approach to guarantee that the outcome of the negotiations embodies an overall balance of the interests of all parties. (Shi, 2001).

The Sixth WTO Ministerial Conference was held in Hong Kong in December 2005. Chinese Commerce Minister Bo Xilai said at the meeting that the Doha Round negotiations were a “development round,” and the international community had reached a consensus to help developing countries gain more. As the world’s largest developing country, it is China’s inescapable responsibility to actively participate in the development round of negotiations. Despite the fact that China still faces many difficulties as a developing country, its government and economic circles are willing to actively promote the facilitation and liberalization process of global trade as well as to play a constructive role in the current round of negotiations (www.sina.com.cn, December 14, 2005). Driven by the world’s major economies, the Hong Kong conference eventually reached compromise on such issues as abolishing agricultural subsidies, which gave the Doha negotiations new momentum. China took the initiative to promise to offer tariff- and quota-free market access and trade aids to the LDCs and made a positive contribution to the success of the conference.

As the biggest target of anti-dumping and special safeguard measures and similar provisions, China is against the trend of abusing various trade relief measures. In the Doha negotiations, China was always supportive of clarifying and improving the existing agreements. China also strongly urged all the key members, especially the developed countries, to recognize China’s full market economy status as soon as possible to enable the Chinese enterprises and goods to participate in international market competition on an equal footing.

3.4 China’s regional economic cooperation

China adheres to a foreign policy of making friends with its neighbours and always making them partners, strengthens good-neighbourly relations and practical cooperation with them, and energetically engages in regional cooperation in order to jointly create a peaceful and stable regional environment featuring equality, mutual trust and cooperation. The content added to Article 5 of the Foreign Trade Law, revised in 2004, provides evidence of this: “The People’s Republic of China shall promote and develop trade relations with other countries and regions based on the principles

of equality and mutual benefit, conclude or accede to regional economic and trade agreements, such as agreements on tariff alliances and free trade zones, and participate in regional economic organizations.” Active participation in and promotion of regional economic integration is China’s long-term strategy to develop good-neighbourly and friendly relations and create a stable and harmonious environment for foreign trade.

China does not seek special status; instead, China upholds equality and mutual benefit for regional economic cooperation. The historical, cultural, political and economic barriers and differences among the economies in China’s neighbouring regions have existed for a long time, and their relations are complex. It is necessary not only to coordinate the relations among major powers but, more importantly, to pay attention to the interests of the small and less developed countries, win their trust, and gradually form a common political will in order to push forward cooperation and the establishment of a free trade zone encompassing China and its neighbouring countries and regions. In promoting this goal, it is more important for China to have patience, pay attention to maintaining diversity, and uphold flexible and pragmatic principles. China is willing to fully participate in various regional cooperation mechanisms and hopes to explore with Asian countries the establishment of various forms of free trade arrangements and, finally, an Asian free trade cooperation network. At the same time, China stands for open regionalism and is willing to make the non-discriminatory principle the basis of trade liberalization. In other words, China will actively expand exchanges and cooperation with countries outside the region while deepening regional economic cooperation.

In recent years the rapid development of regional economic cooperation and integration has become an important trend for various major economies in promoting free trade and enhancing trade competitiveness. China works hard to strengthen regional economic cooperation while actively upholding and participating in the multilateral trading system. Currently the regional economic cooperation arrangements in which China has taken part include:

Asia-Pacific Economic Cooperation. China formally joined in 1991. In addition to the annual informal leaders’ meeting, Asia-Pacific Economic Cooperation has already formed multilevel working mechanisms, including the financial and trade ministerial meetings, Senior Officials Meetings, committees and working groups, and the secretariat. The leaders’ meeting in 1994 determined the “Bogor Goals” of trade and investment liberalization, that is, that the developed and developing members should achieve trade and investment liberalization and facilitation in 2010 and 2020, respectively. The leaders’ meetings in 1995 and 1996 adopted the “Osaka Action Agenda” and the “Manila Action Plan,” respectively, to implement the goals of trade and investment liberalization. Asia-Pacific Economic Cooperation is a coordinating forum, and its conference resolutions and member countries’ commitments are not mandatory to the members.

China-ASEAN free trade zone. China has signed agreements on trade in goods and services in the China-ASEAN Free Trade Area with the Association of Southeast Asian Nations (ASEAN), and the Agreement on Trade in Goods has been in effect since July 2005. At present China has reduced tariffs on 5,375 kinds of products for the ASEAN countries, and the average tax rate has dropped from 9.9 per cent to 5.8 per cent. At the same time, the ASEAN countries' average tariffs on China's exports have decreased to different degrees ("China mulls curbs," 2007). Over the past two years, China and ASEAN have enjoyed accelerated growth of bilateral trade, deepened economic integration and enhanced business links, which benefit their populations. China-ASEAN trade volume reached US\$160.84 billion in 2006 and US\$202.55 billion in 2007, an increase of 23.4 and 25.9 per cent, respectively, over the preceding year. ASEAN has become China's fourth-largest trading partner.

Shanghai Cooperation Organization. In May 2003 this organization officially launched the meetings for economic and trade ministers and the trade and investment facilitation negotiations. Its long-term goal is to gradually realize the free flow of goods, capital, services and technology, and its medium-term goal is to make stable, predictable and transparent rules and procedures, implement trade and investment facilitation and conduct large-scale economic and trade cooperation. Its short-term task is to make multilateral agreements and a list of legal measures for various nations to take in accordance with its Outline of Multilateral Economic and Trade Cooperation, determine the preferred areas for economic and trade cooperation, and demonstrate cooperation projects and put them into practice.

Asia-Pacific Trade Agreement. China joined the Bangkok Agreement in 2000. This is the first regional trade agreement with substantive preferential arrangements to which China has acceded. In November 2005 its first ministerial council was held in Beijing. The parties signed a revised version of the Bangkok Agreement and renamed it the Asia-Pacific Trade Agreement, which reserved a comparatively large space for carrying out investment, services and trade facilitation negotiations.

Greater Mekong Subregion Economic Cooperation. China, Cambodia, Laos, Myanmar, Thailand and Vietnam are the sponsor members. It was established in 1992, aiming to strengthen economic ties, eliminate poverty and promote development. The Asian Development Bank is its initiator, coordinator and major financier. Focusing on the five key strategic points of infrastructure construction, cross-border trade and investment, private sector participation, human resources development, environmental protection and sustainable use of natural resources, it developed cooperation for over 180 projects in the nine major fields of transportation, energy, telecommunications, environment, agriculture, human resources development, tourism, trade facilitation and investment, and raised funds worth more than US\$10 billion.

In addition, the regional economic cooperation China is now actively promoting or negotiating for includes the Tumen River subregional economic cooperation and the China–Gulf Cooperation and China–Southern African Customs Union FTAs. Promoted by the China-ASEAN FTAs, the mechanism for regional cooperation among China, Japan, South Korea and ASEAN is deepening.

3.5 China and free trade agreements

There has been a substantial increase in the number of regional trade agreements signed in the past 15 years. These agreements have been actively pursued and promoted by the overwhelming majority of WTO member countries, including developed and developing ones. FTAs have been widely regarded by China's major trading partners and some neighbouring countries as an important way to improve the trade and investment climate and accelerate China's economic growth.

Regional economic integration has aroused general concern in China's economic circle since the 1990s. Most scholars agree that regional economic integration and liberalization conform to the trend of economic globalization and act as a beneficial complement and driving force in the multilateral trade system (Chen, W., 2008). FTAs will increase the trade and investment opportunities among the member countries, but will also have a trade discrimination effect against non-member countries. So countries will benefit if they participate and suffer losses if they do not. China has been actively involved in regional economic integration and has established closed economic mechanisms (including FTAs) with its major trading partners. This will help to improve China's international division of labour and competitiveness and bring about a sustained and stable development in its foreign trade. At the same time, FTAs will help to strengthen the cooperation between China and neighbouring countries and achieve good-neighbourly relationships, partnerships, common development and prosperity.

For the time being, China's bilateral and regional preferential trade agreements have had good economic and political effects both at home and abroad. They have become a new form of China's opening up to the outside world and a new platform for achieving mutually beneficial progress with its trade partners (Yi, 2007). For example, a sustained and rapid growth was seen in China's trade with ASEAN in recent years, which can be largely attributed to the China-ASEAN FTA and the implementation of the Early Harvest Plan. Against this background, the October 2007 report to the 17th National Congress of the Communist Party of China clearly put forward a "strategy of free trade areas and expanding bilateral and multilateral trade and economic cooperation." At present, around 30 bilateral and regional FTAs are under process of negotiation or feasibility study. China will have a more active and open attitude toward bilateral and regional FTA negotiations.

3.5.1 Main considerations influencing China's bilateral free trade negotiations

The Chinese government actively promotes the development of bilateral economic and trade relations as well as conducting bilateral free trade negotiations to promote the following strategies:

To cope with the challenges of regional economic integration and bilateral free trade negotiations. Facing economic globalization and intense competition in trade and investment, both the developed and developing economies hope to get more reliable and preferential conditions for access to important markets through free trade negotiations, thereby creating commercial opportunities. By June 2008 the WTO had been notified of about 300 regional trade agreements, 247 of which were in force. Most of these agreements were in the form of free trade areas. It is estimated that the trade volume by the various regional trade groups accounts for more than 50 per cent of the global trade volume. Since the 1990s Asian countries have accelerated the process of regional trade liberalization. The ASEAN, China-ASEAN, India-ASEAN, Japan-ASEAN and South Korea-ASEAN free trade zones and the South Asia free trade zone were set up one after another.

During the same period, many bilateral FTAs sprang up in succession. Singapore formally signed bilateral free trade agreements with New Zealand (2000), Japan (2002), the European Free Trade Association (2002), Australia (2003), the United States (2003) and Jordan (2003), and is negotiating with Canada, Mexico, India, Sri Lanka, South Korea and other countries. Thailand formally signed bilateral FTAs with India (2003) and Australia (2004), and bilateral free trade negotiations with New Zealand and Japan are underway. Korea signed the first bilateral FTA with Chile in 2003 and has conducted bilateral negotiations with Singapore and Japan. Pakistan signed a bilateral FTA with Sri Lanka in 2005. Singapore, Chile and New Zealand also officially started trilateral FTA negotiations in October 2002. Japan's bilateral FTAs with Mexico, Singapore, Malaysia, Chile, Thailand, Indonesia and the Philippines entered into effect in April 2005, August 2005, July 2006, September 2007, November 2007, July 2008 and December 2008, respectively. If China does not attach importance to and strengthen the bilateral FTA negotiations, it will be in a disadvantageous position to expand export markets and attract and utilize foreign capital in the future.

To coordinate in the foreign policy of good-neighbourly and friendly cooperation with neighbouring countries. China's surrounding environment is generally stable and friendly, but there are also some local historical barriers and disputes over territory and territorial waters. Some countries and regions keep a wary eye on China's peaceful development. China has controversies with some neighbours about the East China Sea and the South China Sea. China has always maintained that joint development is the priority and disputes can be set aside for the time being. China sees strengthening bilateral economic and trade cooperation, achieving mutual benefits and sharing development as the most effective ways to reduce conflict, establish mutual trust and maintain regional peace. It is helpful for China to create peaceful, stable, good-neighbourly and friendly relations with its neighbouring and extended regions by signing bilateral FTAs to achieve freer flow of commodities, capital and personnel.

To create a mutually promoting situation with regional economic integration and a multilateral trading system. China's push forward with bilateral free trade areas does not exclude attempts at regional and multilateral trade liberalization. The FTAs China has signed with some countries and regions can enable China to accumulate experience in opening its domestic market and integrating into the global economy while also learning lessons related to regional economic integration and multilateral trade liberalization. Bilateral trade liberalization can further mutual promotion and can develop simultaneously with regional economic cooperation and the improvement of multilateral trading systems.

To break through prejudices and restrictions by some trading partners against China's foreign trade development. China's accession to the WTO left it with the so-called non-market economy status (Article 15 in China's Protocol of WTO Accession). This status becomes a means for some members to abuse trade relief as a weapon to limit China's exports. This is unfair to China. Therefore, in all its bilateral FTA negotiations, China has insisted on the recognition of its market economy status. Such a request not only conforms to the reality of China's economic reform process but is also conducive to breaking down prejudices and restrictions imposed by some of China's trading partners, as well as to curbing trade protectionism and maintaining an international trade order that features fair competition.

To promote the further opening of the domestic market and the reform of the governmental administration system. Both bilateral and regional FTAs involve the issue of opening up China's domestic market. For example, the two Closer Economic Partnership arrangements between the Chinese mainland and Hong Kong and Macau further opened up part of the service trade market in the mainland, the Sino-ASEAN FTA substantially increased China's imports of agricultural products from the ASEAN, and the Sino–New Zealand FTA will gradually open the imports of New Zealand's dairy and livestock products. In the past, all of these fields had met with the most resistance to opening on the mainland. Through bilateral free trade negotiations, China opened itself up first to some countries and regions, thus encountering less domestic resistance. This process is conducive to gaining experience and promoting greater opening of the domestic market, and will move forward the reform of governmental functions and administration systems.

3.5.2 Bilateral free trade negotiations: The record

In addition to the multilateral and regional economic cooperation mechanisms, the Chinese government attaches great importance to bilateral communication and exchange in economic and trade fields with all the countries and regions in the world. China has established economic and trade mixed (joint) committee mechanisms with more than 140 countries and regions. These bodies hold regular consultations to discuss bilateral economic and trade situations and resolve contradictions

and problems in order to guarantee coordinated and healthy development of economic and trade relations.

So far, in addition to the FTA signed with ASEAN, China has signed the following bilateral FTAs:

- The Closer Economic Partnership Agreement signed between the mainland and Hong Kong in June 2003.
- The Closer Economic Partnership Agreement signed between the mainland and Macau in October 2003.
- The Agreement on Free Trade in Goods and the Agreement on Free Trade in Services signed between China and Chile in November 2005 and April 2008, respectively.
- The Agreement on the Early Harvest Program for the FTA signed between China and Pakistan in August 2007.
- The FTA between China and New Zealand signed in April 2008, which is China's first FTA with a higher-income OECD member.
- The FTA between China and Singapore signed in October 2008.
- The FTA between China and Peru signed in April 2009.

China is currently negotiating bilateral free trade with countries including Australia, Iceland, Norway and Costa Rica. In addition India, Switzerland and South Korea all plan to conduct free trade negotiations with China, and some of them have officially initiated feasibility studies on free trade zones.

3.6 Sino-U.S. strategic partnership relations

Sino-U.S. relations remain the most important issue in China's foreign affairs. As the largest developing country and the largest developed country in the world, China and the United States share common strategic interests, although divergences do exist. Mutual cooperation is the focus of improving bilateral relations. China and the United States are each other's second largest trading partners, and their economies share strong complementarities. In recent years, apart from the traditional Chinese exports to the United States, such as textiles, garments, footwear, furniture and toys, exports of mechanical and electrical products and high-tech products, such as automatic data-processing equipment, machinery and electronic products, have increased rapidly. Meanwhile, China is one of the major buyers for U.S. airplanes, mechanical and electrical equipment, fertilizer, grain and chemical products. Both China and the United States have benefited tremendously from this trade and economic cooperation.

Frictions always exist in Sino-U.S. trade and economic relations. Noteworthy issues in recent years include intellectual property rights, anti-dumping, China's trade surplus, trade policy, the yuan exchange rate and U.S. export controls against China. Some issues were applied to the WTO dispute settlement mechanism, since neither side was ready to yield. However, the two countries are interdependent and each has a stake in the other, so these problems can only be solved through negotiations and consultations. China's robust development has raised some doubts and prejudice in the United States and the international society, which has led to an over-politicization of disputes and divergences. This will harm the normal development of Sino-U.S. trade and economic relations. China advocates the idea of "business is business," focusing on the overall interest of China-U.S. relations, strengthening cooperation and seeking common ground while reserving differences and achieving win-win results.

3.7 China's special and preferential trade policy toward the least developed countries

China's position on helping the LDCs is to engage in active participation and promotion. Over the years China has been providing assistance to some developing countries, in particular LDCs, to the best of its capacity. This has included debt relief, preferential loans and economic assistance. One significant measure is to apply preferential trade arrangements to LDCs that have diplomatic relations with China.

China has applied zero tariff rates to some imports from Cambodia, Laos and Vietnam since January 1, 2004, and to the 25 LDCs in Africa since January 1, 2005. In September 2005, on the 60th anniversary of the founding of the United Nations, Chinese president Hu Jintao promised that China would adopt five measures to help the developing countries, in particular the LDCs, accelerate their growth. Among these is the application of zero tariff rates to unfinished goods from LDCs that have established diplomatic relations with China. Since July 1, 2006, China has fulfilled its commitments. The number of export items from the LDCs in Africa that have diplomatic ties with China receiving zero-tariff treatment has increased from 190 to over 440. Through July 1, 2008, 42 LDCs had diplomatic ties with China. The majority of these countries' exports to China have received zero-tariff treatment.

4.0 Four major challenges likely to shape China's future trade relations

Although the focus of this paper is the commercial policies that might support the adoption of a sustainable trade strategy for China, we must take due account of the other challenges that China faces in the conduct of its trade relations. Interestingly, many facets of these challenges are related in some degree to the objectives of a sustainable trade strategy. Arguably, others are not; still, they may present alternative challenges to policy-makers in China.

4.1 A rising number of bilateral trade disagreements: going beyond trade defence instruments to regulatory policies and other forms of protectionism

From 1995 to 2008 China was the country subjected to the most anti-dumping investigations in the world. One out of seven anti-dumping cases involved China. The scope of the exports involved continues to expand, and they are mainly concentrated in light industry, textiles, electrical and mechanical items, and other labour-intensive products in which China has a competitive advantage. While the trade conflicts between China and developed countries are growing, China's trade conflicts with developing countries are also on the rise.

In addition to the anti-dumping, countervailing and safeguard measures and the special safeguard measures, barriers set up by many countries against China's technical standards, health and safety inspection, environment and labour protection, and other standards also grew, and their forms were increasingly diverse, comprehensive and overt. They were gradually extended from trade in goods to trade in services, investment, intellectual property rights, the yuan exchange rate and so on. China remains vulnerable here, especially in light of its WTO accession protocol, which allows trading partners to take certain measures, in violation of the WTO's most-favoured nation clause, against Chinese commerce for a specified number of years.

Concerns about worldwide misapplication of trade defence instruments and regulatory policies are coupled with the new, murkier forms of protectionism that have appeared during the current global economic slowdown. Discrimination in government procurement practices, which have assumed importance because of the large fiscal stimulus packages adopted by certain nations to bolster aggregate demand, has received particular attention. So-called green protectionism and the conditions applied to subsidies and bailouts received by firms headquartered in trading partners have provided another source of concern (see Baldwin and Evenett 2009 for an overview).

In recent years Chinese firms have invested abroad and developed commercial operations in greater numbers. These operations seek new ways to sell to foreign markets and can tap foreign technology and expertise. Their treatment by foreign governments is likely to be of growing concern to China. Already China has expressed concern about the restrictions certain industrialized countries have placed on the acquisitions of Chinese-owned firms, for example. This type of dispute is likely to grow in number and will probably increase Chinese interest in the behind-the-border policies of its trading partners.

Existing multilateral disciplines and regional accords do not provide for fast redress against foreign regulatory malpractice, and in some cases do not ban the use of certain types of discrimination against firms headquartered in other countries. While concerns about these forms of protectionism may lead to disputes (including warnings about “trade wars”), the medium- to longer-term consequence is that the forms of discrimination resorted to during this global economic downturn will define in part the negotiating agenda of future multilateral trade negotiations and regional trade agreements. There is historical precedent here, as the Uruguay Round’s negotiating agenda was influenced by the forms of protectionism employed in the global economic downturn of the early 1980s.

These newer forms of protectionism go well beyond tariffs and often implicate domestic policies, such as those toward subsidies and industrial policy, government procurement policy, environmental policy, national standard-setting regimes and associated certification policies, and competition law (as this can be used to frustrate the mergers or acquisitions of firms). The question arises as to whether a sufficient constituency of nations, including China, are willing to constrain some of their discretion in the implementation of these policies in return for assurances that other trading partners will do likewise. The size and location of that constituency will define whether any viable initiative is regional, sectoral or multilateral in nature.

The experience of the Doha Round, in particular the rejection of the Singapore issues (which related in large part to policies other than tariffs) by a large proportion of the WTO membership, must raise questions about the appetite for signing binding rules on these policies. Of course, the reasons for rejecting negotiations in the past need to prevail in the future (especially in light of the recent increase in protectionism); still, the question arises as to whether there are alternatives to binding accords, and this is where soft-law, non-binding alternatives come in.

4.2 Potential dispute settlement cases concerning WTO accession obligations

Even though China’s trade policy reviews have been positive, not every trading partner may share this assessment of the implementation of China’s WTO accession obligations. Moreover, some

trading partners have expressed concern about governmental measures implemented since China joined the WTO. In 2007 and 2008, for example, criticism from abroad could be heard about China's new competition law, which, some assert, disadvantages non-Chinese firms. The national treatment obligations of the GATT and GATS can be interpreted very broadly, and this may result in disputes between China and its trading partners.

While China's record of settling disputes with trading partners is encouraging (as noted earlier), some matters have been taken to WTO dispute settlement. Moreover, there are no guarantees that other matters will not be taken to the WTO for adjudication in the future. Managing such disputes has both a diplomatic and a legal dimension and, should cases be lost, a domestic political dimension, as compliance or non-compliance could implicate different Chinese interests. Bilateral dialogues and the like arguably have a role to play here, especially with larger trading partners such as the United States and the European Union.

China is entering into the late-middle stage of industrialization, namely, the stage of accelerated growth and increased production by the heavy and chemical industries. From 2001 to 2006 the average annual growth rate of the output value of China's heavy and chemical industries increased by about 16.0 per cent, 2.8 percentage points higher than light industry's rate over the same period. This is actually the result of the transfer of the international heavy and chemical industry to China and will inevitably lead to rapid growth of China's energy demand and carbon emissions.

According to calculations by Professor Wang Zheng, director of the Policy Simulation Research Centre of the Sci-Tech Policy and Management Science Institute at the Chinese Academy of Sciences, China's carbon emissions increased by 131.15 per cent from 1990 to 2005, with an average annual growth rate of about 5.8 per cent and an increased rate since 2002. In comparison, the average annual growth rate of China's GDP in the corresponding period reached 10.2 per cent. This shows that China's energy-use efficiency has been gradually improving, and GDP per unit of carbon emissions is gradually increasing (www.ycwb.com, December 6, 2007).

Nevertheless, the estimates show that China has exceeded the United States in total carbon emissions to become the world's biggest carbon emitter, releasing up to 6 billion tonnes in 2007. And China's carbon emission per capita has increased rapidly. According to International Energy Agency estimates, in 1990 it was 50.3 per cent of the average global level, rising to 60.5 per cent in 2000 and 92 per cent in 2005. Now it is equal to the world average. Although China's carbon emissions are still only one-third of developed countries' average level, they are 1.7 times higher than the average for the developing countries, and the pressure to cut its emissions is increasing ("Outlook weekly," 2009).

The growth of China's carbon emissions has received international attention and criticism. China has a large population base, and even though its carbon emissions per capita are not high, according to the International Energy Agency's estimate in its *World Energy Outlook 2007*: "China may replace the U.S. in 2007 and become the world's largest carbon emitter, and India will become the world's third-largest carbon emitter around 2015." The agency said that if China and India kept their current policies unchanged, the global annual emissions of energy-related carbon dioxide would rise from 27 billion tonnes in 2005 to 42 billion tonnes by 2030, and the economic development of the two countries will become the main driving factor. At the United Nations Climate Conference held in Bali, Indonesia, in December 2007, some industrialized countries shined the spotlight on China and India, going further to argue that China and India, like the major developed countries, must assume responsibility for emission reductions in the new global emission reduction framework.

In terms of trade policy, much depends on the manner in which any climate change treaty is implemented. In particular, concerns have been raised about so-called border tax adjustments—a form of border tax, just like a tariff—that might be imposed on imports from countries with "low" or "unacceptably low" national carbon taxes. The potential for abuse in the application of these border taxes, plus the paperwork and costs associated with even a fairly implemented regime, would fall on exporters, especially exporters from countries, like China, with high carbon emissions.

In principle, global measures to slow down climate change are not inconsistent with the underlying goals of a sustainable trade strategy for China. Nevertheless, there may be some tension between the instruments used to implement any climate change accord and some of the specific objectives of the sustainable trade strategy. Assuming China prioritizes the latter in coming years, then the sustainable trade strategy's objectives may shape the position China takes on climate change negotiations. There may well be potential complementarities (or "win-win") opportunities to be tapped here. For example, the upgrading of Chinese manufacturing industries toward higher-value-added, less-carbon-intensive goods and production processes could be substantially facilitated by technology transfer and funds negotiated as part of a climate change accord.

4.3 Until recently, the import prices of resources and energy have continued to rise sharply

From 2002 to 2007 the prices of primary commodities on the international market rose consistently. Since 2008, however, there have been substantial increases the volatility of commodity prices, which have been a disruptive influence. For example, the international oil price has risen from US\$20 per barrel in early 2002 to US\$148 per barrel in mid-2008, subsequently falling to approximately US\$50 per barrel. Similar fluctuations have been found in the prices of copper, aluminum, nickel, lead, zinc and tin. The annual price increase of iron ore has fluctuated between 8.9 and 71.5 per cent since 2003.

At present China is a net importer of primary products and the largest importer of bulk resource commodities. Consequently, the continuously rising prices of resources and energy have brought about a series of adverse effects on China's economy and trade. First, import-based inflation pressures are growing—China's consumer price index reached 4.8 per cent in 2007 and further increased to 8 per cent in the first quarter of 2008. Second, the terms of trade have deteriorated, meaning that China can buy fewer imports with its export revenues.

The price of imported resources and energy is not the only consideration—access to such resources in the first place is also important. This is of particular concern given that some resource-selling companies and jurisdictions enter into long-term contracts, limiting the amount of resources available to “second movers” or later developers. In recent years China has signed accords with a growing number of countries and firms to supply raw materials. These accords have been the subject of scrutiny in some quarters, raising concerns about the knock-on effects for other countries' sustainable development.

There is a broader, systemic implication of this discussion of resource use and the adoption of a sustainable trade strategy. Arguably the Chinese contribution to a more sustainable trajectory for global development would be mitigated if unsustainable or less-sustainable activities in China were not eliminated but were transferred to other developing countries. For example, if the abandonment by China of energy- and raw material-intensive production of low-end manufactures meant that such production expanded in Vietnam and Cambodia, then the ultimate benefit to the global environment would be less than if all East Asian nations updated their production processes together. Quite understandably, Chinese policy-makers may take the view that their primary concern is with Chinese sustainable development. Even so, any Chinese aspirations to lead the world or their region on sustainable development will require a view of resource and energy use that is not confined to within its borders, and may call for international, or at least regional, initiatives to complement national implementation of a sustainable trade strategy.

5.0 Which Chinese commercial policy options would support a sustainable trade strategy?

In this section we attempt to draw together the pertinent factors, mentioned in previous sections, that shape the options available to Chinese policy-makers as they consider implementing a sustainable trade strategy. In the discussion that follows, the policy options identified are related to each of the five objectives of that trade strategy. Readers interested in a brief summary of the principal suggestions should refer to the summary table at the end of this paper.

The first objective of the proposed sustainable trade strategy for China is to rebalance the economy away from a substantial dependence on export demand, toward domestic sources of demand, such as consumption. Of course, this matter has taken on greater importance given the recent global economic downturn and proposals that the major economies of the world, in particular the countries with large current account surpluses, engage in coordinated fiscal policy expansion. In the Chinese context, the sharp export slowdown experienced in 2008 and early 2009 testifies to the Chinese economy's vulnerability to foreign macroeconomic shocks.

Despite the importance of this first objective, it is unclear whether the traditional tools of commercial policy (unilateral, reciprocal and multilateral initiatives) are the most effective instrument to rebalance this aspect of the Chinese economy. State measures that encourage Chinese households to limit their savings and expand spending on goods and services are the prescription that follows from standard macroeconomic analysis. Increased government spending on infrastructure projects and further measures to redistribute income to poorer people (who typically spend more of their incomes and save less) will reinforce the rebalancing of demand in the Chinese economy.

Indeed, the stimulus package announced by the Chinese authorities in 2008 as well as other, prior measures are moves in this direction. They may well have to be reinforced by further steps, especially if the global economic downturn persists. Another caveat, of course, is that steps to reorient aggregate demand in China provide incentives to business to reorient supply; however, the former does not guarantee the latter. Existing state measures that slow down or impede the reallocation of resources across sectors of the Chinese economy will frustrate rebalancing too. To summarize, there is much to the rebalancing of the Chinese economy that does not implicate Chinese commercial policy.

The second objective of the sustainable trade strategy is to promote the shift of Chinese export activities into higher-valued-added goods and services, reducing the volume of Chinese commerce that foreign trading partners need to absorb but without lowering Chinese export revenues. To the

extent that higher-value-added goods and services involve production and distribution stages that are “greener,” progress along the environmental and economic dimensions of sustainable development may be possible.

Upgrading of goods, services, and associated production and delivery processes is seen as key to attaining this objective, and another paper in this project describes the national measures that China might take in this regard (Pan & Evenett, 2010). Our concern here is with the implications for Chinese commercial policy-making. As is well known, added value tends to be higher in the design and distribution stages of commercial activities as compared with the production stages. In commercial policy terms, then, an emphasis on market access must be broadened to include greater protection abroad for Chinese intellectual property and for subsidiaries established abroad to supply higher-end Chinese goods and services. Moreover, higher-end products tend to face stringent standards (quality, health, safety and so on), and these can be implemented in a way that effectively discriminates against non-domestic suppliers.

In sorting through the policy options here, there are a number of key choices. Perhaps the most important factor is whether China might seek binding measures regarding a given regulatory policy implemented by a trading partner. Binding disciplines on a regulatory policy or standard-setting regime backed by a serious dispute settlement regime covering transparency, due process and non-discrimination would have clear advantages to Chinese firms trying to upgrade. However, in each case China’s trade policy-makers will have to assess whether negotiating partners are ultimately willing to take on binding obligations and, just as importantly, whether other Chinese ministries and government agencies will be willing to accept their discretion and practices being influenced by a trade agreement. Many jurisdictions must face such an assessment when deciding whether to seek binding obligations on regulatory or other behind-the-border matters.

If binding approaches are unacceptable or unlikely to be effective, then attention turns to soft-law initiatives. In many areas of regulatory policy there are already internationally recognized soft-law initiatives. The question would then arise as to whether China’s interests are best served by an existing soft-law initiative or whether a new initiative could be created on terms that better suit both China’s needs and those of the trading partners in question.

One particularly attractive feature of a Chinese-led soft-law initiative with East Asian partners on the various regulatory policies of interest here is that it could build on a solid foundation of existing cooperation within the region. Any regulatory standards and best practices could be better tailored to East Asian circumstances. Moreover, concerns about any adverse cost implications that improved regulations would have for firms would be mitigated by the fact that other countries in the region, which are often the most aggressive competitors for the same global customers, will be undertaking the same reforms.

Another important choice facing Chinese policy-makers is whether to pursue reforms in other countries' regulatory policies through an FTA or other cooperative instrument that enables more than one regulatory policy to be addressed at the same time. An issue-by-issue approach to seeking improvements to regulations may allow for greater specificity, whereas a broader initiative may allow for common disciplines to be applied across a wide range of policies of interest to Chinese firms.

Experience in the European Union and between Australia and New Zealand suggests that progress in aligning and reforming regulatory policies seems to be possible between geographically proximate neighbours. Given China's extensive cooperative arrangements with countries in the East Asian region, perhaps the most promising vehicle for aligning foreign regulatory policies with Chinese interests in the near-to-medium term lies in a series of regional initiatives or a single cross-cutting regulatory initiative. With respect to both options, the steps taken by the Asia-Pacific Economic Cooperation nations on regulatory measures may provide some food for thought. Finally, a time may come in the medium-to-longer term where further progress on regulatory reform is possible at the WTO; however, in the near term, initiatives in East Asia or in selected FTAs outside of East Asia probably offer the greatest scope for progress on the second objective.

The sustainable trade strategy's third objective is to promote the development of China's service sector, potentially even at the expense of the manufacturing sector. Another paper in this project examines this objective in greater length (Zhang & Evenett, 2010); here we are concerned with what Chinese commercial policy can contribute toward this objective. Even if service sectors could be identified where foreign direct investments or foreign personnel could make a substantial contribution to the development of the respective Chinese service sector, the question arises as to whether China should open this market unilaterally or as part of a reciprocal trade agreement, possibly to a select group of trading partners. There may well be some service sectors where foreign investment has a positive track record in China or in other developing countries, but where domestic sensitivities limit the amount of market opening. Of course, opening a service sector to firms in a foreign nation with no expertise in a given service may effectively shield Chinese rivals from any competition, but this hardly helps improve the Chinese sector either.

With respect to opening unilaterally or opening to a subset or all of China's trading partners, in reality little may differentiate these two options. (The implication being that preferential opening to a select group of trading partners may not limit competition, in large part for the reason given next.) The so-called rules of origin of service sector firms in FTAs, say between two countries, A and B, often refer to service firms that have a base in trading partner A having, in this case, access (through exporting, the right to establish a subsidiary and so on) in country B. A firm headquartered in a non-signatory to the FTA between A and B may have an established commercial presence in country A and therefore be entitled to supply services under the FTA to country B. For this reason, experts on service sector liberalization tend to argue that little is gained in terms of shielding domestic service sector firms from foreign competition by signing an FTA of this type.

The previous paragraph suggests that market opening is essentially a choice between unilateral or multilateral reform. Of course, given that the latter accords deal with commitments to measures such as market access, it would be possible for China to progressively liberalize foreign market access on a unilateral basis while retaining the “negotiating chip” of not locking in that reform until a sufficiently attractive multilateral trade deal is obtainable. Therefore, in the near-to-medium term Chinese policy-makers might progressively and unilaterally liberalize service sectors where additional foreign competition and managerial practices could trigger improvements by Chinese rivals. Over the longer term such unilateral opening may be reinforced by negotiated multilateral commitments, which offer better access to foreign services markets and greater certainty.

The development of Chinese service sector firms that can supply foreign markets while being based in China, for example, with back-office services, is another potential goal. The trade policy contribution to this subsidiary objective would take the form of making sure that the temporary movement of Chinese service sector experts into foreign markets to advise and consult with clients was not unduly permitted and to making sure that the liability laws of trading partners are not changed so as to effectively preclude the international outsourcing of services.

In this regard the experience of India is significant and could be studied in greater detail. In recent years industrialized country restrictions on temporary movement of persons and liability law changes have been concerns of Indian service sector providers, especially in their dealings with the U.S. market. More generally, the growing number of developing countries that effectively established themselves as providers of back-office and software services could become allies of China in any international initiative to keep industrialized countries’ service sector markets open. The worsened limitations on the access to visas for foreign workers in a number of countries over the past 12 months as a result of the global economic downturn suggest that this is not a hypothetical consideration.

With respect to the fourth objective, that of promoting Chinese firms, brands and intellectual property in the world economy, to the extent that there is a direct role for Chinese commercial policies, that role relates to limiting the costs faced by Chinese firms and discrimination from foreign regulatory processes. Those processes relate to foreign investments (that condition commercial presence); protection of copyrights, trademarks and other forms of intellectual property; merger and acquisition laws and the like. The considerations raised in the discussion above of the potential contributions of binding, reciprocal agreements and soft-law alternatives to attaining the second objective apply with equal force here.

The fifth objective of a sustainable trade strategy, supporting the development of a harmonious, sustainable multilateral trading system, may have a number of implications for Chinese commercial

policy-making. Several aspects relating to this objective are discussed here, but nothing should be inferred from the order in which we discuss them.

It is highly likely that several of China's trading partners will continue to raise complaints against what they perceive as infractions of WTO accords. In the past 12 months the United States and the European Union have raised the profile of their trade disputes with China, in some cases joining other countries in bringing formal disputes to the WTO's Dispute Settlement Understanding. It seems that the patience of China's trading partners is running out.

As far as managing these almost inevitable disputes, one option available to Chinese authorities is to strengthen the bilateral dialogues underway with its major trading partners and potentially create dialogues with other trading partners. Dialogues are, of course, two-way processes and would enable China to raise concerns about regulatory and trade policies in trading partners. If successful, dialogues would forestall the development of formal legal trade disputes and dissipate criticism.

In deliberations during the Doha Round, Chinese officials have indicated a desire to see the multilateral trading system evolve in a manner that better favours developing countries. This is a distinct matter from managing trade disputes and relates much more to the agenda-setting and decision-making processes of the WTO. Of course, in the near term the matter of completing the Doha Round on terms that China finds agreeable will be the first priority.

Over the medium to longer term the extent to which China's WTO membership can be used to advance the objectives of any sustainable trade strategy will depend on whether the WTO membership decides the multilateral trading system is a useful place to develop further multilateral rules. Typically there is a several-year hiatus between the conclusion of one round and the start of another. This does not preclude China's advancing elements of its sustainable trade strategy through plurilateral and critical mass agreements at the WTO, but even these initiatives would require the assent of the entire WTO membership at the beginning and end of any such negotiation. Progress at the WTO, then, is hostage to the entire membership's views.

Given that many of the elements of China's development trajectory are shared by other developing countries (such as having a growing number of national firms that are expanding abroad for the first time), developing country constituencies may coalesce behind WTO initiatives that limit impediments to upgrading (such as inappropriate technical barriers to trade and sanitary and phytosanitary standards), condition policies affecting the overseas expansion of Chinese firms (such as investment rules and competition laws), open service sector markets and ensure that environmental protection does not become a form of protectionism. Again, much will depend on whether countries that seek improvements in trading partners' regulatory regimes are prepared to take on binding obligations for their own regulatory policies and practices. The willingness to take

on binding obligations may grow over time, so an incremental approach may be feasible. Consultation with Chinese firms that are active in international markets may reveal which foreign regulatory policies are of greatest concern, facilitating the prioritization implied by an incremental approach.

Deliberations at the WTO are likely to be dominated by the Doha Round for the foreseeable future, and any conclusion of these multilateral trade negotiations followed by a likely hiatus of five years or so, so the international initiative of greatest relevance to sustainable development in China may be that relating to climate change. Indeed, the international and national measures taken in light of any climate change accord are likely to be a more promising near- to medium-term vehicle for advancing a sustainable trade strategy than China's WTO membership. Ensuring compatibility between that strategy and any global climate change accord will be a central priority for Chinese policy-making.

6.0 Concluding remarks

In this paper we outlined the objectives of a Chinese sustainable trade strategy along with a number of recent trade-related and other developments that are likely to affect Chinese trade policy priorities. Ultimately the purpose has been to sketch out the different commercial policy initiatives that could advance a sustainable trade strategy. A table relating each of the five objectives of a sustainable trade strategy to potential commercial policy initiatives follows this section and summarizes the key findings of this study.

The commercial policy options identified in this study indicate how Chinese trade policy-making could be aligned with the objectives of sustainable development in China. Having said that, we stressed that not every trade policy instrument will significantly contribute to each objective of the sustainable trade strategy and, indeed, one of those objectives (the first) is probably best addressed through macroeconomic and other non-trade policies. Our discussion, then, seeks to shed light on what can be reasonably expected of commercial policies in advancing sustainable development in an economy of growing global significance.

One consideration that recurred throughout this study was the extent to which China and its trading partners were willing to take on binding commitments in trade agreements with respect to regulatory policies that are most implicated by the sustainable trade strategy. Of course, willingness to take on binding commitments may change over time, and incremental, confidence-building soft-law initiatives may have particular appeal in the near-to-medium term.

With respect to the role that China's WTO membership can play in advancing its sustainable trade strategy, the legacy of the Doha Round of multilateral trade negotiations cannot be overlooked, and suggests that the potential for new initiatives in that forum are only likely in the medium-to-longer term. Ensuring that the outcome of any global accord on climate change is aligned with Chinese priorities for sustainable development is a more pressing priority.

Taken together, these observations indicate that China's sustainable trade strategy is likely to be advanced by bilateral and regional dialogue-driven and soft-law measures in the near-to-medium term, complemented possibly by a global climate change accord. The development of binding obligations on the regulatory matters of direct interest to a Chinese sustainable trade strategy is a far longer-term and worthwhile enterprise.

Objectives of China's sustainable trade strategy	Recommendations for choice of trade policy instruments
1. Promote the rebalancing of the Chinese economy away from its currently unsustainable path.	<ul style="list-style-type: none"> • Use macroeconomic tools and reforms to public services and the welfare state that decrease the need for Chinese households to save so much. • Fulfillment of this objective is not suited to trade policy tools.
2. Promote added value in economic activities, not just sales.	<ul style="list-style-type: none"> • Do not prioritize reciprocal trade agreements (bilateral, regional and multilateral) that seek lower tariffs on low-end manufactured goods. • If upgrading of exports is frustrated by inappropriate use of foreign standards, seek obligations on transparency, non-discrimination and process rights in binding accords (assuming foreign demands are acceptable to China) or soft-law accords.
3. Promote services, not just manufacturing.	<ul style="list-style-type: none"> • Prioritize reciprocal trade accords (bilateral, regional, multilateral, plurilateral or critical mass) in service sectors of interest to China. • Place less emphasis on securing access to foreign markets for manufacturing.
4. Promote Chinese firms (including multinationals), brands and intellectual property rights. (Nationality matters.)	<ul style="list-style-type: none"> • Seek changes and improvements to relevant foreign national laws and enforcement processes, and obligations on transparency, non-discrimination and process rights in binding accords (assuming foreign demands are acceptable to China) or soft-law accords.
5. Support a harmonious, sustainable architecture for international trade.	<ul style="list-style-type: none"> • Establish and reinforce bilateral processes to limit trade disputes. • Once the Doha Round is completed, advance multilateral initiatives in the policy areas associated with upgrading, the overseas expansion of Chinese firms (such as competition law), service sector reform and environmental protection at the appropriate time and if China is prepared to take on binding commitments in these policy areas. • Monitor climate change negotiations to ensure that the likely impact of any accord is consistent with China's sustainable trade strategy.

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