This paper examines the impressive growth in Chinese trade since the late 1970s, and argues that the roots of this growth can ultimately be traced to two key developments: domestic reforms in 1979 and accession to the WTO in 2001.
I. Two Key Moments in History

When examining individual countries’ trade histories, it is hard to find a more compelling argument in support of trade than that expressed by the past twenty to thirty years of Chinese growth. In that time, the People’s Republic of China has gone from being a closed communist economy struggling to recover from the failed policies of Mao’s “Great Leap Forward” and Cultural Revolution to quickly closing in on Japan’s spot as the second-largest economy in the world (2009 will be Japan’s last year as such).

Ultimately, the drive behind China’s economic success can be largely traced to two major milestones. In December of 1978, Deng Xiaoping announced his policy of *gaige kaifang* (literally “reform and opening up”), beginning a transition away from three decades of centrally-planned economics. As part of his effort to modernize China, Deng introduced reforms aiming to reduce barriers to trade.

The second milestone came in 2001, when China finally succeeded in its effort to join the World Trade Organization (WTO). As part of the terms of accession, China further reduced tariffs and took other steps to encourage international trade. This paper examines both the state of Chinese foreign trade today as well as how the changes in 1978 and 2001 helped spur growth to its current levels.
II. A Brief Overview of Chinese Trade

The preceding graph traces China’s exports, imports, and trade balance (net exports) across more than a half-century of economic history. As is evident from the graph, trade was negligible and stagnant under the Maoist policies of the 1950s to mid-1970s. Imports and exports first began to expand just around the reforms of 1978, a fact demonstrated more clearly if the graph is focused to neighboring decades (see Appendix A). Imports and exports continue to grow slowly during and after this initial reform stage until the turn of the century. Then, in 2001, China’s accession to the WTO and the accompanying policy changes result in a massive growth in both imports and exports. Exports seem to have benefitted more than imports, which is reflected in the sprouting trade surplus after 2003.

It is important to note that the graph above is cut off in 2007, the last data set included in the original source. Starting in 2008, of course, the global economy was rocked by the financial crisis and an ensuing recession. This was reflected in China’s trade numbers for 2009, when
exports fell 16% over the year before.¹ This was the first time since 1970 that exports had dropped more than 1% (with only two drops, each of .6%, in 1983 and 1996).² Still, the negative effects on China’s economy were remarkably minimal when compared to other top economies. By December 2009, Chinese exports were once again expanding.³

### III. China’s Trading Partners

<table>
<thead>
<tr>
<th>Trading Partners</th>
<th>Export Destinations</th>
<th>Import Origins</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Country/region</strong></td>
<td><strong>Value</strong>*</td>
<td><strong>Country/region</strong></td>
</tr>
<tr>
<td>United States</td>
<td>298.3</td>
<td>United States</td>
</tr>
<tr>
<td>Japan</td>
<td>228.9</td>
<td>Hong Kong</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>174.9</td>
<td>Japan</td>
</tr>
<tr>
<td>South Korea</td>
<td>156.2</td>
<td>South Korea</td>
</tr>
<tr>
<td>Taiwan</td>
<td>106.2</td>
<td>Germany</td>
</tr>
</tbody>
</table>

*Value in billions USD

The table above (shown graphically in Appendix B) lists China’s top trading partners, export recipients, and importers in 2009. The United States, Japan, South Korea, and Germany are present across the board (total trade with Germany is $105.7 billion total, falling just short of Taiwan). The United States’ total is dominated by the goods it imports from China, but it is also a significant bilateral exporter. The United States can be grouped with Japan and Germany (the world’s 1st, 2nd, and 4th largest economies, respectively) as trading partners which are important simply because of their global economic role. The other top partners also have strong economies, but not enough to justify their inclusion over France or the UK, for example. Instead, China

¹ Wu 2010  
² Heston, Summers and Aten 2009  
³ Wu 2010
trades with South Korea and “countries” like Hong Kong and Taiwan because their geographic proximity makes them natural markets.

Hong Kong and Taiwan are particularly interesting examples because their trade totals are so unbalanced. China exports extensively to Hong Kong, but imports almost nothing in return; the opposite case (although less extreme) exists with regards to Taiwan. This is because Hong Kong is situated near the southern provinces of China which account for the vast majority of Chinese manufacturing. Guangdong, China’s most productive province, is situated directly adjacent to Hong Kong. Combined with its access to international trade routes, this makes Hong Kong a natural entrepôt where Chinese goods are funneled for re-exporting abroad. Imports arriving in China, on the other hand, are more broadly distributed based on consumption. Wealthier provinces and provincial level cities (like Jiangsu province and Shanghai) to the east are accessed at lower cost by direct exports to those areas.

Taiwan, as mentioned above, exports a significant amount to China but imports relatively little. Taiwan has a highly-developed manufacturing sector, which is why China is eager to import Taiwanese goods. However, the total population of Taiwan is barely 23 million, making it a relatively small market for Chinese exports.
IV. China’s Top Commodities

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Electrical machinery and equipment</td>
<td>301</td>
<td>Electrical machinery and equipment</td>
<td>244</td>
</tr>
<tr>
<td>Power generation equipment</td>
<td>236</td>
<td>Mineral fuel and oil</td>
<td>124</td>
</tr>
<tr>
<td>Apparel</td>
<td>101</td>
<td>Power generation equipment</td>
<td>124</td>
</tr>
<tr>
<td>Iron and steel</td>
<td>47.3</td>
<td>Ores, slag and ash</td>
<td>70</td>
</tr>
<tr>
<td>Furniture</td>
<td>38.9</td>
<td>Optics and medical equipment</td>
<td>67</td>
</tr>
</tbody>
</table>


*Value in billions USD

Chinese trade (both imports and exports) is dominated by capital goods. These goods are beginning to dwarf China’s previous prominent exports of apparel and furniture, reflecting the trend of increasing development and complexity in Chinese manufacturing techniques. To fuel this manufacturing, China demands heavy imports of energy resources and fundamental ores. The category labeled “optics and medical equipment” is difficult to pinpoint because it entails optical, photographic, cinematographic, and a variety of medical equipment along with precision measuring tools. As per capita GDP rises (Appendix 3), increased disposable income may be driving Chinese consumers to buy more “luxury” personal electronics such as cameras and camcorders. Furthermore, the Chinese government is eager to complement economic modernization with social services progress in the form of sophisticated healthcare. In any case, 2009 does not represent an unusual level of demand for items in this category; China imported around $60 billion within this category in 2005.4

V. China and the WTO

While Deng’s reforms in 1978 set the stage for China to begin contemplating economic liberalization and growth, the recent explosive growth in Chinese trade is primarily due to its ultimate accession to the World Trade Organization (WTO) in December 2001. The admission

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4 “China’s Customs Statistics”, 2005
process took 15 and a half years, the longest in WTO history until it was surpassed by Russia in 2009.⁵ The process was extensively drawn-out because of concerns held by WTO members (prominently including the United States) regarding fair competition in international trade. Thus, China was only allowed to join the WTO after making dramatic reductions to trade barriers.

One clear requirement for China to be eligible to join the WTO was a substantial drop in import tariffs. In 1996, a decade into the negotiations, China cut tariffs from an average of 35% to 23%. A year later, tariffs were further reduced to 17%. In 2001, several months before being accepted into the WTO, China again lowered tariffs, this time to a little over 15%.⁶ As part of the negotiations, a “US-China Bilateral WTO Agreement” was reached in November 1999. This agreement stipulated that China would continue to reduce tariffs until a goal of 9.4% in 2005.⁷ China did continue lowering tariffs after its accession to the WTO, but only reached 9.6% in 2009.⁸ Today, China has a tariff imbalance similar to the United States in that agricultural tariffs are much higher than those levied on manufactured goods (15.7% compared to 9.2%). This is presumably a decision by policymakers to preserve social stability by protecting the 900 million residents of rural China, most of who rely on some form of agricultural production for sustenance.

The bilateral agreement with the United States addressed a host of other topics as well, including several interesting points. China agreed in principle to raise its annual foreign movie import quota from 10 to 40 films (it was instead lifted to 20, where it still stands today).¹⁰

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⁵ “Becoming a Member of the WTO”, 2005
⁶ “Reducing Customs Duties”
⁷ “Summary of US-China Bilateral WTO Agreement”, 1999
⁸ “2009 China Customs”, 2010
⁹ “China’s rural population to halve in 30 years: economist”, 2010
¹⁰ Epstein, 2009
Another point of the agreement required China to allow private entities to participate in the import/export industry without direct government supervision.\textsuperscript{11}

The chart above displays Chinese exports in the decades immediately surrounding WTO accession in 2001. There was a clear upward shift in the slope (which represents the increase in value of exports per year) at this point. In fact, this rate multiplied more than six-fold in 2001-2007 compared to 1990-2001, from 190 billion RMB/year to 1.2 trillion RMB/year.

In the Doha round of negotiations, China was relatively inactive for an economic player of its size. One former US trade official suggested that China was “still somewhere between the developed and developing world…it looks for maximum flexibility in this regard, and it doesn't want to get out in front on any position.”\textsuperscript{12} In this sense, China was (and remains) in a complicated situation. While its advanced export sector would stand to gain from expanded access to developing markets (allying it with the United States and other developed countries), it

\textsuperscript{11} “Summary of US-China Bilateral WTO Agreement”, 1999  
\textsuperscript{12} “Q&A: China Post-Doha”
Three Decades of Chinese Trade, 1978-2008

still feels unable to compete successfully on a level playing field with the world’s most-developed countries (aligning it with the developing world). Ultimately, an inability for the United States, China, and India to come to an agreement on agricultural subsidies was one of the main reasons the Doha talks collapsed in 2008.\textsuperscript{13}

VI. Openness in the Chinese Economy

For a country of its economic size, China is quite open. The graph above reflects openness by measuring total trade as a percentage of GDP. In 2007, China’s openness score was 80%, second only to Germany (86%) among the top ten GDPs worldwide. Although the graph is rather uneven, some basic trends can be spotted. From 1952 to 1978, openness averaged 11%. The reforms of 1978 are immediately accompanied by a small jump in openness, which averages 28% until 2001. After WTO accession in 2001, there is a clear and sustained rise in openness.

\textsuperscript{13} ibid
VII. Institutional Development

China is not yet a full-developed country, and perhaps in no area is this as clear as in institutional development. The Corruption Perceptions Index in 2010 gave China a 3.5/10 for a ranking of 78th out of 178 countries worldwide. While this may suggest China is performing above-average in terms of corruption, consider the fact that China was ranked last among the world’s top ten economies. This corruption may be an unfortunate consequence of the reform period under Deng Xiaoping. Deng greatly diminished the central government’s involvement in local administration and gave local government much more control over policies to encourage economic growth. These factors combined to make it simple and low-risk for local officials to make money from bribes and special deals with local entrepreneurs.

This lack of central control over local affairs also manifests itself in another weak spot in China’s institutional development: the protection of intellectual property rights (IPR). The United States Trade Representative kept China at the top of its “priority watch list” in 2009 due to unsatisfactory enforcement of IPR regulations. The report acknowledged China’s “increased attention to the IPR environment” but concluded that “China’s IPR enforcement regime remains largely ineffective and non-deterrent”. Particularly as China’s manufacturing becomes increasingly developed, the United States will push the issue of IPR protection in negotiations as a way to preserve its competitiveness in high-tech industries.

14 “Corruption Perceptions Index”, 2010
15 “Priority Watch List”, 2009
VIII. Policy Recommendations

Chinese leaders need to enact change on two fronts: institutional and strategic. Institutionally, China should realize that issues like corruption and IPR infringement discourage trade. Steps should be taken to increase local government accountability and transparency, which would simultaneously enhance the central government’s ability to enforce IPR protection.

Perhaps more importantly, I believe Chinese leaders would benefit by broadly re-evaluating the state of their economy in comparison to the rest of the world. China’s economy is strong enough to compete more openly, and a comprehensive reduction in trade barriers would help further develop export sectors. It is true that some industries might be hurt by such a move, but that is due to the fact that many Chinese industries are massively inefficient. Chinese leaders realize this, and have started taking centralized action to address the problem. In August 2010, the national government ordered over 2,000 firms to shut down inefficient factories across the country.\[16\] Of course, allowing the market to determine which firms should be closed would be a more efficient process.

However, this points to a much larger and more difficult problem. Chinese officials, to a certain degree, like having inefficient industry. Ultimately, inefficiencies keep the almost billion-strong Chinese workforce employed. In a country with little to no political room for venting, Chinese leaders value social stability above all and recognize that economic well-being is a centerpiece of such stability. Therefore, it seems unlikely that we will see any drastic changes in Chinese protectionism for inefficient industries without significant political reforms, reforms which are not seriously on the table for consideration.

\[16\] “China orders 2,000 firms to shut overcapacity by end-Sept”
Appendix: Further Graphs and Charts

Appendix A: Chinese Trade 1970-1990 (billions RMB, 2005 index)
source: *Penn World Tables 6.3, National Account Data*

Appendix B: Chinese Trading Partners (2009, billions USD)
Appendix C: Chinese GDP per Capita (1952-2007), in 2005 International Dollars

source: Penn World Tables 6.3
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