

TO: Wu Yi, Minister of Foreign Trade and Economic Cooperation

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RE: Domestic Concerns and China's Accession to the World Trade Organization

### **Executive Summary**

The People's Republic of China's (PRC) future economic prosperity is tied to World Trade Organization (WTO) accession. However, internal agencies representing industrial sectors have made accession difficult due to the need for domestic consensus for negotiations. To solve this gridlock, I propose that the Ministry of Foreign Trade and Economic Cooperation (MoFTEC) lobby top leadership to reform or consolidate these agencies to reduce the number of interests the MoFTEC needs to accommodate in negotiations. This can be achieved by emphasizing how the overall greater economic growth and increased international legitimacy provided by joining the WTO would help ensure that the Chinese Communist Party (CCP) can remain in power. For the remaining agencies, the MoFTEC should guarantee certain WTO accommodations to protect these agency interests.

### **Background and Context**

Since the beginning of the PRC's economic reforms in the latter half of the twentieth century, trade liberalization through accession to the WTO has been critically important. While progress has been made over the last 14 years, more can be done to increase domestic Chinese government consensus (Yong 2002). This is particularly important due to the well-documented benefits of WTO accession. One study finds that, by 2005, China would have a 3% social welfare increase of about 26.6 billion USD as compared to only a 0.2% social welfare increase of about 1.3 billion USD if China did not join (Anderson 1997).

Recently, political scientist Helen Milner published a book titled *Interests, Institutions, and Information* (1997) which analyzes the impact of domestic politics on foreign policy. Given the complexity of the PRC's bureaucracy, using the model proposed by this book to analyze domestic agency-level support for China's accession to the WTO enables us to better understand and advance the goal of accession. Milner (1997) claims that policy coordination is determined by political institutions, domestic self-interest, and information availability. She further suggests that foreign policy decisions result from competition between domestic actors with varying interests in a hierarchical system that she defines as "polyarchy" (Milner 1997, 16). She then argues that a political actor's willingness to cooperate internationally is dependent upon how policy in a foreign country affects the home country as well as how policy benefits the home country (Milner 1997, 47).

The PRC's plan to join the WTO has the MoFETC as the chief negotiator and coordinator (Yong 2002). Given our traditional focus on international trade, we have historically been focused on boosting the overall economic growth of the PRC by reducing protectionism and increasing global integration. However, we do not have jurisdiction over the other agencies that we are working with, meaning that we have to accommodate the interests of protectionist industrial agencies such as the Ministry of Posts and Telecommunications and the Ministry of Machine-Building Industry (Yong 2002). Despite the overall economic benefits of free trade, they view WTO accession as having high negative externalities and low home benefits since free trade will remove subsidies and force competition with foreign firms. Given these differing interests and institutional frameworks, I propose the two following solutions: reforming institutions and placating industrial agency interests.

### **Policy Recommendation Options**

#### ***Reform Institutions and Coordination by Reducing the Number of Industrial Agencies***

Given Milner's (1997) model, a key barrier to the PRC's accession to the WTO has been that the political systems involved in coordinating our accession have been too inefficient due to the large number of self-interested actors that can block action towards meeting WTO accession requirements. However, reducing the number of industry agencies by either merging them or reducing their cabinet rank would decrease the number of actors needed to agree to WTO accession, potentially making the path to consensus clearer (Yong 2002; Olson 1965). The advantages of this approach can be seen in the recent 1988 Canada-US Free Trade Agreement. Due to the US organizing a centralized fast-track negotiating authority with fewer actors, the US negotiations were more efficient than their Canadian counterparts due to the Canadians constantly having to negotiate with different actors during the process while the Americans did not (Delagran 1992).

This would require lobbying top leadership up to and including Premier Zhu Rongji. However, they can be convinced of the necessity of joining the WTO by emphasizing how this will help cement the current government's power. As mentioned before, joining the WTO will lead to substantial economic growth that will increase the CCP's popularity in the public's eye. Additionally, by joining a prominent international organization such as the WTO, the CCP will increase its international legitimacy and deepen ties with countries throughout the globe.

- **Advantages:** As shown by the Canada-US example, reducing the number of actors involved in trade can lead negotiations to be more efficient due to fewer interests needing to be considered (Delagran 1992). This approach would also largely maintain the trade liberalization priorities of the MoFTEC since it would remain as the policy coordinator with either fewer or less powerful agencies making up the rest of the coordination team.

- **Disadvantages:** This proposal is well beyond the power of the MoFTEC and would require convincing China's highest leadership that the benefits of trade liberalization outweigh the costs. Moreover, this proposal is likely to be opposed by the agencies that would either be consolidated or demoted. Many of these agencies represent powerful domestic interests.

***Placate Industrial Agency Interests by Creating an Adjustment Period and Enabling Subsidies***

If we are unable to diminish or remove the influence of industrial agencies, the MoFTEC could placate their interests by insisting upon WTO accommodations such as a transition period with export subsidies (Drabek 1996). Despite our recent rapid growth, the PRC is still largely a developing country where many citizens depend on the employment guaranteed by industrial agencies. The WTO has allowed most developing countries to have a transition period where protections such as export subsidies are slowly rather than abruptly liberalized (Pangestu 2000). This would satisfy the needs of industrial agencies and potentially convince them to support a more efficient WTO accession.

- **Advantages:** As shown by the WTO granting accommodations to most developing countries, these accommodations are also likely to be extended to the PRC. If the accommodations are sufficient, the industrial agencies may agree to WTO accession. If they are not, we could negotiate with the WTO to personalize accommodations due to our domestic politics, which has also been common practice in the past (Pangestu 2000).
- **Disadvantages:** The accommodations required by our industrial agencies may exceed those that the WTO is willing to provide. This is especially important since both the US and the EU are suspicious of the PRC's accession to the WTO due to our rapid economic growth (Yong 2002). This may lead the organization to be more reluctant than usual to accommodate the PRC.

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