

~ Master of Military Studies Requirements for the Degree ~

*United States Marine Corps  
Command and Staff College  
Marine Corps University  
2076 South Street  
Marine Corps Combat Development Command  
Quantico, Virginia 22134-5068*

## MASTER OF MILITARY STUDIES

**TITLE: ECONOMIC INTERDEPENDENCE AND A  
COOPERATIVE CHINA: U. S. POLICY CHOICES**

SUBMITTED IN PARTIAL FULFILLMENT  
OF THE REQUIRMENTS FOR THE DEGREE OF  
MASTER OF MILITARY STUDIES

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**16 APRIL 01  
AY 2000-01**

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## Report Documentation Page

<b>Report Date</b> 2002	<b>Report Type</b> N/A	<b>Dates Covered (from... to)</b> -
<b>Title and Subtitle</b> Economic Interdependence and a Cooperative China: U.S. Policy Choices	<b>Contract Number</b>	
	<b>Grant Number</b>	
	<b>Program Element Number</b>	
<b>Author(s)</b>	<b>Project Number</b>	
	<b>Task Number</b>	
	<b>Work Unit Number</b>	
<b>Performing Organization Name(s) and Address(es)</b> Joint Military Operations Department Navy War College 686 Cushing Road Newport, RI 02841-1207	<b>Performing Organization Report Number</b>	
<b>Sponsoring/Monitoring Agency Name(s) and Address(es)</b>	<b>Sponsor/Monitor's Acronym(s)</b>	
	<b>Sponsor/Monitor's Report Number(s)</b>	
<b>Distribution/Availability Statement</b> Approved for public release, distribution unlimited		
<b>Supplementary Notes</b> The original document contains color images.		
<b>Abstract</b> The purpose of this research is to advance the Economic Interdependence Theory as it relates to China and to Advocate the WTO as a mechanism which will lead to the establishment of the Rule of Law. Incorporating China into the WTO will provide for greater peace and prosperity to the extent China establishes greater legal and administrative transparency. This will be in the interest of both China and the U.S. The paper provides analysis of China's historical background and provides a detailed analysis on how China's interdependence serves to create not just prosperity but hope for more Democratic Institutions. Second, the paper provides analysis of how free trade benefits American jobs, consumers, and the trade balance. Additionally it analyzes current problems and potential future problems as they relate to China. Moreover, it details how the WTO serves as a unique mechanism that can bring about both economic and political reform in China. Finally U.S. policy choices are advanced for consideration.		
<b>Subject Terms</b>		
<b>Report Classification</b> unclassified	<b>Classification of this page</b> unclassified	

<b>Classification of Abstract</b> unclassified	<b>Limitation of Abstract</b> UU
<b>Number of Pages</b> 59	

**REPORT DOCUMENTATION PAGE**

FORM APPROVED - - - OMB NO. 0704-0188

public reporting burden for this collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington headquarters services, directorate for information operations and reports, 1215 Jefferson Davis highway, suite 1204, Arlington, VA 22202-4302, and to the office of management and budget, paperwork reduction project (0704-0188), Washington, dc 20503

1. AGENCY USE ONLY (LEAVE BLANK)	2. REPORT DATE	3. REPORT TYPE AND DATES COVERED <b>STUDENT RESEARCH PAPER</b>
4. TITLE AND SUBTITLE  <b>ECONOMIC INTERDEPENDENCE AND A COOPERATIVE CHINA: U.S. POLICY CHOICES</b>		5. FUNDING NUMBERS  <b>N/A</b>
6. AUTHOR(S)  <b>MAJOR ROBIN ANNE GALLANT UNITED STATES MARINE CORPS</b>		
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES)  <b>USMC COMMAND AND STAFF COLLEGE 3300 RUSSEL ROAD , MCCDC, QUANTICO, VA 22134-5068</b>		8. PERFORMING ORGANIZATION REPORT NUMBER  <b>NONE</b>
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)  <b>SAME AS #7.</b>		10. SPONSORING/MONITORING AGENCY REPORT NUMBER:  <b>NONE</b>
11. SUPPLEMENTARY NOTES  <b>NONE</b>		
12A. DISTRIBUTION/AVAILABILITY STATEMENT  <b>NO RESTRICTIONS</b>	12B. DISTRIBUTION CODE  <b>N/A</b>	
ABSTRACT (MAXIMUM 200 WORDS) <b>THE PURPOSE OF THIS RESEARCH IS TO ADVANCE THE ECONOMIC INTERDEPENDENCE THEORY AS IT RELATES TO CHINA AND TO ADVOCATE THE WTO AS A MECHANISM WHICH WILL LEAD TO THE ESTABLISHMENT OF THE RULE OF LAW. INCORPORATING CHINA INTO THE WTO WILL PROVIDE FOR GREATER PEACE AND PROSPERITY TO THE EXTENT CHINA ESTABLISHES GREATER LEGAL AND ADMINISTRATIVE TRANSPARENCY. THIS WILL BE IN THE INTEREST OF BOTH CHINA AND THE U.S. THE PAPER PROVIDES ANALYSIS OF CHINA'S HISTORICAL BACKGROUND AND PROVIDES A DETAILED ANALYSIS ON HOW CHINA'S INTERDEPENDENCE SERVES TO CREATE NOT JUST PROSPERITY BUT HOPE FOR MORE DEMOCRATIC INSTITUTIONS. SECOND, THE PAPER PROVIDES ANALYSIS OF HOW FREE TRADE BENEFITS AMERICAN JOBS, CONSUMERS, AND THE TRADE BALANCE. ADDITONALY IT ANALYZES CURRENT PROBLEMS AND POTENTIAL FUTURE PROBLEMS AS THEY RELATE TO CHINA. MOREOVER, IT DETAILS HOW THE WTO SERVES AS A UNIQUE MECHANISM THAT CAN BRING ABOUT BOTH ECONOMIC AND POLITICAL REFORM IN CHINA. FINALLY U.S. POLICY CHOICES ARE ADVANCED FOR CONSIDERATION.</b>		
14. SUBJECT TERMS (KEY WORDS ON WHICH TO PERFORM SEARCH)  <b>CHINA &amp; ECONOMIC INTERDEPENDENCE THEORY</b>	15. NUMBER OF PAGES: <b>47</b>	
	16. PRICE CODE: <b>N/A</b>	

17. SECURITY CLASSIFICATION OF REPORT  <b>UNCLASSIFIED</b>	18. SECURITY CLASSIFICATION OF THIS PAGE:  <b>UNCLASSIFIED</b>	19. SECURITY CLASSIFICATION OF ABSTRACT  <b>UNCLASSIFIED</b>	20. LIMITATION OF ABSTRACT
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**Date:** \_\_\_\_\_

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## Executive Summary

**Title:** Economic Interdependence and a Cooperative China: U. S. Policy Choices

**Thesis:** Through pursuit of a more prosperous China, the United States has the potential to shape the China of tomorrow. The WTO will prove to be the mechanism to this end.

**Discussion:** The economic interdependence perspective identifies incentives for states to contain their international disputes when the economic costs of conflict outweigh any potential gains. China has a greater need to increase prosperity within its country than it does to project power, therefore cordial relationships will most likely continue.

Historically, more open trade has benefited American workers and consumers. The past ten years has witnessed less trade restrictions than anytime in history, and through it all, unemployment and inflation have been at record lows. Additionally, the balance of payments, on the whole has shown continued growth in America which has equated to greater prosperity. Furthering free trade with China should continue this trend.

As China has moved towards a more market-oriented economy, it has experienced greater prosperity and freedoms. Unfortunately, with market competition comes corruption and income inequalities which have proven to be formidable obstacles along the road to Chinese reform. Continued progress in China will depend on resolution of the conflict between the economic reforms and that of its political reforms.

The World Trade Organization is a unique mechanism that can bring about both economic and political reform. It can do this through its drive for greater legal and administrative transparency. Encouraging China to become part of the WTO rather than shutting them out seems a far safer wager for global peace and prosperity and would be in the best interest for the U.S. to pursue. Bottom line is China needs to maintain peace to sustain its economic growth which is a sure-fire way of furthering itself along the road of great power status.

**Recommendation:** Trade must not be impeded with China. Instead of implementing trade sanctions, the US needs to move towards adding positive incentives to help induce behavioral improvements. Moreover, Americans need to understand the benefits to both the consumers and the American job market that increased trade to China will further. Rather than promoting democracy, the United States should promote prosperity. As countries become more prosperous, their citizens demand more freedoms and from this democracy can emerge. Now, while China has more at stake than the United States, is the best time possible for America to shape the China of tomorrow. Greater legal transparency and enforcement mechanisms in China's should be America's number one priority. The focus should be on the fundamental problem which causes human rights violations and environmental problems. Instead of promoting democracy, the US should help build and extend civil society through markets.

## *Preface*

An historical analysis of the interaction between economics and global power, thoroughly analyzed in *The Rise and Fall of the Great Powers* by Paul Kennedy, coupled with present day realities of a rising China and a relative decline in the United States economy prompted my search for the direction U.S. policy should pursue to ensure U.S. national interests remain secure.

I have a number of people that assisted me in my work. First I would like to thank Pat Lane from the MCU Research Center who spent many hours assisting me in research. Additionally, I would like to thank Maj Yau Choon Ang from Singapore for allowing me to share ideas with him and enter into lengthy discussions and Colonel (retired) Michael J. Flynn III for his assistance in obtaining articles on China. Without the assistance of LtCol Michael M. Weber all plurals would have remained possessives. Without the knowledge, guidance, and organizational skills of Dr Janeen M. Klinger, this document would have remained disorganized thoughts left unwritten. Finally I would like to thank my husband and children for their patience while I disassociated myself from them for the past six months.

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## I. INTRODUCTION

From a poor, third world country ruled by a repressive regime to an economic and democratic power house that rivals the per capita income of the United States, Taiwan proves that Asian societies can assume democratic principles along the way to economic prosperity. Scholarly works on China's developmental potential vary tremendously. Some, such as Segal, describe China as a perpetual second-rank middle power, home to a fifth of mankind, overrated as a market, a power, and a source of ideas; a country that should be restrained as much as it should be engaged through a policy he describes as constraint.<sup>1</sup> While others, such as Papayoanou and Kastner, characterize China as a substantial and increasing military and economic power, and as such, requires the United States to pursue a policy of engagement.<sup>2</sup> Whether viewed as benign or malign, China's politico-economic system and outward-oriented developmental strategy are changing and will most likely continue to change well into the 21<sup>st</sup> century.<sup>3</sup>

### A. China in Historical Perspective

Prior to 1850, China and India were the largest economies in the world.<sup>4</sup> The surrounding countries viewed China as the center of the universe and as such copied their culture, accepted their Confucian philosophy, and paid them tribute.<sup>5</sup> After 1850, however, the humiliation of western imposed colonial rule and the loss of extensive territory during the Russo-

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<sup>1</sup> Gerald Segal, "Does China Really Matter", *Foreign Affairs*, September/October 1999, pp 24 and 35 His constraint policy is a cross between restraint and engagement

<sup>2</sup> Paul A Papayoanou and Scott L. Kastner, "Sleeping With the (Potential) Enemy: Assessing the U.S. Policy of Engagement with China", *Security Studies*, Vol9 #12, Autumn-Winter 1999,2000, p 157

<sup>3</sup> Denney Roy, "China's Post-Deng Foreign Relations", *International Journal*, Winter 1997-98, p 135

<sup>4</sup> Robert Gilpin, *The Challenge of the World Global Economy: Capitalism in the 21<sup>st</sup> Century*, p36

Japanese war struck a blow to Chinese national pride. In the eyes of the West, “China must not be allowed to modernize too far or acquire the strength to repel the West,” rather a weak and dependent China was thought to best serve the interests of the West.<sup>6</sup> This subjugation of China, whether intentional or not, becomes glaringly obvious when comparing economic performance between Western Europe and China. In 1820 GDP per capita for the West was \$1,034 to China’s \$500. Right before the Communist takeover this gap widened to \$4,902 for the West to a paltry \$454 for China. By the time the revolution started, China was one of the poorest countries in the world with an average life expectancy of only 36 years compared to 72 years for the West.<sup>7</sup>

**Mao Zedong**. The unification of China under the Kuomintang stirred hopes of national pride only to be dashed by renewed Japanese imperialism during which the Chinese people were subjected to many atrocities. As a result, a revolutionary movement, led by Mao Zedong, succeeded in over-throwing, but not completely defeating, the Kuomintang government. Mao quickly established legitimacy. Both successes, illustrated by such things as industrialization, the Korean War, development of nuclear capabilities, and failures evidenced by the Great Leap Forward and the Cultural Revolution,<sup>8</sup> have marked Mao’s rule; yet through it all, his regime remained intact.<sup>9</sup>

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<sup>5</sup> June Grasso et al, *Modernization and Revolution in China*, M. E. Sharpe Inc., 1997 This book provides a detailed account of China's history pre-modern history in the context of understanding contemporary China.

<sup>6</sup> Lu Aiguo, *China and the Global Economy since 1840*, St Martin’s Press, Inc., 2000, p 66

<sup>7</sup> Ibid, pp 57 and 67 Whether China was economically repressed by the West or whether it was endemic to China itself is an argument outside the scope of this paper, although the evidence I gathered points to a combination of both.

<sup>8</sup> For further study on these two events refer to Zhang’s *Transforming China*, and Aiguo’s *China and the Global Economy Since 1840*. For a detailed read on China’s past read Aiguo’s *China and the Global Economy Since 1840*

<sup>9</sup> Although Mao and Deng did purge their ranks and it was predicted that Deng’s succession would occur only after a serious power struggle (for prediction,

Mao symbolized communism in the eyes of America. Mao's national strategy during the period he called the New Democracy emphasized restoration and development of economic relationships with the West, and he believed that America would be receptive towards greater trade and openness with China. However, by 1950, the spread of communism came to be viewed as a grave national threat in the United States. China's participation in the Korean War further threatened American security interests and, as a result, the United States severed all economic and political ties to China. The ensuing embargo ultimately had minimal effect because the China of the 1950s was so poor that they could exploit a track to self-sufficiency and not depend on world trade.

**Deng Xiaoping**. Although Mao diplomatically opened the doors to the West in the early 1970s, it was Deng Xiaoping, who ushered in significant economic reforms under his "Four Modernization Program" which emphasized agriculture, industry, science and technology, and national defense. Deng's main goal was to fend off poverty in order to advance socialism and his modus operandi was to "seek truth from facts."<sup>10</sup> He put this philosophy into action through a reform process that was very succinctly described by Zhang as dynamic gradualism.<sup>11</sup> Deng commented, "After having taken a step, we must review what we have done to find out what needs to be speeded up, what needs to be slowed down and what needs to be contracted. This is the way we have to proceed; we must not rush headlong into things."<sup>12</sup>

Deng stated that egalitarianism would not work in the early stages of development. He further remarked that he did not accept that there is a direct connection between multi-party democracy and China's most pressing goal of rapid and efficient development. Rather, Deng

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refer to *Research Institute for Peace and Security, Asian Security 1995-1996*, Brassey's, Virginia, 1995 p 79)

<sup>10</sup> Michael Twohey, *Authority and Welfare in China: Modern Debates in Historical Perspective*, St Martin's Press, Inc., NY, 1999, p 99

<sup>11</sup> Wei Wei Zhang, *Transforming China*, St Martin's Press, Inc., 2000, p 46

believed that multi-party systems would simply divert the people's attention away from developmental goals. On another occasion he declared that although democracy was China's goal, keeping the country stable must take priority because this would ensure a more lasting and substantive democracy in the future.<sup>13</sup> However, he stated that the form of democracy would not be a Western bourgeois form of democracy; rather, it would be a socialist democracy. As a result, with the exception of the 1989 Tiananmen Square incident, China's government has not been subjected to a major crisis.<sup>14</sup> For now, the average Chinese views prosperity and stability as higher priorities than freedom and democracy and the future of China may hold more enduring democratic systems with fewer political and economic traumas on the road to that goal.<sup>15</sup>

## **B. Analysis**

History suggests that trade embargos are relatively unsuccessful. Since 1970 economic sanctions imposed by the United States have failed to work in 87 percent of the cases in which they have been tried.<sup>16</sup> Moreover, China has used the threat of embargoes as a means of restricting U.S. business in China. This became clear when Li Peng announced that China would buy \$1.5B worth of aircraft from Airbus Industrie rather than Boeing because, "...the Europeans did not attach political strings to cooperation with China, unlike the Americans who arbitrarily

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<sup>12</sup> Wei Wei Zhang, *Transforming China*, St Martin's Press, Inc., 2000, p 47

<sup>13</sup> Michael Twohey, *Authority and Welfare in China: Modern Debates in Historical Perspective*, St Martin's Press, Inc., NY, 1999, pp 104-107, 151  
These ideas are also discussed in Roy, "Post Deng China", *International Journal*, p138

<sup>14</sup> ...although civil unrest has been a problem as will be detailed in section IV. Additionally, the failure of the radical transition to democracy in Eastern Europe and Russia to bring about economic reform is in sharp contrast to the success China enjoys under a government that has gradually evolved from an autocratic communist dictatorship to an oligarchical nationalist statism and gives even greater credence to Mao's gradualist theory of growth and change.

<sup>15</sup> Michael Twohey, *Authority and Welfare in China: Modern Debates in Historical Perspective*, St Martin's Press, Inc., NY, 1999, pp149-150

resort to the threat of sanctions or the use of sanctions.”<sup>17</sup> Trade restrictions with China would simply prove fruitless and act as a reminder to China of the humiliation of their past.

Furthermore, America’s unwillingness to work with China after Mao’s successful revolution may have simply deepened his ideological fanaticism.<sup>18</sup> This disengagement ultimately resulted in what Aiguo details as China’s de-linking from the rest of the world and their determined effort to self-reliance thus ensuring China would never again be dependent on outside sources.<sup>19</sup>

Clearly, this is not a course America or her allies want to see repeated.

With over 40% of the Chinese economy linked to the international market, China’s leadership believes that joining in on globalization is imperative to ensure continued economic progress. China’s economy depends heavily on both export trade and foreign direct investment. As such, China’s WTO entry could be key to determining future relations with the United States. The United States plays a critical role in China’s development as emphasized in the People’s Daily which stated the importance of “...developing amity and cooperation with developed countries in the West, including the United States.”<sup>20</sup>

### C. Scope of This Paper

We have narrowed the scope of this paper to three factors. First, although there are a number of theoretical models with the potential to apply to China, this paper will attempt to emphasize

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<sup>16</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb010/pb10.htm>, Policy Brief No 10, Nov 1996

<sup>17</sup> Aaron L. Friedberg, “The Struggle for Mastery in Asia”, *Commentary*, Vol 110, No 4, Nov 2000, p 19

<sup>18</sup> Michael Twohey, *Authority and Welfare in China: Modern Debates in Historical Perspective*, St Martin’s Press, Inc., NY, 1999, p 94 (This unwillingness to work with Mao grew from the assumptions of Sino-Soviet collusion.)

<sup>19</sup> Lu Aiguo, *China and the Global Economy since 1840*, St Martin’s Press, Inc., 2000, p 71 (Aiguo provides a very detailed account of Mao’s reign of delinking and self-reliance. Also Twohey (p 79-96) delves into the theoretical basis of Mao’s efforts.)

<sup>20</sup> Joseph Fewsmith, “The Politics of China’s Accession to the WTO”, *Current History*, Sept 2000, pp269 and 271

the dominance of the economic interdependence theory. Second, China's economic growth will continue; however, there will be unintended consequences of this growth. For example corruption and political instability in China will impact the policy choices that United States pursues. Third, the new administration will continue to "engage" China although that engagement appears to be predicated on China as a strategic competitor rather than a strategic partner.

The next section highlights how economic interdependence will shape the relationship between the United States and China. Section III reviews why trade serves America's self-interest. It analyzes how the benefits America receives from open trade with China should outweigh the costs. Section IV analyzes issues in China to determine how trade with China may support U.S national security objectives. It examines China's track to capitalism and the pitfalls that may hinder future reform efforts. Section V examines the costs and benefits of Chinese WTO membership to both the U.S. and China. Evidence suggests that the international trade arena can play a significant role in moving China towards cooperative co-existence with the rest of the world. The conclusion summarizes a list of policy objectives for the United States based on the analysis provided.

## II. ECONOMIC INTERDEPENDENCE THEORY<sup>21</sup>

### A. The Perspective

The economic interdependence perspective identifies incentives for states to contain their international disputes when the economic costs of conflict outweigh any potential gains.<sup>22</sup> This perspective has clear applicability to China. China unmistakably benefits from economic integration and therefore has an economic stake in the existing international system.<sup>23</sup> In 1977 China's trade totaled \$15B. By 1997, its trade exceeded \$325B and its growth rates averaged 9% for nearly 20 years.<sup>24</sup> Moreover, per-capita incomes increased from \$350 per capita in 1986

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<sup>21</sup> Avery Goldstein, "Great Expectations: Interpreting China's Arrival", *International Security*, Vol 22 No 3, Winter 1997/1998, pp 36-73 Goldstein advances five theoretical perspectives which he ascribes to China in his article. The economic interdependence theory is elaborated above. The other four are the power perspective, flawed regime perspective, nuclear peace perspective, and institutional perspective theories. The Power perspective theorizes two possible scenarios that will lead to conflict. The first is that hegemonic instability will ensue as China rises in power. The United States, the current hegemon, will feel threatened and result in an American effort to subordinate China in the global arena to maintain American superiority. The balance of power theory postulates that China's rise will trigger an arms buildup in the area with the other Asian states who will then develop tighter alliances against China. The two theories that emanate from the flawed regime perspective are the democratic peace theory and the democratic transition theory. The democratic peace theory argues that the domestic institutions and political values of liberal democracies ensure peace among them, but this case fails to hold up between liberal democracies and non-democracies. The second theory is the democratic transition theory and suggests shifts from authoritarianism to democracy have competitors for leadership which adopt aggressive foreign policies that garner popular support by tapping into nationalist sentiments and elite support by placating the institutional remnants of authoritarian rule, especially the military. The nuclear peace perspective theory asserts that the advent of nuclear weapons have revolutionized international politics by altering the costs of conflict among the great powers. The institutional perspective argues that formal and informal organizational practices might mitigate the effects of anarchy, dampen conflict and enhance the prospects for cooperation. This last theory is closely linked to the economic interdependence theory and will be used to further support the later.

<sup>22</sup> Avery Goldstein, "Great Expectations: Interpreting China's Arrival", *International Security*, Vol 22 No 3, Winter 1997/1998, pp 69-70

<sup>23</sup> Ted G. Carpenter and James A. Dorn, *China's future: Constructive Partner or Emerging Threat*, Cato Institute, 2000, p143. He contrasts China with Russia who maintained ideology and non-market economy to right up before the fall.

<sup>24</sup> Papayouanou and Kastner, "Sleeping with the (Potential)Enemy:

to \$3,800 per capita in 2000.<sup>25</sup> Even more striking, foreign direct investment (FDI) went from \$1B in 1983 to over \$42B by 1996 and accounted for over 41% of China's total exports.<sup>26</sup> Each of the above demonstrates China's dependence on integrating into the world economy. Even more telling is the relationship in trade with the United States. While China's trade to the United States was 22.9% of total trade and 9.5% of GDP, US trade to China was merely 4.6% of total trade and 0.9% of GDP.<sup>27</sup> The aforementioned statistics clearly shows China's deeper dependence on trade than that of the United States. China's relationship with the industrialized and newly industrialized countries is essential to its continued growth.

## **B. An Economic Model**

Not only is China currently benefiting but, by all accounts, should continue to prosper through integration in the world market thereby furthering the benefits both they and the U.S. obtain. McKibbin and Tang used a global model to highlight the benefits of China's integration into the world economy and their lifting of existing barriers. The results of their test revealed that in the short run, tariff reductions led to an initial decline in GDP because of restructuring of inefficient firms. In the medium and long run, however, China experienced a substantial benefit to GDP and to a lesser degree, GNP.<sup>28</sup> As a result, China became more alluring to world

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Assessing the U.S. Policy of Engagement with China", *Security Studies* Vol 9 No1/2 Autumn 1999-Winter 2000 p 172

<sup>25</sup> Library of Congress, China: A Country Study

<http://lcweb2.loc.gov/frd/cs/cntoc.html> provided per capita data for 1986 and Central Intelligence Agency, The World Fact Book: China, <http://www.cia.gov/cia/publications/factbook/geos/ch.html> provided per capita data for 2000

<sup>26</sup> Paul A. Papayoanou, and Scott L. Kastner, "Sleeping with the (Potential)Enemy: Assessing the U.S. Policy of Engagement with China", *Security Studies*, Vol 9 No1/2 Autumn 1999-Winter 2000, p 174

<sup>27</sup> Paul A. Papayoanou, and Scott L. Kastner, "Sleeping with the (Potential)Enemy: Assessing the U.S. Policy of Engagement with China", *Security Studies* Vol 9 No 1/2 Autumn 1999-Winter 2000, p 185

<sup>28</sup> GDP is gross domestic product and reflects the total final output of goods and services produced by a countries economy. GNP is gross national product and is the total domestic and foreign output claimed by residents of a

investors who saw investment potential in China. The more foreigners invested the greater the increase in China's capital stock which resulted in permanent positive change to the structure of China's economy. As the capital account went up, the current account went down which meant they imported more and exported less.<sup>29</sup> The rest of the world also benefited from trade with China but in the different balance of trade accounts. The rest of the world viewed investment opportunities in China as more attractive; therefore, the rest of the world increased their capital outflows to China to take advantage of more lucrative investment opportunities. Since this resulted in appreciation of China's currency, China's goods became more expensive thereby decreasing the amount of goods the rest of the world imported from China and increasing their exports to China and to the rest of the world. The bottom line is global consumption increased and global production increased permanently leading to a benefit for all as classical trade theory suggests.

### C. Economic Interdependence and International Organizations

Some scholars believe past Chinese actions prevent it from effectively entering into multilateral agreements. They contend that China's preference for bilateral, rather than multilateral agreements diminishes their prospects for effective regional institutions. This assertion seems to be confirmed by recent events in Beijing where the Chinese government rejected a recent proposal by US defense Secretary William Cohen that China take part in joint military exercises by Asia-Pacific countries. Chinese Foreign Ministry spokesman Sun Yuxi told a press conference, "Strengthening military alliances and engaging in joint military exercises are not conducive to promoting peace and stability in the Asia-Pacific region." The offer by Cohen was

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country. It comprises GDP plus incomes accruing to residents abroad less the income of foreigners within China.

<sup>29</sup> Warwick J. McKibbin, and K. K. Tang, "Trade and Financial Reform in China: Impacts on the World Economy", *The World Economy*, vol 23, No 8, August 2000, p 992-999

with the intent of building stability in Asia which currently lacks a multilateral security arrangement similar to that of NATO.<sup>30</sup>

However, the preceding analysis fails to take into consideration other methods of multilateral cooperation that China and the region are pursuing – many of them in the economic realm. China has the honor of being one of only five permanent members of the UN Security Council. China was applauded internationally, especially by the United States, for maintaining valuation on its currency during the Asian economic crisis.<sup>31</sup> Madeline Albright praised China for holding its exchange rate constant in the face of massive devaluations of other Asian currencies.<sup>32</sup> China's exchange rate has become a symbol of China's commitment to global economic stability and Asia's recovery from its economic crisis. The Association of South East Asian Nations (ASEAN), initially created to counter a Chinese threat,<sup>33</sup> is working with China to develop an ASEAN-China regional code of conduct in the South China Sea. Once adopted, this code of conduct could help build up trust, enhance cooperation, and reduce tensions in the Spratly/South China Sea area. The Treaty of Amity and Cooperation, created by ASEAN, espouses mutual respect for sovereignty, noninterference in internal affairs, peaceful settlement of intra-regional disputes and effective cooperation. In regards to trade, ASEAN exports to China increased over 102.5% from 1993-1996 and Chinese exports to ASEAN countries

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<sup>30</sup> Nicholas R. Lardy, <http://afpc.org/crm/crm334.htm>, *China Reform Monitor* No. 334 September 25, 2000 American Foreign Policy Council, Washington, D.C., "Beijing rejects SecDef Cohen's call for joint military exercises; China strengthens ties with Taliban, Syria, Russia, Cambodia" (Interesting statement fro Yuxi considering China's deterrence capabilities directed against its neighbors, in particular Taiwan and Japan. Refer to Thomas J. Christensen, "Chinese Realpolitik", *Foreign Affairs*, Vol 75 #5, Sept/Oct 96, p 43

<sup>31</sup> Aaron L. Friedberg, "The Struggle for Mastery in Asia", *Commentary*, Vol 110, No 4, November 2000 p 20

<sup>32</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb047/pb47.htm>, Policy brief #47, April 1999

<sup>33</sup> Larry M. Wortzel, "Three New Looks at China", *Parameters*, Winter 2000-01, p 143

increased 14.4% from 1995 to 1996 making ASEAN China's seventh largest market<sup>34</sup> and thereby showing Chinese willingness to work multi-laterally. Furthermore, pursuing an Asian NATO myopically looks to a military alliance as the sole effective way to build peace. NATO was a military alliance built after a World War and because of the threat of Soviet expansion into Europe. Informal economic and security alliances are developing in Asia to secure prosperity and develop a more robust economy for all Asians. Frankly, without a military threat, a creation of an "Asian NATO" may do more harm than good.

China has displayed relatively solid international cooperation and responsibility. In addition to regional agreements, China is a part of many multinational organizations to include Asian Pacific Economic Co-operation Forum (APEC), Economic and Social Commission for Asia and the Pacific (ESCAP), United Nations (UN), International Atomic Energy Association (IAEA), World Intellectual Property Organization (WIPO), and International Fund for Agricultural Development (IFAD).<sup>35</sup> Moreover, China refused to block UN actions, most recently for the deployment of UN peacekeepers in East Timor. China also peacefully incorporated both Hong Kong and Macao in keeping with the promised one China, two system concept. Additionally, as already noted, China maintained restraint during the Asian financial crisis. China also displayed cooperation through its desire to join regional trade organizations and through its 13-year drive to join the WTO. All of the above demonstrate China's desire to become a responsible part of the global community. Although it would be naïve to think

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<sup>34</sup> <http://www.asean.or.id> after Japan, the US, Hong Kong, Germany, Republic of Korea and Taiwan

<sup>35</sup> <http://www.cia.gov/cia/publications/factbook/geos/ch.html>, other multinational organizations include: AfDB, APEC, AsDB, BIS, CCC, CDB (non-regional), ESCAP, FAO, G-77, IAEA, IBRD, ICAO, ICC, ICFTU, ICRM, IDA, IFAD, IFC, IFRCS, IHO, ILO, IMF, IMO, Inmarsat, Intelsat, Interpol, IOC, ISO, ITU, LAIA (observer), MINURSO, NAM (observer), OPCW, PCA, UN, UN Security Council,

participation in these institutions will solve all security issues, it is safe to say that China's participation will keep them engaged with the rest of the world inclining them to become more globally responsible. Moreover, incorporating China into the World Trade Organization provides another mechanism to foster international cooperation and economic interdependence. China's accession to the WTO and the regularization of normal trade relations between the United States and China as well as inclusion into the G-8 would be a significant step in the gradual integration of China into the world economy. Each of these would pacify China's quest for status while also enhancing its stake in the emerging global system.<sup>36</sup> Brezezinski says it best when he states that China is too big to be ignored, too old to be slighted, too weak to be appeased, and too ambitious to be taken for granted.<sup>37</sup>

#### **D. Economic Prosperity and the Potential for Democracy**

Since China successfully pursued dynamic gradualism on its course to economic prosperity, why would they not be successful in pursuing this same strategy in the political arena? As mentioned earlier, China already started to evolve from an authoritarian to an oligarchical rule. Jiang Zemin does not have the same hold over the Chinese that Mao and Deng held. Moreover, China's citizens place stability and prosperity as higher priorities than democracy and individual rights. However, in the next 10-20 years, China will most likely witness increasing tensions between its inflexible political system and its dynamic economic system. Party legitimacy has been degraded over the past 50 years. From the Cultural Revolution and Great Leap Forward, to The Tienamen Square incident to the current peasant

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UNAMSIL, UNCTAD, UNESCO, UNHCR, UNIDO, UNIKOM, UNITAR, UNTSO, UNU, UPU, WHO, WIPO, WMO, WTOO, WTrO (applicant), ZC

<sup>36</sup> Zbigniew Brzezinski, "Living With China", *The National Interest*, No 59 Spring 2000, p 19

<sup>37</sup> Zbigniew Brzezinski, "Living With China", *The National Interest*, No 59 Spring 2000, p 7

uprisings over corruption, the CCP has taken a number of blows to its legitimacy.<sup>38</sup>

Additionally, China's rising middle class seeks increasingly more individualism. While the CCP subordinates the individual to the state, the rising "meritocracy cadre" is growing in China. Santoro provides two examples of young Chinese citizens who are advancing up the ranks in Western companies based on performance rather than Communist Party connections.<sup>39</sup> As this process continues so will further need to reform political institutions.

As societies grow wealthier, their citizens tend to demand greater civil and political liberties.<sup>40</sup> According to some theorists, democracy occurs soon after a country's population reaches an annual per capita income level of \$5K to \$7K.<sup>41</sup> China's per capita income has increased to \$3.8K (1999 estimated PPP)<sup>42</sup> and is on its way to supporting more democratic institutions such as the village level elections which are already being conducted in China.<sup>43</sup> Both South Korea and more recently Taiwan provide excellent examples of two Asian countries which have already successfully shifted to democracy. Incorporating China into the global trade environment will provide the prosperity and the incentive, perhaps a very strong incentive, for its people to move towards a more democratic course.

Papayouanou advances that economic ties have a tendency to influence non-democratic governments to pursue more cooperative foreign policies based on how much influence

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<sup>38</sup> Jasper Becker, "Anger at Dam Corruption Growing", *Hong Kong South China Morning Post*, 29 September 00 translated by FBIS and Weiguo, Yu, "In Developing the Western Region, We Should Give No Opportunity for Corrupt Officials to Exploit", *Beijing Renmin Ribao*, 23 Sept 00, translated by FBIS

<sup>39</sup> Michael A. Santoro, "Global Capitalism and the Road to Chinese Democracy", *Current History*, Sept 2000, p 264

<sup>40</sup> Denney Roy, "China's Post-Deng Foreign Relations", *International Journal*, Winter 1997-98, p 138

<sup>41</sup> Denney Roy, "China's post-Deng Foreign Relations", *International Journal*, Winter 1997-98, p 139 This is also advanced by Michael A. Santoro, "Global Capitalism and the Road to Chinese Democracy", *Current History*, September 2000, p 264

internationalist economic interests have in the regime. He further suggests that if the dominant political coalition is comprised of groups with internationalist economic interests or if the leadership is autonomous yet committed to internationalization, the cultivation of economic ties should have positive effects.<sup>44</sup> Although there are a number of other variables that could influence China's foreign policy objective, one can strongly argue that economics will have a significant taming impact.

#### **E. Analysis.**

“To be a Great Power – by definition, a state capable of holding its own against any other nation – demands a flourishing economic base.”<sup>45</sup> This statement can be supported with the Chinese example because they place economic growth ahead of defense buildup. As such, cordial relationships will most likely continue with other countries and conflict averted as the latter will draw economic commitment away from the other three legs of the modernization program – agriculture, industry, and science and technology. Additionally, as per-capita income increases in China so also will the drive for greater individual freedom. The desire for greater freedom was silenced during the Tiananmen Square massacre; however, less traumatic uprisings are continuing. Until China resolves its imbalance between economic and political reform, its progress towards greater economic potential will most likely be thwarted. China knows that economic engagement is imperative if it wants to advance economically. China also realizes that engagement means less political control which places the regime in a quandary. As it engages,

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<sup>42</sup> Purchasing Power Parity (PPP) measures how much goods and services can be purchased with the recorded income per capita of different countries depending on the relative prices of similar products.

<sup>43</sup> Jimmy Carter Center

<sup>44</sup> Paul A. Papayoanou, and Scott L. Kastner, "Sleeping with the (Potential) Enemy: Assessing the U.S. Policy of Engagement with China", *Security Studies* Vol 9 #12, Autumn-Winter 1999, 2000

<sup>45</sup> Paul Kennedy, *The Rise and Fall of the Great Powers*, Vintage Books, 1989, p 539

its citizenry will be exposed to outside influences which will likely continue to reduce the legitimacy of the Communist party. The current regime may be forced to execute another Tiananmen or encourage political change commensurate with economic change and the will of its people.

### III. COSTS AND BENEFITS - AMERICA

China's integration into the world economy is becoming a matter of fact. First, it is the second largest economy in the world with a GDP of \$4.8T, and an 11.1% share of world trade, topped only by the United States who has 20.7%.<sup>46</sup> Second, it is the eleventh largest exporter and fourteenth largest importer of goods and services as of 1996. Third, it accounts for 40% of FDI, second only to the United States. Fourth, it is the 8<sup>th</sup> largest source of capital in the world and the largest source of capital out of all developing countries.<sup>47</sup> Fifth, China is an economic partner to the U.S with bilateral trade amounting to \$62.6B in imports to the US and \$12.9M in exports from the US, making China the fourth largest trading partner to the U.S.<sup>48</sup> Moreover, the Asian Pacific region as a whole accounts for \$535B or 33% of total US merchandise exports and imports in 1998.<sup>49</sup> Imagine the benefits both countries would accrue if tariff and non-tariff barriers were lifted? The case for China is important because its success or failure will significantly affect the Asian Pacific region which will impact on the United States. No one country, including the U.S., dominates the Asian market and, like it or not, U.S. continued prosperity relies on continued trade with Asia.

#### A. Jobs

Popular sentiment maintains that opening markets with China means a loss of jobs. The fear is that the cheaper labor afforded by China will mean a mass exodus of industry from the U.S. to China. In one sense this is true; however, free trade does not mean a loss of jobs for

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<sup>46</sup> <http://www.cia.gov/cia/publications/factbook/geos/ch.html>

<sup>47</sup> Warwick J. McKibbin and K. K. Tang, "Trade and Financial Reform in China: Impacts on the World Economy" *The World Economy*, Vol 23, No 8 p 980

<sup>48</sup> Zbigniew Brezinski,, "Living With China", *The National Interest*, No 59 Spring 2000, p 9

<sup>49</sup>

Americans. It does, however, mean a different composition of the jobs offered.<sup>50</sup> As markets open, the global economy has experienced shifts in jobs not unlike that experienced many times before. The United States has encountered two major types of job shifts. Location displacement shifts occurred in the textile industry during the mid to late 1800s. As the North Eastern states industrialized, labor intensive industries, such as textiles, moved to the Southern United States because it was no longer economical or efficient for the North to produce clothing. Workers in the North had two choices, they could move to where the industry relocated or they could move to another economic sector. The other type of shift took the form of industry obsolescence. An example of this is the development of the automobile which replaced the horse and buggy. The second shift resulted in a complete disillusionment of an industrial sector and opened up a whole new economic sector which required higher education levels, more technical training, and higher levels of capitalization. As a result, the United States advanced a notch on the developmental ladder.

Roberts provided an excellent example of the vitality of the economy by pointing out that in 1900 over 40% of the 26M employed in the US were in the agricultural sector. In just under 100 years, this percentage dropped to about 2%. As farmers became more efficient, they were able to produce more with less.<sup>51</sup> As a result, other jobs were created and displaced workers filled these new positions. The same holds true for the US today in the context of global trade. Although in a micro-economic sense workers will be affected, this displacement, on the whole, will be temporary, and other jobs will be created which will further enrich the country and the world.

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<sup>50</sup> Russel Roberts, "Speaking About Trade to the Open-Minded Skeptic", *Cato Journal*, Vol 19 No 3 p443

<sup>51</sup> Russel Roberts, "Speaking About Trade to the Open-Minded Skeptic", *Cato Journal*, Vol 19 No 3 p443

Technological innovation lies at the heart of economic shifts described above and is the process of linking knowledge and training with production. From labor intensive to capital/energy intensive to technology intensive, technology has linked each phase of movement and each phase of innovation entailed job creation and loss.<sup>52</sup> In fact, most evidence points to the creation of new technologies rather than the opening of markets with labor intensive countries such as China, to be the main culprit in low-skilled job losses in this country.<sup>53</sup> Moreover, the United States, unlike most other countries, has the ability to train and educate its workforce to assimilate more advanced technology and higher wage jobs. Therefore, because Americans are fairly well educated relative to citizens of other countries, the impact on job displacement is short-lived.

U.S. firms have had considerable success increasing sales to China. Most U.S. exports to China are high value-added goods, such as aircraft and computers, produced in industries that pay American workers above-average wages.<sup>54</sup> In contrast, China produces low technology good that are labor intensive. For these reasons, the US should reject protectionism since it locks in inefficiencies and increases costs to the global economy as a whole.<sup>55</sup> Had the United States government protected the horse and buggy industry at the expense of the automobile industry where would they be today?

The bottom line is reflected in the unemployment rate of the United States. Throughout the 1980s and 1990s, the United States has progressively moved towards greater freedom of trade with the global economy by lifting tariff and non-tariff barriers. Through it all, the

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<sup>52</sup> James H. Mittelman, *The Globalization Syndrome*, Princeton University Press, New Jersey, 2000, p 61

<sup>53</sup> Dick Clark, *International Trade and the U.S. Economy*, The Aspen Institute, Washington, D.C., 1995 p 13

<sup>54</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb047/pb47.htm>, Policy brief #47, April 1999

unemployment rate has decreased and is currently at a record low of 4%. Although other factors such as stable monetary and fiscal policies have played an integral part, lifting trade barriers has not been detrimental to American well being and has actually benefited national and international security through focus on global prosperity – working towards increasing the “haves” and decreasing the “have-nots”. Therefore, removing tariff barriers increases competition in an economy and the only countries that have something to fear from open trade are those that can not compete.

## **B. Consumers**

Politicians and policy makers, especially for local and state government, are concerned about jobs because unemployed or potentially unemployed workers vote. We are concerned about jobs because it is through them that we are compensated. In turn, this compensation is returned back to the market place in exchange for goods and services. When trade is opened, competition drives costs down and quality up resulting in the best possible product at the lowest feasible cost for the consumer.<sup>56</sup> An example of this would be the car industry of the 1980s. Japanese auto imports flooded the market with lower prices and better quality than that of U.S. automakers. In response, the American car industry asked Congress to protect their interests through tariffs and quota’s on Japanese imports. Congress passed such legislation, but then Japanese automakers slashed prices and creatively worked around these protectionist measures. Regardless, American consumers still preferred Japanese cars over American because they were a cheaper, better quality vehicle. The American car industry evaluated the experience and streamlined to improve the quality of their vehicles, and regained consumer confidence. As a

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<sup>55</sup> Dick Clark, *International Trade and the U.S. Economy*, The Aspen Institute, Washington, DC 1995

<sup>56</sup> Brink Lindsey, “Free Trade From the Bottom Up”, *The Cato Journal*, Vol 19, No 3, p 360

result, the American consumer was the ultimate winner; they profited from free trade through greater consumption gains. Although this logic holds up to any criticism, it is normally not the majority who are happy that have the loudest voice, but rather the more visible minority, those unemployed, that have the loudest voice. Sadly, this results in leaders more often than not opting for less efficiencies and higher prices to serve the interest of their more vocal constituencies.

The office of Special Trade Representative estimates that existing WTO agreements add about \$3K to the purchasing power of the average four-person household each year.<sup>57</sup> Although this meant greater freedom of trade, it did not necessarily result in American job displacement. The sneaker industry provides a perfect example. Beginning in the mid-1980s, Nike increasingly shifted production of athletic shoes from Korea and other Asian locations to China where labor was relatively cheaper. U.S. consumers reaped the benefit of lower-priced goods produced in China, where costs are lower than in other Asian locations. Moreover, the job losses associated with rising Chinese exports of footwear, as well as several other important products, primarily occurred elsewhere in Asia, not in the United States.<sup>58</sup> Therefore the American consumer gained without any impact to the American worker.

### **C. The Trade Balance and the Balance of Payment Statement**

The United States has experienced a trade deficit for nearly 30 years yet our economy has continued to become more prosperous.<sup>59</sup> Litan explains that the influx of funds from Asia,

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<sup>57</sup> Robert E. Litan, "The Globalization Challenge", *The Brookings Institute*, Spring 2000p 37

<sup>58</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb047/pb47.htm>, Policy brief #47, April 1999

<sup>59</sup> One of the most important tools for analyzing a countries economic position is the balance of payment statement. This statement contains three main parts called the current account, capital account, and the balance of official reserve transactions. The net value of exports and imports comprises the current account section. The capital account reflects the net change in claims and liabilities of a country in contrast with the rest of the world. The average American views exports as good and imports as bad. This perspective myopically views only a portion of the overall health of the

which meant an increase to our capital account, during the financial crisis kept U.S. interest rates low and encouraged investment and consumption which offset declines in American exports.<sup>60</sup> Unemployment was at a record low, consumer confidence was at a record high, and just as importantly global stability and prosperity, on the whole, has been increasing. All of this has occurred while we maintained and increased our trade deficits with Asia.<sup>61</sup> China and other Asian nations, who had significant trade surpluses with the rest of the world, faced a severe financial crisis. Although imports and exports play an important role in the U.S. balance of payments, they do not play an exclusive role.<sup>62</sup> A look at the balance of payments must be tempered with other variables such as fiscal and monetary policies pursued as well as external factors that affect the global economy such as OPEC.

What often goes unsaid is the relative gains in trade America has experienced in Asia. In 1996, US overall trade with Asia stood at \$570B compared to \$270B with Europe.<sup>63</sup> Expectation for this trend to continue weighs heavier than any reversal. Additionally, the exports the United States provides to developing China are high end goods such as machinery, chemicals, and services while in return China exports to the United States labor intensive goods such as clothing, footwear, toys, and small appliances. Additionally, China, under existing non-WTO

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economy. Normally when a country is in a net trade deficit, then the capital account increases. Funds in this account can be used to expand capacity which creates permanent increases in an countries production capabilities. This is an oversimplification of the general equilibrium model but its purpose is to point out that a trade deficit is not necessarily a bad position to be in.

<sup>60</sup> Robert E. Litan, "The Globalization Challenge, *Brookings Review*, Spring 2000, p 35

<sup>61</sup> The growing deficit the United States has experienced in its trade with China not surprisingly has been accompanied by sharply declining deficits with Hong Kong, Taiwan, and Korea. Thus the argument that the growing deficit with China has caused a large loss of manufacturing jobs in the United States is misguided.

<sup>62</sup> Wallace C. Peterson and Paul S. Estenson, *Income, Employment, and Economic Growth*, W. W. Norton & Co, NY 1992 provides a comprehensive macroeconomic study with analysis on monetary and fiscal policy.

criteria has free market access in the United States while the United States faces tariff, non-tariff and quota barriers into China's market. Through a free-trade mechanism such as the WTO, China will reduce their barriers which will increase American trade with them.

#### **D. Analysis**

Clearly, open trading with China should be welcomed. The American form of government encourages innovation and freedom of choice. Businesses are able to react to the market rather than direction from the government. As a result, greater efficiencies are created. Further competition from outside sources increases efficiencies which benefit the consumer. Domestic businesses that are less efficient than foreign businesses close down, but because of the enterprising spirit that defines America, other businesses are created. Moreover, the ability to educate a population in addition to the quality of education afforded allows for merely a temporary displacement among the workforce. Furthermore, unemployment rates have been decreasing overall during the past twenty years, which coincides with greater openness of trade among the world. Therefore, arguments against more open trade with other countries such as China are self-defeating.<sup>64</sup> Additionally, the trade balance between other countries is only one of a number of factors when assessing the health of a country's economy and should be weighed against all elements.

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<sup>63</sup> Kishore Mahbubani, "An Asia-Pacific Consensus", *Foreign Affairs*, Vol 76 No 5, Sept/Oct 1997, p 151

<sup>64</sup> David H. Carstens, "Bringing Environmental and Economic Internationalism into U.S. Strategy", *Parameters*, Vol XXXI, No 1, Spring 2001 p.106 - In an excerpt Carsten very succinctly sums up America's vested interest in trade when he states, "From 1995 to 1998, the U.S. imposed/threatened economic sanctions 60 times against 35 different countries, affecting an estimated 42% of the world's population. Economic sanctions cost our nation approximately \$20B in lost annual exports with varying effects. The bottom line is that U.S. companies bear most of the economic burden."

#### **IV. COSTS AND BENEFITS - CHINA**

China's economic success is self-evident; however, they have experienced a number of costs for the rural and urban sector. The themes covered in both these sectors revolve around developmental progress, income inequalities, environmental concerns, corruption, and the prospects for democracy. Once China opened its doors to greater trade, it became inexorably linked to the rest of the world. As we have seen, China's main efforts have focused on economic development. Presently, China has a greater vested interest in maintaining harmonious relations with the United States than does the United States with China. This is so because China has more at stake in trade with the United States. As noted before, China's trade with the U.S. amounted to 22.9% of total Chinese trade consisting of 9.5% of Chinese GDP, while trade with China accounted for only 4.6% of total U.S. trade and .9% of US. GDP.<sup>65</sup> The aforementioned proportions are not likely to continue. As China opens its doors wider to foreign investment and trade, the United States will most likely develop greater economic interest as their ties with China expand. Anticipating the change, it behooves the U.S. to begin now to improve relations and shape the situation to its advantage.

##### **A. Agriculture**

To understand how economic interdependence figures in so prominently for China, we need to understand China's growth track. As mentioned above, Mao initially planned to engage in trade with the West. As the rise of communism brought fear of a Sino-Soviet military threat, it prompted the U. S. to impose a total trade embargo. Mao, therefore, chose autarky and pursued a course of self-reliance. Following the Soviet model of central planning, Mao's desire for both self-reliance and greater prosperity drove him to place his emphasis on industrialization

to the detriment of agriculture. By 1978, Nearly 71% of the total workforce was still working subsistence level farming,<sup>66</sup> as opposed to the United States who employed merely 2% of their workforce and produced enough food per farmer to feed over 80 people.<sup>67</sup> The PRCs attempt to develop industry too early resulted in perpetual low growth in the industrial sector and the death of over ten million Chinese through starvation.<sup>68</sup> As evidenced above, the rural agricultural sector oftentimes was overlooked by developing countries because it is viewed as making a marginal contribution to growth.<sup>69</sup>

Learning from the mistakes of the Great Leap Forward, Deng Xiaoping endorsed and encouraged rural development through a three-pronged strategy of land reform, supportive policies, and integrated development objectives. The land reforms evolved from a commune-based collectivization system to a contract responsibility system where peasants had a free hand in keeping or selling goods in the free market.<sup>70</sup> The government support policies included incremental reductions in mandatory delivery quotas, decreases in taxes, deregulation to crop prices which provided the necessary incentives to raise productivity. As productivity increased, rural farmers used excess profits towards entrepreneurial endeavors which met integrated development objectives. As a result, town and village enterprises began to flourish in a free market environment and the living standards for the rural Chinese increased significantly. The

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<sup>65</sup> Paul A. Papayoanou, and Scott L. Kastner, "Sleeping With the (Potential) Enemy: Assessing the U.S. Policy of Engagement With China", *Security Studies*, Vol 9, No 1-2, Autumn-Winter 1999/2000, p 185

<sup>66</sup> Wei-Wei Zhang, *Transforming China*, St Martin's Press, Inc, NY, 2000 p 9

<sup>67</sup> Michael P. Todaro, *Economic Development*, Longman, NY, p 289

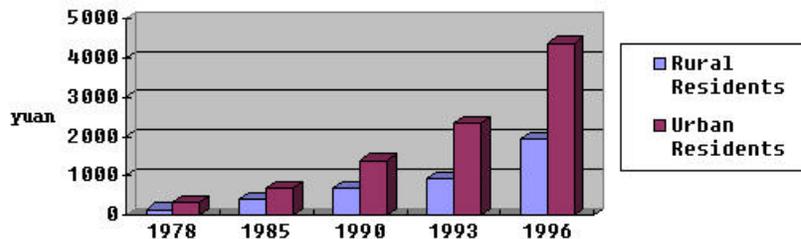
<sup>68</sup> Fan Gang, Dwight H. Perkins and Lora Sabin, "People's Republic of China: Economic Performance and Prospects", *Asian Development Review*, Vol 15 No 2 pp 50-52.

<sup>69</sup> Gunnar Myrdal, Nobel Laureate in Economics, stated, "It is in the agricultural sector that the battle for long-term economic development will be won or lost."

<sup>70</sup> Wei-Wei Zhang, *Transforming China*, St Martin's Press, Inc, NY, 2000 p 9

chart below provides a comparison of changes in living standards from 1978-1996.<sup>71</sup> This success in the agricultural sector had an exponential effect on the Chinese economy. As farmer's incomes increased, demand for consumer goods increased to encourage the growth of industry.

### Per Capita Annual Income of Urban and Rural Household



### B. Income Inequality.

Although an apparent success story, prosperity in China has not been equal in either time or space. When reforms began focusing on industry, it affected agriculture. Productivity gains in agriculture reduced the need for labor and price reforms and also lowered the cost of agricultural products. These efficiencies in the agricultural sector resulted in a surplus of unemployed labor and a mass migration from the rural to urban areas which were beginning to experience take off.<sup>72</sup> Rural citizens who moved into the urban areas were not afforded housing, medical care, or other safety nets provided to registered urban dwellers. Additionally, this growing unemployment in the urban areas placed a strain on the CCP who feared that growing

<sup>71</sup> Taejoon Han, *China: a shared poverty to uneven wealth?*, The George Washington University, The Elliott School of International Affairs, <http://www.gwu.edu/~econ270/Taejoon.html>, This chart also references the urban area changes in per capita income as well as highlighting the dramatic income inequalities between the rural and urban areas which is discussed below. The amounts are in yuan. In 2000, Chinese per capita income was \$3.8K as previously mentioned.

<sup>72</sup> Fan Gang, Dwight H. Perkins and Lora Sabin, "People's Republic of China: Economic Performance and Prospects", *Asian Development Review*, Vol 15, No 2, p 72

discontent would lead to increased public instability. Moreover, inequalities opened up between the more vibrant coastal areas to that of the in-land areas. FDI tended to be concentrated in the coastal regions which created widening socio-economic differences between the coastal areas and the interior regions. This influx of FDI coupled with the migration from the agricultural regions of the interior to the urban areas of the coast gave rise to increases in income inequalities, criminal activities, environmental degradation, and social diseases.<sup>73</sup> As of 1995, city workers made three times more than rural workers and the gap can be expected to rise.<sup>74</sup> Loss of arable land to soil erosion and housing construction also affected rural income losses. Both time and space ultimately contributed to increasing income distribution inequality. Income inequality has aggravated tensions in provinces such as Xinjiang over the past decade. As international markets began to expand in China, income inequality will come to the forefront in China's domestic policy. Concerns for domestic policy can spill over into their foreign policy resulting in a very de-stabilizing environment. Unlike the United States, China's job displacement could become more problematic because China does not have the level of education, market sophistication, or social welfare programs to absorb and cushion it.

### **C. Village Elections and Corruption**

The economic reforms in rural areas and the development of town and village enterprises have brought about political reforms through the introduction of village-level elections. On their own initiative, Chinese citizens were organizing village committees to manage affairs. As the towns grew, corruption and nepotism grew even more giving rise to peasant discontent.<sup>75</sup> As a

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<sup>73</sup> James H. Mittelman, *The Globalization Syndrome*, Princeton University Press, New Jersey, 2000, p 54

<sup>74</sup> Research Institute for Peace and Security, *Asian Security 1995-1996*

<sup>75</sup> Yu Weiguo, "In Developing the Western Region, We Should Give No Opportunity for Corrupt Officials to Exploit" *Beijing Renmin Ribao* 23 Sept 00 p 8 (trans by FBIS) discusses corruption in Western Development in China

result, the CCP instituted village level elections. Although these elections are far from Western standards, they are exposing the Chinese to the democratic practices. The CCP carefully selects officials who they place in these elections because they have a vested interest in ensuring party stability throughout the country. The CCP has an urgent need to allay corruption because corruption seriously undermines the regime's authority and the long-term prospects for China. The next generation CCP leadership can be expected to make even greater progress towards power sharing, negotiating, and consensus building<sup>76</sup>. Even though ethnic Chinese own 70% of the "clan" businesses, the new financial technocrats, who reflect the tenets of liberal-economic globalization transmitted by business and law schools are now coming of age. Leadership is moving from reliance on Soviet trained engineers to Western and Asian trained lawyers and economists.<sup>77</sup> This transition in political ideology can re-inforce economic prosperity as "cohabitation of communism and commercialism is inherently contradictory."<sup>78</sup> At any rate, Taiwan's success provides encouraging evidence that democracy and the Chinese culture are compatible.<sup>79</sup>

Because China's form of government tends to build on nepotism and party favors, embezzlement, such as the case with Chen Xitong who was mayor of Beijing, is common place. Chen misappropriated over \$2B from the government as well as from foreign and Chinese businessmen. Cases like this have contributed not just to internal unrest, but also to a reduction in confidence for both domestic and foreign investors which has resulted in an increase in capital

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Jasper Becker, "Anger at Dam Corruption Growing", *Hong Kong South China Morning Post* 29 Sept 00 (trans by FBIS) discusses Peasant Anger over corruption at Three Gorges Dam.

<sup>76</sup> China's third generation leadership under Jiang Zemin is unlike that of Mao or even Deng and runs along the line of collective consensus.

<sup>77</sup> Li Cheng, "Seeking Common Ground at a Time of Tension and Conflict", *Asian Survey*, Vol XL, No 1, Jan/Feb 2000, p 115-116

<sup>78</sup> Zbigniew Brzezinski, "Living With China", *The National Interest*, Spring 2000, p 8

flight from China in recent years.<sup>80</sup> Much of the problem with corruption is attributed to a lack of legal and administrative transparency. Without this transparency, standards are not created and thus rights are not enforceable. Another serious problem that has recently been corrected grew from the allowance of official institutions such as the PLA to enter into profit making activities, which has resulted in extensive smuggling operations.<sup>81</sup> These smuggling operations hurt both the domestic and foreign economy. The domestic Chinese economy suffers because legitimate business lose profits that they otherwise would have made had the smuggled goods not been substituted and the government of China suffers lost tax revenues. The foreign economies are affected because of the smuggling and pirating of computer software, and other intellectual property thefts and copyright violations. China's flawed legal system clearly contributes significantly to the rise of corruption, smuggling, piracy, and continued social unrest.

Elections at the grassroots level have been making some progress in Guangdong too. Since town and village enterprises are well developed in Guangdong and their profits often constitute a considerable proportion of the local inhabitants' income as well as make significant contributions to the provision of social services at the local level, people are very concerned with the leaders of the local governments who own the enterprises and appoint managers to run them. Hence, voter participation can often become quite enthusiastic.<sup>82</sup> While this is good for democracy, it has the propensity to increase corruption. Corruption is a symptom of a rapidly modernizing society especially since it lacks laws and regulations. Guangdong's establishment

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<sup>79</sup> Zbigniew Brzezinski, "Living With China", *The National Interest*, Spring 2000, p 13

<sup>80</sup> Wei-Wei Zhang, *Transforming China*, St Martin's Press, Inc, NY, 2000 p 133

<sup>81</sup> Ibid, p 135 and Stephen Kho, *The Impact of the World Trade Organization of the Lack of Transparency in the People's Republic of China*, University of Maryland, No 2, 1998 provides an essay on how the WTO can bring transparency to China which will be discussed in part 4 of this paper.

of law enforcement mechanisms and personnel was overshadowed by the highly publicized smuggling and corruption in Guangdong.<sup>83</sup> China's induction into the WTO will help it move forward on its quest to develop the rule of law. Additionally, although political reform is not anticipated anytime soon,<sup>84</sup> the need for greater accountability, current grass roots democracy, and further economic development may promote greater levels of democracy although only time will tell.

#### **D. Urban Growth, State Owned Enterprise (SOE) failure, and private enterprise success**

By following the Stalinist model, China's premature emphasis on heavy industry at the expense of agriculture developed the platform for the problems encountered today in China's urban reform – the failing SOEs. Urban reforms were even more sweeping than agricultural reforms. Like agricultural reforms, China executed them in a dynamically gradualistic manner.<sup>85</sup> Reforms began with a few selected SOEs which were allowed to market their surpluses over state mandated quota's. Although these reforms sparked some positive changes and increased productivity, by 1997 SOE losses increased by over 500% from 1985 and their gross value of industrial out put decreased from 77.6% in 1978 to 26.5% in 1997.<sup>86</sup> However, the success of the rural town and village enterprises spilled over into the urban areas and the private sector soon gained considerable momentum. The creation of private enterprise has given rise to a rapidly

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<sup>82</sup> Joseph Y. S. Cheng, "Guangdong Challenges: Organizational Streamlining, Economic Restructuring, and Anticorruption", *Pacific Affairs*, Vol 73, No 1, p 29

<sup>83</sup> Ibid, p 31

<sup>84</sup> Ibid, p 35

<sup>85</sup> Wei-Wei Zhang, in his book *Transforming China: Economic Reforms* coined the term dynamic gradualism when describing China's growth. He uses it to dissuade viewing China's growth as all gradual or all radical and uses a number of examples such as "the fast reforms executed in the rural sector esp in regards to land reforms, town and village enterprises yet with a guiding philosophy of gradual shifts such as the pricing policies and government quotas on agricultural production. See pages 46-53 for further elaboration.

<sup>86</sup> Kathy Wilhelm, China Cover Story, *Far Eastern Economic Review*, 18 Feb 99, p 14

growing middle class that employs over 17.5M people as of 1997. Even more importantly, the relationship between state and society has changed by reducing the states direct control on the individual citizen. The individual's income level and profession he pursues have replaced political allegiance and status in an SOE.<sup>87</sup> As interdependence becomes more prevalent through MNCs and other forms of FDI, so will the Chinese citizens exposure to "other" forms of Western ways.

Although upward mobility was experienced by many through transition from SOEs to private enterprise, others experienced downward mobility. Much of this has to do with the relative constraints on training human capital and engaging in research and development compared to what is possible in the more developed countries such as the United States. Improving education becomes more urgent if the PRC wants to catch up to the NICs and post-industrial economies. Guangdong Province decided this was important enough that they drew up a five-year plan that incorporated not just local training but training in Western University to study international economics, finance, and management.<sup>88</sup> In addition to training and R&D, the SOE's cradle-to-grave package mandated by the state creates organic inefficiencies. As a result, the traditional SOEs have little chance of competing with private industry. One solution was initiated by Shenzhen and Shunde provinces which developed systems separating the government from the company. In the case of Shenzhen, they created city investment management companies which created a relationship of investor to legal entity. Shunde created a shareholding cooperative system. Another solution laid out by the CCP has been the authorization to sell all but the "strategically oriented" SOEs. The CCP illustrated this through a

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<sup>87</sup> Wei-Wei Zhang, *Transforming China*, St Martin's Press, Inc., 2000, p 87

<sup>88</sup> Cheng, Joseph Y.S., "Guangdong Challenges", *Pacific Affairs*, Vol 73, No 1 p 31

movement to incorporate into its constitution an amendment which endorsed the private sector as an important part of the economy.<sup>89</sup> Both solutions recognize the importance of separating the government from enterprises, thereby privatizing which is an important distinction as China moves towards global integration.

As China struggles to move from a centrally planned, state-owned economy to a free market economy it must overcome a number of challenges. As the traditional SOE disintegrated, the CCP tax base has been jeopardized. Broad Air Conditioning is an example of a private company which has become the backbone of the Hunan province.<sup>90</sup> Its \$192M in sales, and 1,200 workers brought vitality to the area and provided the largest tax base to the province.<sup>91</sup> This new tax base is important in a couple of respects. Pre-reform China obtained state funding through taxation of the SOEs. Post-reform China, on the other hand, created a value-added tax out of necessity as a result of the considerable decline in revenue from taxation on the profit losing, inefficient SOEs. However, because of a lack of competent rules of law, inadequate enforcement measures, and rampant corruption, China is encountering significant collection problems. Given the chronic lack of international competitiveness of SOEs as well as the increasing acts of corruption, the decrease in state revenue can be anticipated to continue. The CCPs need for an increased tax base serves to maintain stability. Infrastructure projects and, even more importantly, a social net to provide for the promised cradle-to-grave benefit package SOEs guaranteed to each worker which included housing, education, health care, and pensions<sup>92</sup>

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<sup>89</sup> Kathy Wilhelm, *China Cover Story*, *Far Eastern Economic Review*, 18 Feb 99, p 11

<sup>90</sup> Louis Putterman and Xiao-Yuan Dong, "China's State-Owned Enterprises: Their Role, Job creation and Efficiency in Long-Term Perspective", *Modern China*, October 2000, p 404

<sup>91</sup> Roberts, Dexter et al, "China's New Capitalism", <http://www.businessweek.com/1999>, 27 Sept 99

<sup>92</sup> Kathy Wilhelm, "China: Cover Story", *Far Eastern Economic Review*, 18 Feb 99 p 14

are needed until domestic or foreign firms can fill the gap. Although SOEs may wish to generate profits, state protection reduces their motivation to change business practices, so where private industry would go out of business in the absence of profit, the state perpetuates unproductive, profit losing enterprises. Therefore SOEs can embark on endeavors that private enterprise would not because of an unwritten bankruptcy policy with the state.<sup>93</sup> China's continued state support of these failing SOEs become a critical point in foreign policy as China moves to increase access to its markets to foreign investors. The infrastructure, human development capacity, and vitality of the Chinese economy pales in comparison to U.S. markets and will significantly impact transitional capabilities.

#### **E. Analysis**

China's land reforms emphasized raising agricultural productivity. This in turn gave rise to the lucrative town and village enterprises. Success in the rural sector prompted Chinese policy makers to adopt labor intensive light manufacturing for export. Corruption, income inequalities, dysfunctional SOEs and the lack of political reform represent significant obstacles in the way of continued economic reform. Since the Asian economic crisis of 1997, China's growth has slowed considerably. Although it has gained some momentum, continued progress will depend on resolution of the conflict between the economic reforms and that of its political reforms.

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<sup>93</sup> Louis Putterman, and Xiao-Yuan Dong, "China's State-Owned Enterprises: Their Role, Job creation and Efficiency in Long-Term Perspective, *Modern China*, October 2000, p 417

## V. World Trade Organization (WTO)

### A. General Description of WTO

The General Agreement on Tarriff and Trade (GATT) was created in 1947 and its initial goal was to lower trade barriers between countries on goods produced. The GATT was not recognized in law as an international organization. The WTO succeeded the GATT during the 1994 Uruguay Rounds and expanded its reach from just goods, to goods, services, and intellectual property rights. The WTO established the rules of trade through agreements which are the legal ground-rules for international commerce and trade policy. The agreements produced have three main objectives: to help trade flow as freely as possible, to achieve further liberalization gradually through negotiation, and to set up an impartial means of settling disputes.<sup>94</sup> The principles of the WTO are: trade without discrimination through most favored nation status, national treatment (which means treating foreign and local goods equally,) free trade enacted gradually through negotiation, giving developing countries longer lead times to allow for adjustment, and predictability through binding agreements which allows for stability, promoting competition through fair trade, and encouraging development and economic reform while providing lesser developed countries flexibility in implementation.<sup>95</sup> Below is a snapshot of WTO commitment success by three broad categories of countries:

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<sup>94</sup> [http://ww.wto.org/english/thewto\\_e/](http://ww.wto.org/english/thewto_e/)

<sup>95</sup> [http://ww.wto.org/english/thewto\\_e/](http://ww.wto.org/english/thewto_e/)

## Percentages of tariffs bound before and after the 1986-94 talks <sup>96</sup>

	Before	After
Developed countries	<b>78</b>	<b>99</b>
Developing countries	<b>21</b>	<b>73</b>
Transition economies	<b>73</b>	<b>98</b>

The WTO helps trade flow smoothly, freely, fairly and predictably. It does this by: administering trade agreements, acting as a forum for trade negotiations, settling trade disputes, reviewing national trade policies, assisting developing countries in trade policy issues, through technical assistance and training programs, and cooperating with other international organizations.<sup>97</sup> Developing countries comprise three fourths of the membership in the WTO and have special provisions to assist in success.<sup>98</sup> These special provisions include, longer time periods for implementing agreements and commitments, measures to increase trading opportunities, provisions requiring all WTO members to safeguard the trade interests of developing countries, and support to help developing countries build the infrastructure for WTO work, handle disputes, and implement technical standards.

One of the most critical elements of ensuring compliance to WTO regulations is through greater legal and administrative transparency.<sup>99</sup> To become a member, the country applying must submit a memorandum describing all laws, regulations, and policies affecting trade and

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<sup>96</sup> [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/fact2\\_e.htm#bind](http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact2_e.htm#bind) (chart) These are tariff lines, so percentages are not weighted according to trade volume or value

<sup>97</sup> [http://www.wto.org/english/thewto\\_e/whatis\\_e/inbr02\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/inbr02_e.htm)

<sup>98</sup> [http://www.wto.org/english/thewto\\_e/whatis\\_e/inbr02\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/inbr02_e.htm)

<sup>99</sup> Stephen Kho, *The Impact of the World Trade Organization of the Lack of Transparency in the People's Republic of China*, School of Law, University of Maryland, No 2, 1998 (145), p15 The Uruguay Round was instrumental in not

investment. Next a working party is created to bring the applicant's domestic laws and regulations in compliance with the WTO. Once this is done the working group produces a report that includes the following: a description of the applicant's trade regime, an amplification of the applicant's plan for implementation, commitments which are enforceable through the WTO dispute-settlement process, and the working party's interpretation regarding their interpretation of the commitment.<sup>100</sup>

## **B. China and the WTO**

The Republic of China (ROC) was one of the founding members of the WTO, however, in 1949, the Peoples Republic of China (PRC) drove the former out and established themselves as the legitimate party in mainland China. The ROC withdrew their membership in 1950 and the PRC chose not to join. In July 1986, the PRC requested formal membership to GATT, and in May 1987 the WTO created a formal working party to determine terms and conditions for membership.<sup>101</sup> As of today, significant trading partners such as the EU and the U.S. have approved most favored nation status to China, and China is projected to enter the WTO within the year.

**The Rule of Law.** As noted above, transparency is a key issue in WTO membership. It is this issue which has been the greatest obstacle to China's membership. However, economic reforms, consistent with WTO standards, are bringing China closer to the ideal of the rule of law in a number of areas. Although human rights monitors complain that the state of civil liberties in China remain medieval, there have been noticeable improvements. Some victims of unlawful detention by local police, for example, recently sued the government and won compensation.

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just furthering trade liberalization but more importantly in establishing a rules-based WTO.

<sup>100</sup> Mark A. Groombridge and Claude E. Barfield, *Tiger by the Tail*, The AEI Press, Washington, D.C. 1999, pp 15-16

Moreover, thousands of local officials are being subjected to public approval with the introduction of elections at the village level to curtail corruption.<sup>102</sup> The Chinese economy and society still work under informal rules and arrangements, which oftentimes goes against the rules of law and encourages corruption. The courts, in many cases, exist in name only and often implement law by arbitration. Government regulations rather than legal precedence usually take priority. Enforcement of China's contract law remains a problem because the law is still in its infancy and not regularly enforced. However, there have been over 40 new sets of laws adopted since the early 1980s. The process of drafting and adopting laws has accelerated in recent years. The Bankruptcy Law, Consumer Rights Law, Corporate Law, Central Bank Law, Commercial Bank Law, Labor Law and Commercial Paper Law have all been created.

Law enforcement, however, remains weak.<sup>103</sup> Highly publicized corruption and smuggling headlines has prompted Guangdong into action in this arena. Their five-year plan includes establishing a system of local laws and regulation as well as a team of law enforcement personnel, to strengthen law enforcement responsibility mechanisms and law enforcement supervisory mechanism and to enhance the sense of law among cadre and people.<sup>104</sup> By inducting China into the WTO, there is greater opportunity to bring China more in line with legal norms which will be in the interest of both China and the United States.<sup>105</sup>

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<sup>101</sup> Mark A. Groombridge and Claude E. Barfield, *Tiger by the Tail*, The AEI Press, Washington, D.C. 1999, p 14

<sup>102</sup> Denny Roy, "China's post-Deng Foreign Relations", *International Journal*, Vol LIII No 1, Winter 1997-98 p 138

<sup>103</sup> Fan Gang, Dwight H. Perkins, and Lora Sabin, *People's Republic of China: Economic Performance and Prospects*, *Asian Development Review*, p 57

<sup>104</sup> Joseph Y. S. Cheng, "Guangdong Challenges: Organizational Streamlining, Economic Restructuring, and Anticorruption", *Pacific Affairs*, Vol 73, No 1, p 30

<sup>105</sup> It must be pointed out that the WTO decides whether a country has rules that unfairly discriminate against foreign goods not whether the rules are unsound. (refer to Litan, "Globalization Challenge" p 36)

**The Results.** Greater transparency and the rule of law will assist China in many ways. First, implementing law and order can alleviate corruption, which has plagued China in recent years. Also, foreign companies will feel more secure investing in China.<sup>106</sup> As a result, SOEs will face greater competition which will create greater efficiencies.<sup>107</sup> Assisting China in embracing the rule of law will not just provide economic benefits but may prove to have democratizing effects. Since the ruling elite finds the former to be in its interest, “the propagation of the rule of law is both politically easier and in the long run more effective.”<sup>108</sup> This theory is not far-fetched because the dynamic has been at work to transform Taiwan, South Korea, and even Singapore.<sup>109</sup>

**The Pros and Cons of WTO membership.** Besides bringing greater transparency to China, the WTO embeds China more deeply into the global system thereby encouraging it to be a more responsible member.<sup>110</sup> Moreover, membership symbolizes status which will direct Chinese nationalism in a more positive venue. Additionally, it allows information and ideas to flow into China from the outside which may ease the process of democratic reform. Opening markets to foreign businesses will inject additional FDI into China as well as needed science and technology thereby creating jobs. Finally, WTO membership will increase the importation of goods into China which will increase China’s domestic wealth.<sup>111</sup>

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<sup>106</sup> Mark A. Groombridge and Claude E. Barfield, *Tiger by the Tail*, The AEI Press, Washington, D.C. 1999, p 2

<sup>107</sup> This could mean the decline of SOEs which will create unemployment problems in China – a situation the U.S. must be sensitive to as China develops.

<sup>108</sup> Zbigniew Brzezinski, "Living With China", *The National Interest*, No 59 Spring 2000, p 16

<sup>109</sup> Although Singapore has been under the same regime, it is simply because that regime enjoys overwhelming approval of the people, therefore democracy is well played out in this country.

<sup>110</sup> China’s current level of responsibility in its participation in international organizations was noted in section 3.

<sup>111</sup> It will also serve to increase foreign markets export trades to China.

Critics of inducting China into the WTO declare that China may fall short of its obligations. However, Lardy points out four reasons why this should not be a concern. First, trade law will provide the first line of defense for any Chinese trade transgressions. Also, China's accession should be contingent on WTO progress reviews that ensure they are in full compliance with their commitments. Moreover, the WTO dispute resolution procedures can be used to challenge China when it violates trade rules. Finally, China's past and current participation in international organizations, as identified in Section 3, engenders confidence that it will meet its obligations.<sup>112</sup>

Some debate has centered on whether China should be inducted as a developed or developing country. Although China has the second largest GDP, it still has very low per capita income, its financial sector is fragile, and its societal stability rests on continued prosperity. Therefore, China, should be allowed longer phase-in periods to meet WTO standards.<sup>113</sup> Additionally, it should be allowed time to restructure its failing SOEs which will be greatly affected by the incoming competition once trade restrictions are lifted. In the absence of gradual restructuring, political instability may well ensue and weaken any economic progress made. Although risky, the leadership in China is anticipating "redeployment of labor into more efficient firms thereby hoping to spur job creation and growth. The leadership, in other words, sees heightened global competition as a means to accelerate economic reform and restructuring."<sup>114</sup> Another risk is China's fragile banking system which currently is not competitive with foreign banking systems. The banking sector must be strengthened prior to

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<sup>112</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb010/pb10.htm>, Policy Brief No 10, Nov 1996

<sup>113</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb047/pb47.htm>, Policy brief No 47, April 1999

<sup>114</sup> Daniel A. Lapres, "The EU-China WTO Deal Compared", *The China Business Review*, July/August 2000

expansion of foreign competition otherwise a financial crisis may ensue.<sup>115</sup> Incorporating China into the WTO as a developing country will help ensure the economic benefits received by China will be proportional to the costs.<sup>116</sup> These risks are much greater for China than they are for the U.S. Although China must commit to WTO standards, long transition periods with firm deadlines for compliance in some sectors may be necessary for China's successful induction into the WTO. The alternative to helping China assimilate into the WTO would be "to risk the world's tenth-largest producer of export goods and the largest trading country in the world, not already subject to the disciplines of the established international trading system, to remain outside the WTO – a situation that is undesirable for the future of the world trading system, China's economic evolution, and the U.S.-China relationship."<sup>117</sup>

### **C. Environmental and Labor Concerns**

Environmental and labor issues in the developing countries are a major political issue for the industrial countries. The lack of or inadequate control measures implemented in the developing countries impacts on industrial countries in areas such as employment and export trade. Free trade advocates such as Griswold profess that non-trade issues such as environmental and labor concerns have no place in the international trade arena and should be handled in a completely separate forum.<sup>118</sup> On the other hand, environmental activists, such as Carstens, asserts that the U.S. should assume a strategy of economic encouragement first, trade sanctions if

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<sup>115</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb047/pb47.htm>, Policy brief #47, April 1999

<sup>116</sup> Nicholas R. Lardy <http://www.brook.edu/comm/policybriefs/pb010/pb10.htm>, Policy Brief No 10, Nov 1996

<sup>117</sup> Nicholas R. Lardy, <http://www.brook.edu/comm/policybriefs/pb010/pb10.htm>, Policy Brief No 10, Nov 1996

<sup>118</sup> Daniel T. Griswold, "The Future of the WTO", *Cato Journal*, Vol 19, No 3, Winter 2000, p 347

the former fails, and military response as a last resort.<sup>119</sup> Carstens correctly identifies the problems facing developing countries though and provides a focus on China. There are three problems with taking a hard line approach with developing countries on these issues. First, economies such as China's cannot effectively deal with these issues at this time because they do not have the financial wherewithal to effect change. Second, they have political concerns that far outweigh social and environmental concerns. Litan points this out when he states that "passing and enforcing more laws that add first-world protections will slow developing countries, such as China's, economic development – and thus improvements in environmental and labor conditions – by driving more business into the underground economy, where even third-world standards are not enforced."<sup>120</sup> Also, as mentioned previously, as average incomes grow, citizens tend to demand improved labor and environmental protection.<sup>121</sup> Finally, placing restrictions on less developed countries simply lifts visible tariffs off and places non-tariff barriers on the goods and services in question. It is very easy to point out a problem, but what is not easy is developing and implementing a solution that is acceptable to all concerned. These concerns, just as they were addressed by the United States for labor rights during the late 1800s and early 1900s and for environmental concerns during the 1960s and 1970s, will be addressed by China when their costs outweigh their benefits and the Chinese citizenry are motivated to action.

Although China's violations seem to make the news often, many of them are no worse than that in Turkey or India for example. India alone backed Soviet aggression, went to war with

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<sup>119</sup> David H. Carstens, David H., "Bringing Environmental and Economic Internationalism into U.S. Strategy", *Parameters*, Vol XXXI, No 1, Spring 2001 (Paul Kennedy would have a field day with Carstens recommendation as many of them would break the U.S. bank – recommendations such as increasing military spending, forgiving billions of dollars in debt, etc.)

<sup>120</sup> Robert E. Litan, "The Globalization Challenge", *Brookings Review*, Spring 2000, p 36

<sup>121</sup> Robert E. Litan, "The Globalization Challenge", *Brookings Review*, Spring 2000, pp 36-37

its neighbors more often than China, flaunted its disregard for nuclear-non-proliferation, used force to resolve colonial issues such as Goa, and has been careless of human rights in Kashmir<sup>122</sup> yet they get less press than does China. Even those we consider our strategic partners, such as Taiwan, South Korea, and Singapore have conducted themselves in ways considered offensive by Western standards. Although not a panacea, incorporating China into the WTO and furthering its development may induce changes which will improve these problems. In fact, Taiwan, South Korea, and Singapore already have demonstrated improvement, and it is quite conceivable that as China's wealth increases, so too will its ability to correct societal problems.

#### **D. Security Concerns**

In the short term, China will most likely maintain peace because North America, Western Europe, Japan, Australia, and New Zealand are a significant share of its export market. Additionally they are all democracies and are allied with each other.<sup>123</sup> Moreover, the PRC leadership is preoccupied with three concerns: political and social stability, economic growth and national unification, none of which can be adequately addressed unless Beijing is able to secure cooperative and accommodative relations with the outside world. Therefore, integration serves the interest of not only the international community but those domestic interests of China as well.<sup>124</sup> Through broader markets, China's wealth will increase. As wealth increases, so does military power. Paul Kennedy provides a very detailed account of how, historically, economic

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<sup>122</sup> Brzezinski, Zbigniew, "Living With China", *The National Interest*, No 59 Spring 2000 p 20

<sup>123</sup> Roy, Denny, "China's post-Deng Foreign Relations", *International Journal*, Vol LIII No 1, Winter 1997-98 p 138 (Yet in the long term, according to the balance of power theorists, there is still the potential for China to become our foe. Free trade, espoused by the WTO, could be the catalyst for Chinese aggression; however, this is unlikely in the near future. Additionally, as the average Chinese gains wealth, they will more than likely demand greater freedoms which has the propensity to advance democracy. As such, according to the democratic peace theory, democracy's normally do not conflict with each other.

shifts have resulted in a rise of new Great Powers who have had a decisive impact upon military/territorial order.<sup>125</sup> Chinese nationalism could also turn the tide of a peaceful global world especially in regards to Taiwan.

Other Asian countries have increased their concern over China's rise especially in terms of border disputes giving credence to the balance of power theory.<sup>126</sup> The most pressing issue relates to Taiwan which is considered by China as their "Manifest Destiny."<sup>127</sup> The other major concerns are portions of Tajikistan, the Spratleys, and the Diaoyu islands which are estimated to contain significant oil reserve – a commodity demanded continuously more by any growing country and will be viewed by China as a vital national interest if it is not already.<sup>128</sup> Despite this, many of China's Asian neighbors want a more prosperous and engaged China. Alliance structures in China by virtue of culture are loosely formed and do not seem to be going down an antagonistic track. In fact, China played a fairly significant role in helping the other Asian countries work through the Asian financial crisis. Although national interests, alliance systems, geography, military organizations, and many other factors will play an integral part in whether China will pursue an aggressive course or not, incorporating them into the WTO would provide

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<sup>124</sup> Wu Xinbo, "Integration on the Basis of Strength: China's Impact on East Asian Security", <https://wwwc.cc.columbia.edu/sec/dlc/ciao/wps/xiw01/>

<sup>125</sup> Kennedy, Paul, *The Rise and Fall of the Great Powers: Economic Change and Military Conflict from 1500 to 2000*, Vintage Books, 1989, p xxii

<sup>126</sup> boundary with India, sections of the boundary with Russia despite a 1997 boundary agreement; portions of Tajikistan, section of boundary with North Korea in the Paektu-san area, Spratly Islands with Malaysia, Philippines, Taiwan, Vietnam, and Brunei; maritime boundary dispute with Vietnam in the Gulf of Tonkin; Paracel Islands occupied by China, but claimed by Vietnam and Taiwan; claims Japanese-administered Senkaku-shoto (Senkaku Islands/Diaoyu Tai), agreement on land border with Vietnam was signed in December 1999, but details of alignment have not yet been made public

<sup>127</sup> Taiwan reunification is incorporated in the preamble of the PRCs constitution which was adopted on 4 Dec 82. Additionally it is an accepted fact that the Chinese people are willing to go to war if Taiwan were to overtly prevent reunification.

<sup>128</sup> David Kerr, "The Chinese and Russian Energy Sectors: Comparative Change and Potential Interaction", *Post Communist Economies*, Vol 11, No 3, 1999. P 337

both a springboard and powerful incentive for global cooperation and peaceful resolution of differences – especially now while the political regime is so dependent on gaining national and individual prosperity. As Secretary of State Madeleine Albright stated, "The China trade bill represents the most important national security vote of the year."

#### **E. Analysis**

Outlined are three courses of action to ensure WTO success for China. First, trade performance and practices must be tracked within China. Second, training and support needs to be provided to Chinese officials to help them understand their rights and obligations under WTO. Third, Congress must provide additional funding to properly staff the WTO to ensure adequate personnel to handle dispute settlements.<sup>129</sup> Nothing in life is a sure bet; however, encouraging China to become part of the WTO rather than shutting them out seems a far safer wager for global peace and prosperity and would be in the best interest for the U.S. to pursue.

Even if China were to take an aggressive stand, their need to develop economically and create jobs domestically may be more conducive to pushing them back into a more peaceful box. Additionally, boisterous posturing by China rather than their commitment to regional peace, could incite their neighbors to reduce trade and investment within China. Therefore, China's propensity to aggressive rhetoric is tempered by situational reality. Bottom line is China needs to maintain peace to sustain its economic growth which is a sure fire way of furthering itself along the road of great power status.

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This article provides in depth analysis on China's growing energy concerns in relation to the declining requirements of the Soviet Union.

<sup>129</sup> Richard N. Haas, Richard N. "Foreign Policy in the Age of Primacy", *Brookings Review*, Fall 2000, p 16 (Although outside the scope of this paper, it bears mentioning that the same sense of engagement must be pursued with regional security issues and national missile defense. As has been stated throughout this paper, although economic interdependence is a critical to Sino-American relations, it is not the only aspect and security needs to be dealt with similarly.)

## VI. CONCLUSION

China's past highlights their struggle to drive forward with the remembrance of humiliation in the background. Through the five theoretical perspectives, although all of them pertain to China, the economic interdependence theory plays a prominent role in today's China. Of all the elements of power, China and the United States seem most linked through economics. As such, it is through this interdependence that the United States and China can move towards engagement. This engagement, if pursued correctly, could be in the best interest of U.S. national security. This paper has attempted to show how both the United States and China can benefit from free trade. Through all the domestic problems faced by China today, the rule of law stands out as the most promising element to reduce the costs to China. Moreover, it is in the interest of the United States to have China follow the rule of law. The WTO could be the mechanism which works towards successful implementation of this element.

It would be arrogant to think that America could sway the tide of China's future course; however, in an ever-increasing global world, each country plays a role in the future of the other. Given America's status, both domestic and international policy choices will provide a fairly significant role in the path China takes. Policy choices need to be well thought out and take into consideration such major actors as the EU, ASEAN, and China's immediate neighbors such as Russia and India.

✓ Trade must not be impeded with China. Instead of implementing trade sanctions, the US needs to move towards adding positive incentives to help induce behavioral improvements.<sup>130</sup>

Trade embargos usually do not get long term support from allies and even when they do get

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<sup>130</sup> Richard N. Haas, Richard N. "Foreign Policy in the Age of Primacy", *Brookings Review*, Fall 2000, p 7

this support, they generally do not work. Trade sanctions did not oust the CCP back in the 1950s; they did not dismantle Castro in the 1960s; they failed to affect all the Middle East regimes in the 1970s and 1980s; and, Saddam Hussein is as powerful today as he was in 1990.

- ✓ Educate Americans that trade, in the macro sense, benefits the American job market and the American consumer. Economic engagement with the rest of the world has played a key part in the U.S. economic revival.<sup>131</sup> However, labor unions prove to be an influential force in American politics; they have a more urgent need to tell of their perceived plight than do the economists to tell of the benefits of trade. As a result, the voices of labor unions are the loudest which makes them a more visible entity than the backers of free trade. Additionally, their voice is the one that politicians listen to.
- ✓ Democracy cannot come from the top down but rather from the bottom up. Promoting democracy was one of the main objectives of the United States National Security agenda under President Clinton. Rather than promoting democracy, the United States should promote prosperity. As countries become more prosperous, their citizens demand more freedoms and from this democracy is born. Promoting free trade with China will increase individual wealth and once this wealth reaches a certain level, the Chinese citizenry will self-actualize thereby desiring more democratic institutions.
- ✓ China's history of humiliation should be considered when making policy choices. Although not advocating a "bleeding heart" liberal stand in regards to China, costs should outweigh benefits. A non-economic example would be the sponsoring of the Olympics on Chinese soil. Although one can argue that their environmental and human rights standards justify

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<sup>131</sup> Robert E. Litan, "The Globalization Challenge", *The Brookings Institute*, Spring 2000p 35

preventing them from holding these games, another can argue that providing approval of the games would improve matters in these areas. This same rationale can be applied to trade issues as they surface.

- ✓ Now, while China has more at stake than the United States, is the best time possible for America to shape the China of tomorrow. Greater legal transparency and enforcement mechanisms in China should be America's number one priority. The European Union, Canada, Australia, and Japan are providing China support to understand the rights and obligations of WTO membership. Lapres provides a pertinent proposal when he recommends congressional funding for the Rule of Law Initiative proposed back in the October 1997 summit meeting with Chinese President Jiang Zemin in Washington. This initiative would provide training for Chinese judges and lawyers and strengthen Chinese commercial law and arbitration.<sup>132</sup>
- ✓ The focus should be on the fundamental problem which causes human rights violations and environmental problems. Again, instead of promoting democracy, the US should help build and extend civil societies and markets.<sup>133</sup> This will benefit not only China, but will also reward us with greater markets and more enlightened Chinese. Friedman states that "we must build bridges to China everywhere possible because these bridges have clearly become a source of restraint on the regime."<sup>134</sup> Once more, as the average citizen increases his prosperity, so to will he desire greater freedoms. It is from the bottom up, rather than the top down, that reform will take place in China and trade will play an integral part in making this happen.

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<sup>132</sup> Daniel A. Lapres, "The EU-China WTO Deal Compared", *The China Business Review*, July/August 2000

<sup>133</sup> Richard N. Haas, Richard N. "Foreign Policy in the Age of Primacy", *Brookings Review*, Fall 20, p 7

- ✓ It is a fairly well accepted fact that the United States and their allies prefer a stable China. As such, the U.S. must show sensitivities to China's problem of rising unemployment and social instability. The U.S. can help by providing guidance to the Chinese on developing a viable unemployment system and more flexible labor markets to include greater entrepreneurial endeavors.

James Hilton wrote a wonderful book called *Lost Horizons* about an American politician, named Conway, and other Westerners who are brought, against their will, to a Utopian community called Shangri-La. The message professed throughout the book by the High Lama to Conway was one of patience and moderation, clearly a policy that would serve the interest of the United States as it relates to China.

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<sup>134</sup> Thomas L. Friedman, "One Nation, 3 Lessons", *Foreign Affairs*, 13 April 2001, <http://www.nytimes.com/2001/04/13/opinion/13FRIE.html>

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