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Policy implications of the accession of China to the  
World Trade Organization for Asia-Pacific countries

by Wook Chae and Hongyul Han



UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION

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# Policy Implications for Asia-Pacific Countries of the Accession of China to the World Trade Organization

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Chae, Wook  
Korea Institute for International Economic Policy, Korea

and

Han, Hongyul  
Hanyang University, Korea

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## **I. Introduction**

China has successfully negotiated with the United States on December 15, 1999 and with the European Union on May 19, 2000 over the matter of its WTO accession. Although the approval processes by the WTO General Council and ratification by China's People's Congress remain undone, China's entry into the WTO is likely to be realized around the end of 2000.

The WTO accession will launch China in the global economy, accelerating its market opening process. The expectation is that this will bring out tremendous changes to international as well as Chinese domestic economy. While developed countries like the U.S., EU, Japan and Canada have been leading the world trade order so far, it is expected that developing countries including China will become much more influential in the multilateral trading system if China joins the WTO. Thus, China will certainly fortify its international political and economic status.

First of all, China will be able to strive for an advanced economy with a new approach to the "reform and open door policy" which has been promoted since 1979. With the entry into the WTO, China will be forced to remove the barriers to trade and investment, improving market access to foreign capital and commodity. Consequently, China's market will expand, with the market function being activated, and foreign enterprises will increasingly advance in the Chinese market. In that process, some domestic industries may suffer from restructuring while overall Chinese economy will be more competitive. Taking it into account that China has already enjoyed MFN status with 140 trading partners, it may not be able to achieve visible export increase for the time being. However, as the market expands in size and market function works effectively, Chinese products will become more competitive internationally, in terms of price and non-price factors. Thus, Chinese products, which are of high price and good quality, will penetrate the world market. It would be worth emphasizing, however, that such effects will come true only if China complies with the WTO rules and bound commitments.

China's entry into the WTO will have a critical impact on the global economy as well.

Primarily, as China promotes "reform and globalization," exports by other countries will rush to China. Then, competition among countries and firms to occupy the huge Chinese market will create further trade, thereby contributing to the world economy. It is also conceivable that China will play an important role in strengthening the efficacy of world trade rules by reforming its domestic institutions in a way that is consistent with international norms.

However, China's entry into the WTO will dramatically change its trading partners, particularly the developing countries. In the short run, developing countries will be able to improve their trade balance with China, as China accelerates its market-opening. In the long run, however, as Chinese products become more competitive in the world market, they are highly likely to make inroads in the market of trading partners. In particular, developing economies in the Asia and Pacific region may be affected mostly because their labor intensive products will have to compete with Chinese commodities. Therefore, unless innovative reform is initiated by those countries, their export will fall behind in competition, and economic growth will be deteriorated.

This article is designed to analyze the economic effects of China's WTO entry on developing countries in the Asia and Pacific region; and to suggest a guidance for their national policies. The article consists of five chapters. Chapter I shows comparative analyses for general economic status and structures of trade and industries in developing countries in the Asia and Pacific region. Chapter II summarizes China's liberalization schedule on the basis of negotiations between China and the United States. Chapter III investigates how China's WTO entry affects developing economies in the Asia and Pacific region. Chapter IV finalizes the article by providing policy implications for developing countries.

## **II. China and AP Developing Economies in World Economy**

### **1. Recent Economic Performances**

Global economic condition has improved since the Asian financial crisis of 1997. Economic growth remained strong in advanced economies and in Asian developing economies. Strong demand in the United States and other advanced economies contributed to the recovery of Asian developing countries from recession. Most of the macroeconomic variables look stable, and the recovery of Asian economies seems to be back on track.

Asian developing economies had continued a significantly high economic growth until they were hit by the currency crisis in 1997. However, after a short period of serious economic and social turmoil, Thailand, the Republic of Korea, Indonesia, Malaysia, and the Philippines – directly affected by the crisis- continued to recover by undertaking macroeconomic stabilization policies and structural reforms, including unilateral liberalization of their trade and foreign investment regimes. Expansion of advanced economies' export markets provided an external environment that is favorable for adjustment, with the United States playing a pivotal role with its the ninth consecutive years of sustained strong output growth.

Despite Asia's high growth rate of 5.9%, which is significantly higher than that of all developing economies(3.8%), growth rates of individual countries varied considerably. Most of East Asian economies grew at high rates. Korea and China were most impressive, growing at 10.7% and 7.1% respectively. Southeast Asian economies slowed a little in 1999, while South Asian countries recorded growth rates higher than the average growth rate of all developing economies. Having experienced serious political instability, Indonesia's recorded growth rate of 0.2%, which is, however, a turnaround after a severe contraction in 1998. Relatively strong performance of most AP developing economies is attributable to factors like export expansion, increased public spending and strong domestic private demands, etc.



External balance has remained sound and the balance of payment crisis seems to be out of sight, mainly thanks to continued export growth, which is due to strong demands in North America. According to Table II-1, summarizing main economic indicators of 1999, external positions of AP economies seem to be comfortable. The current account position as a share of GDP is mostly positive except for some South Asian economies like Pakistan and Sri Lanka. Malaysian foreign exchange reserves continued to rise, reaching up to 30.9 billion US\$, mainly due to sustained current account surpluses. The situation is similar in Thailand, of which gross official reserves are expected to be around US\$ 30 billion thanks to a surplus in merchandise trade and tourism service.

**Table II-1. Economic Indicators of World and AP Developing Economies(1999)**

Region	GDP Growth	CPI	Unemployment	Current Account	Trade(bil \$ U.S)	
					Exp	Imp
<b>World</b>	3.4	3.6	6.3	-0.6	6612.3	6620.9
<b>Advanced</b>	3.2	1.4		-1.1	3500.7	3564.9
<b>Developing</b>	3.8	6.6				
<b>Asia</b>	5.9	2.4		2.3	2012.5	1816.1
Bangladesh	5.2	6.2				
India	4.5	4.7		-1.9	53.7	72.8
Pakistan	2.7	5.7		-2.9	10.9	15.3
Sri Lanka	4.3	4.7				
Indonesia	0.3	20.8	19.1	3.5	57.8	44.8
Malaysia	5.6	2.8	3.7	16.3	96.9	82.6
Thailand	3.2	0.3	4.2	2.6	65.8	57.6
Philippines	3.3	60.7	9.1	2.2	45.7	44.7
Korea	10.7	0.8	6.3	6	169.4	145.3
China	7.5	1.4	3.1		219.7	208.3
Singapore	5.4	0.5	4.6	24.8	155.3	141.6
Taiwan	5.8	0.5	3	3.3	144.8	135.5

Source) World Economic Outlook(IMF) and World Outlook, DRI. 2000

Note. Growth and CPI data are from IMF and others are from DRI.

Overall, the performance of macroeconomic variables including inflation looks stable, and provides basis for optimism on the Asian economies. IMF estimates that per capita incomes of East and Southeast Asian economies are expected to reach pre-crisis level by the end of 2002. According to the long-term forecasts by the World Outlook(DRI), economic growth will continue to remain strong in the year 2005. The forecasted world GDP growth rate is 3.4%, which is significantly higher than that of

1999. The high growth forecast is associated with the high growth of the developing economies. The average growth rate is expected to be 5.2%, while that of Asia remains at 3.9%. Among AP developing economies, Korea and India are expected to moderate from 9.1% and 6.3% in 1999 to 5.3% and 5.7% in 2005.

**Table II-2. Forecasts for 2005 Major Economic Indicators**

Region	GDP Growth	Per Capita	CPI	Unemployment	Current Account	Trade	
						Exp	Imp
<b>World</b>	3.4	6824	3.4		-1.0	1107.06	11307.6
<b>Advanced</b>	2.8		2.4		-1.2	5657.6	5829.6
<b>Developing</b>	5.2		7.2				
<b>Asia</b>	3.9	3015	3.7		0.3	3261.5	3204.9
Bangladesh	5.1	401	6.8				
India	5.7	627	5.8		-2.6	93.6	125.2
Pakistan	5.0	595	5.5		-4.2	17.7	24.8
Sri Lanka	5.4	1214	6.8				
Indonesia	6.0	1292	7.0		-1.0	107.7	105.6
Malaysia	5.5	5763	4.1	4.4	0.6	196.5	190.9
Thailand	6.6	3919	4.7		-5.0	87.6	100.8
Philippines	4.7	1172	5.8	8.3	-3.0	56.5	60.4
Korea	5.3	12841	4.9	4.3	-1.3	801.9	872.9
China	8.1	1460	6.5			507.9	591.3
Singapore	5.9	40383	1.2	2.4	16.7	247.3	221.2
Taiwan	6.4	21583	3.2	2.9	2.2	273.1	262.2

Source) World Outlook, DRI

However, many international organizations like IMF warn that due structural reforms should be undertaken in order to maintain the growth momentum of AP developing economies. Though it seems unlikely to lead to another turmoil, very recent developments both in the world economic environment and inside Asian economies cast some doubts on the future of these economies in spite of their strong macroeconomic performances for the past two years. They are struggling with volatile foreign exchange and stock markets. Structural adjustment is being delayed, making international investors think twice before they make any decisions. Difficulties are coupled with high oil prices. There is growing speculation that the United States' 9<sup>th</sup> consecutive economic boom soon will end. Overall, Asian economies seem to be facing totally different world economic environment from the one in the beginning of the year. In order to avoid another serious recession, Asian economies may have to

learn from the past.

## **2. Structure of World Trade and AP Developing Economies**

The world trade has picked up again since 1999 from the slowdown in 1998. Again, the strong demands of North America and recoveries of the Asian economies were the main forces. According to the WTO, “the recovery in Asia was stronger than expected and led to double-digit real import growth in 1999.” In many countries, a fiscal stimulus, replenishment of inventories and a rebound in the global demand for electronic goods sustained the economic growth. Particularly, the information technology sector and the automobile industry recorded strong global output growth. Within the information technology sector, the unit sales of personal computers rose by 22%, and the dollar value of the global sales of semi-conductors expanded by 18%. One of the most dynamic branches of the global information technology industry in 1999 was mobile phones. It is estimated that worldwide sales of cellular mobile phones reached 283 million units, an increase of two thirds over the 1998 sales.<sup>1</sup> This observation leads us to examine the relevance of export structure of AP developing economies in the rapidly changing world trade structure. As export is the growth locomotive of most of the Asian developing economies, catching up with the global trend will be crucial to maintain their new growth momentum since 1998.

Figure II-1 shows the structural change of the world trade between 1990-1997 by commodity and by region. Overall, Asian trade out-grew total world trade, trade by advanced economies and by all developing economies. The world trade in manufactures grew most significantly during this period. Trade in machinery and transportation equipment is unique, because it is the only sector in which advanced economies recorded the highest growth of trade among various groups of economies. Both advanced economies and the Asian economies recorded the second highest growth in the sector of chemicals and chemical products. In all remaining products, the Asian economies are the most active traders. In short, world trade is being more and more concentrated on advanced economies and Asian Economies. In terms of commodity, trade shares of the industrial and capital intensive products like machinery, transportation equipment, chemicals seem to be ever increasing. This

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<sup>1</sup> WTO Annual Report 2000.

feature of the world trade development suggests that it is more and more plausible to explain international trade flows by theories based on technological aspects and economies of scale, instead of the factor endowment theory alone.

**Figure II-1. Growth of World Trade by Commodity Group**

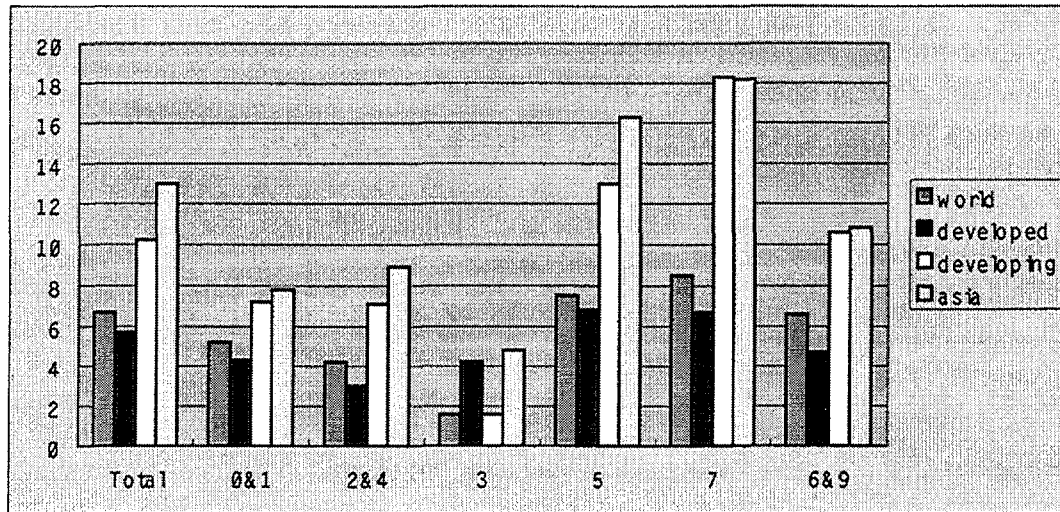


Table II-3 describes the regional structure of trade and changes thereof by commodity group during the period of 1990-1973. EU takes the largest portion of export and import in all categories. For example, shares of EU's export and import of SITC 0&1(Food, Live animals) are 41.7% and 42.4% respectively, mainly due to it's heavy intra-regional trade. However, EU's shares have decreased for most of exports and imports between 1990-1997. United States is both a heavy exporter and importer of manufactured products. Unlike EU, exports and imports of most categories had increased their shares during the same period. While EU lost its export and import shares by 4.5% and 6.1% points, the U.S. had gained its shares by 1.0% and 1.3% points, respectively. Developing Asian economies had increased their shares remarkably. Their shares of total export and import grew to 19.6% and 18.3%, respectively. Exports of the Asian developing economies are highly centered on other manufactured goods of SITC 8. However, exports of machinery and transportation equipment recorded the highest increase while other export shares increased in all categories too. It is expected that rebounding oil prices have led to an increase of world fuel exports in excess of 20%, and above average growth was also recorded for

office and telecom equipment, and automotive products.<sup>2</sup>

**Table II-3. Regional Structure of Trade by Commodity Group**

(%, share of own trade)

SITC	Developed Economies		Developing Economies		EU		US		JAPAN		Developing Asia	
	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.
<b>0-9 Total</b>	66.8	64.9	29.4	29.4	38.5	36.4	11.9	15.5	7.8	5.4	19.6	18.3
All commodities	(-4.5)	(-5.5)	(6.0)	(6.0)	(-4.5)	(-6.1)	(1.0)	(1.3)	(-0.6)	(-0.1)	(6.5)	(5.5)
<b>0&amp;1 Food, live animals,</b>	64.5	66.4	32.3	26.0	41.7	42.4	11.3	9.1	0.5	9.7	13.6	12.2
Beverages, tobacco	(-4.0)	(-4.9)	(3.9)	(3.1)	(-4.1)	(-5.7)	(-1.0)	(0.2)	(0.0)	(0.5)	(2.1)	(3.3)
<b>2&amp;4 Crude materials,</b>	58.4	60.9	35.1	33.1	24.3	35.2	14.3	9.6	1.3	10.7	18.7	21.2
oils and fats,	(-4.8)	(-7.4)	(6.2)	(7.2)	(-4.7)	(-6.5)	(-1.6)	(1.7)	(0.2)	(-2.3)	(5.0)	(5.6)
<b>3 Mineral fuels,</b>	32.7	60.5	56.7	20.3	14.4	30.6	2.9	18.4	0.5	7.6	12.2	11.2
Lubricants	(5.2)	(-1.0)	(0.0)	(-3.9)	(0.4)	(-1.3)	(-0.3)	(1.4)	(0.2)	(-1.5)	(2.4)	(-1.3)
<b>5 Chemicals</b>	79.8	63.7	16.6	31.0	51.3	41.6	13.7	9.7	5.9	3.9	11.4	18.8
	(-3.7)	(-4.8)	(4.8)	(5.0)	(-5.4)	(-6.6)	(0.9)	(2.2)	(0.7)	(-0.5)	(4.8)	(4.4)
<b>7 Machinery and</b>	75.2	64.9	23.0	31.5	40.2	34.2	15.1	18.4	13.6	3.7	19.4	20.2
Transport equipment	(-9.3)	(-7.1)	(10.5)	(7.8)	(-6.7)	(-7.6)	(0.8)	(0.9)	(-3.2)	(0.8)	(8.7)	(7.0)
<b>6&amp;8 Other</b>												
Manufactured goods	61.6	66.5	34.4	28.8	39.6	37.7	8.6	15.4	5.3	5.5	26.8	18.5
	(-7.6)	(-7.3)	(8.0)	(6.9)	(-8.4)	(-8.0)	(1.4)	(1.3)	(-0.7)	(0.2)	(6.4)	(5.7)

Source) UN International Trade Statistics(1999)

Note. Numbers in ( ) indicate % change during 1990-1997

While it is true that developing economies have great stakes in manufactures trade, it is important to note that their shares fall very short of average level of developed economies. Table II-4 shows the trade structures by major trading groups. Looked at total world trade, machinery and transport equipment(SITC) takes a lions share, followed by other manufactured goods of SITC 6&8. Developed economies' export share of machinery and transport equipment(44.4%) greatly exceeds the world average(39.5%), though the export share of other manufactured goods fall little short of the average. This pattern is most conspicuous in the U.S and Japanese trade. The U.S and Japanese export and import shares of machinery and transportation are even greater than the average of developed economies, while those of other manufactured goods are far below them. In contrast, developing Asian economies are net importers of machinery and transportation equipment. Meanwhile, Asian developing economies have increased their share of machinery exports by 10.5% points during 1990-1997,

<sup>2</sup> WTO Annual Report, 2000

while exports share of other manufactured products decreased by 5.7% points. Import shares of machinery and transportation equipment increased significantly and uniquely, implying again that developing economies need to enhance their export structures in consistence with the structural change of world trade. It is moving in right direction, but there still is a long way to go.

**Table II-4. Commodity Structure of Trade by Region**

SITC	Developed Economies		Developing Economies		EU		US		JAPAN		Developing Asia	
	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.	Exp.	Imp.
	<b>0-9 Total</b>	100	100	100	100	100	100	100	100	100	100	100
All ommodities												
<b>0&amp;1 Food, live animals,</b>	7.5	8.0	8.6	6.9	8.5	9.1	7.4	4.6	0.5	14.2	5.4	5.2
Beverages	(-0.8)	(-0.7)	(-1.8)	(-1.5)	(-0.7)	(-0.7)	(-2.3)	(-0.8)	(-0.1)	(-0.2)	(-2.1)	(-0.8)
<b>2&amp;4 Crude materials,</b>	3.8	4.1	5.2	4.9	2.8	4.2	5.3	2.7	0.7	8.7	4.2	5.1
Oils and fats,	(-0.8)	(-0.9)	(-1.2)	(-0.8)	(-0.7)	(-0.9)	(-2.2)	(-0.2)	(0.0)	(-3.5)	(-1.2)	(-1.2)
<b>3 Mineral fuels,</b>	3.8	7.3	15.0	5.4	2.9	6.6	1.9	9.3	0.5	11.1	4.9	4.8
Ludricants and	(-0.4)	(-2.3)	(-11.6)	(-5.9)	(-0.7)	(-1.7)	(-1.4)	(-3.8)	(0.1)	(-7.0)	(-3.3)	(-5.9)
<b>5 Chemicals</b>	11.1	9.2	5.3	9.8	12.4	10.7	10.8	5.8	7.1	6.9	5.4	9.6
	(0.7)	(0.6)	(0.9)	(0.0)	(0.7)	(0.7)	(0.4)	(1.1)	(1.6)	(0.0)	(1.0)	(-0.3)
<b>7 Machinery and</b>	44.4	39.4	30.9	42.3	41.3	37.0	50.3	46.8	69.1	27.6	39.0	43.6
Trans. Equipment	(2.7)	(3.4)	(12.1)	(6.7)	(2.9)	(2.4)	(4.2)	(3.6)	(-1.6)	(8.9)	(10.5)	(7.3)
<b>6&amp;8 Other Manufactures.</b>	26.0	29.1	33.2	27.8	29.2	29.4	20.5	28.2	19.3	29.2	38.8	28.7
	(-1.9)	(-1)	(0.9)	(1.0)	(-2.9)	(-1.4)	(1.6)	(-0.1)	(-1.2)	(2.0)	(-5.7)	(0.2)

Source) UN International Trade Statistics(1999)

Note. Numbers in ( ) indicate % change during 1995-1998

This observation contradicts the traditional view that liberalization of manufactures trade is in the interest of developed countries. In fact, manufacture exports account for almost three quarters of the developing country exports. Some projections show that manufactures share would increase by 80% in 2000. Such a change in the structure of merchandise exports has potentially important implications for the AP developing economies with China's accession to the WTO. Not only the average developing economies gain from the liberalization of the Chinese market, but also, they, as a group including China, would have a greater stake in the next round of multilateral trade negotiations for the liberalization of these products.

Of course, export structures of AP developing economies are not homogeneous. The

differences in the export structure will lead to different impacts on their exports to the Chinese market. Table II-5 summarizes export shares and change thereof between 1990-1997. First, South AP economies are relatively more dependent on primary exports. The exports of primary products (SITC 0) took the share of 16.88% and 19.83% for India and Sri Lanka, respectively. These figures are significantly higher than those of other AP economies, except for Thailand (18.08%). An important feature of Bangladesh's trade is that garment is a dominant export industry. In 1998, textile and clothing took over 80% of total exports, replacing jute exports from the leading exports which recorded around 6%. In the case of India, the share of primary exports increased by 2.95% during the period, while share increases of major manufacturing goods (SITC, 6, 7, 8) remained at around 1% point. Shares of exports of light-industry products including leather, rubber and machines etc. and miscellaneous manufactured articles including apparel, footwear, etc. are 39.06% and 19.07% respectively, while those for Sri Lanka are 15.50% and 53.19%.

**Table II-5. Export Structure by Commodity Group of AP Developing Economies(1990-1997)**

Exports	0		1		2		3		4		5		6		7		8		9	
	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ	1997	Δ
Bangladesh																				
India	16.8	2.9	0.46	-0.4	4.9	-4.9	1.7	-1.3	0.8	0.55	8.1	0.7	39.1	1.8	7.48	0.06	19.1	0.8	1.6	-0.4
Pakistan																				
Sri Lanka	19.8	-12.9	1.23	0.9	4.2	-3.5	0.7	-0.8	0	-0.4	0.87	-0.15	15.5	2.1	2.56	-0.3	53.2	17.2	1.9	-2.3
Indonesia	7.56	-1.3	0.46	-0.1	10.2	3.5	25.8	-17.9	3.2	-1.52	3.46	-1.14	21.8	-2.1	10.0	8.7	17.4	6.96	0.2	-0.3
Malaysia																				
Thailand	18.0	-10.1	0.36	-0.03	4.5	-1.2	2.2	1.3	0.1	0.09	3.71	2.29	15.5	-2.9	39.2	16.9	13.4	-8.1	2.98	1.8
Philippines																				
Korea	1.95	-1.1	0.14	-0.05	1.3	-0.2	3.9	2.9	0.03	0.03	7.83	3.97	21.4	-0.7	50.0	10.7	8.84	-19.7	4.59	4.3
China	6.05	-4.5	0.57	0.02	2.3	-3.4	3.8	-4.6	0.35	0.09	5.6	-0.4	18.8	-1.4	23.9	14.9	38.6	18.1	0	-18.7
Singapore	1.73	-1.1	1.49	0.03	1.0	-2.1	8.7	-9.4	0.27	-0.5	6	-0.27	5.6	-1.4	65.9	15.8	7.7	-1.2	1.5	0.2
Taiwan																				

Note. Numbers in the right columns of each economy indicates % change between 1990-1997.

Southeast Asian economies have similar export structure to each other. Although exports of manufacturing goods are most important, primary exports also have significant shares. However, the export structures of Southeast economies are in the

process of a rapid change. In Thailand, the share of primary export decreased by more than 10% points during the last decade, while that of machineries and transportation equipment(SITC 7) increased by almost 17% points. Indonesian exports of these products increased by 8.7% points, though the contraction of primary export is relatively small. In Philippines, merchandise exports and their contribution to GDP increased significantly. Also, the export structure continued to shift from primary to manufactured products, of which shares reached to 86% in 1997. Major exports include electronics, automotive products and apparels.

Finally, the export structure of Asian middle income economies is quite different from other AP developing economies. For instance, Korea's export is concentrated on machinery and transportation equipments(SITC 7), with total share of manufacture exports over 90%. Between 1997-1990, the share of heavy industry gained 10.7% point while shres of light industrial products shrank considerably.



### **III. China's Liberalization Schedule**

#### **1. Basic Policy Directions**

China has achieved economic growth by 10% annually and is considering the first 10 years of the 21<sup>st</sup> century as a strategic period for heading towards an advanced economy. Since China promulgated the first explicit industrial policy in 1989, its economic policies have been oriented toward industrial restructuring. While striving to strengthen the status of agricultures by developing the rural economy, it has promoted the development of so-called 'pillar' industries such as those of machineries, electronics, petroleum and raw chemicals, automobiles, and construction. Such industrial restructuring has been proceeded also in relation to foreign trade. The foreign trade policy has been made to encourage exports of agricultural products with comparative advantages, home electronic appliances, and some high value-added products. Encouragement was also granted to imports of crucial parts, equipment and technologies.

With such trade policy, China's trade volume has substantially grown so that it becomes the 9<sup>th</sup> largest trading nation in the world. Furthermore, as China has been successfully transforming its economy from a centrally planned autarchy into a market-based system, it became fairly open to trade and investment. Since the early 1990s, China has gradually cut its tariff rate from over 40% to the current 15%. As for non-tariff barriers, after the landmark promulgation of the "Law of Foreign Trade of the People's Republic of China" in 1994, China accelerated its elimination of license requirements and most of import quotas and introduced an automatic import licensing system.<sup>3</sup>

In its bid for the membership of the WTO, China has made comprehensive commitments to liberalizing trade and investment. Therefore, with China's entry into the WTO, many of the trade barriers are expected to be further lowered or removed and foreign enterprises in China will have a better chance to gain 'national treatment'.

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<sup>3</sup> Lu, Ding, 'Industrial Policy and China's Participation in Globalization', China-Korea Economic Forum 2000, p.9.

'Five-year Plan for National Economic and Social Development and the Long-term Target for the Year 2010' defines the new directions of state intervention and provides a blueprint of national development into the 21st century (Table 1).<sup>4</sup> According to the outlines, economic reform and industrial restructuring must be China's main policy instruments to ensure a sustainable and rapid economic growth in the globalized economy. In specific, institutional building for a market economy and development of the 'pillar industries' will be the major policy agenda in coming years. Furthermore, it is expected that China will accelerate the plan upon its entry to the WTO in response to the comprehensive market-openings. Accordingly, China will shift from the centrally planned economy to the socialist market economy where the market plays a fundamental role in resource allocation, and from an quantitative growth mode to an qualitative growth mode which is driven by increasing efficiency and productivity .

**Table III-1 Objectives for the Year 2010**

- GDP to be doubled the year 2000 figure.
- Control population within 1.4 billion and enable people to lead an "even more comfortable life".
- Establish "a relatively complete socialist market economy," a sounder macroeconomic control system with better agility and effectiveness, and a regulatory framework more in compliance with the rule of law.
- Establish a modern enterprise system for state-owned enterprises and develop a number of internationally competitive large enterprises and business groups.
- Optimize industrial structure by:
  - Enhancing commercialization and specialization in agriculture;
  - Building up a group of national infrastructure projects and matching development of infrastructure and basic industries to national economic growth;
  - Promoting pillar industries and making them the major driving force of economic growth;
  - Increasing markedly the proportion of the tertiary sector in the national economy and its service function.
- Promote a more co-ordinated development of regional economies and gradually narrow the gap in development between different regions.

Source: Lu(2000), p.6.

<sup>4</sup> Those outlines were approved at the 4<sup>th</sup> session of China's 8<sup>th</sup> National Peoples' Congress in March, 1996.

## **2. Overviews of U.S.-China Agreement**

### **Agricultures and fisheries**

By joining the WTO, China is committing to establish a “tariff-only” import regime; all non-tariff barriers will be eliminated. Any other measure, such as inspection, testing, and domestic taxes must be applied in a manner that is consistent with WTO rules requiring a transparent and non-discriminatory system and all health measures must be based on sound science. The tariff on agricultural products will decline from an overall average of 22% to 17.5%<sup>5</sup> (Table 2), and that of fisheries will be reduced from 25.3% to 10.6% by January 1, 2005. For grains, tariff rates on sorghum will be reduced from 3% to 2%, and those on barley malt will be reduced from 30% to 10% by 2004. Tariff concessions on key dairy products that China will phase in by 2004 are as follows: cheese from 50% to 12%, yogurt from 50% to 10%, lactose from 35% to 10%, ice cream from 45% to 19%, and other food preparations from 25% to 10%. And for key meat products, tariff concessions by 2004 are as follows; frozen beef cuts from 45% to 12%, frozen beef tongue and offal as well as frozen pork cut and offal from 20% to 12%, and frozen chicken and turkey parts from 20% to 10%. Furthermore, tariffs on specialty crops such as vegetables, nuts, and citrus will be reduced from 13-30% to 10-15%, 30-35% to 10-20%, and 35-40% to 12-15%, respectively .

As for tariff-rate quotas(TRQ), China, like many WTO members, will use a TRQ system (refer to Table 3) and state trading for certain sensitive commodities such as wheat, corn, rice, cotton, and soybean oil. China will permit any entity including foreign enterprises to have the right to import and distribute most agricultural products including fisheries, which is to be phased in over a three-year period. China has also committed not to grant export subsidies for agricultural products when it joins the WTO, while committing to cap and reduce trade-distorting domestic subsidies.

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<sup>5</sup> The average duty on agricultural products of U.S. priority interest will fall from 31% to 14%.

**Table II-2 Schedule of Tariff Reduction on Agricultures**

Items		Currehnt Rates(%)	Rates to be Reduced	Due years
<b>Averages</b>		22	17.5	Jan. 1, 2005
Grains	Sorghum	3	2	2004
	Barly Malt	30	20	
Dairy	Cheese	50	12	2004
	Yogurt	50	10	
	Lactose	35	10	
	Ice Cream	45	19	
	Other Food Preparations	25	10	
Meats	Frozen Beef Cuts	45	12	2004
	Forzen Beef Tongue and Offal	20	12	
	Frozen Pork Cuts and Offal	20	12	
	Frozen Chicken and Turkey Parts	20	10	
Vegetables	Lettuce	16	10	2004
	Cauliflower	13	10	
	Broccoli	13	10	
	Canned Tomato Paste	25	20	
	Tomato Ketchup	30	15	
Nuts	Shelled Almonds and Hazelnuts	30	10	204
	Pistachios	35	10	
	Shelled and Canned Walnuts	30	20	
Citrus	Oranges, Lemons, Grapefruits	40	12	2004
	Grapefruit Juice	35	15	
Other Fruits	Apples, Pears, Cherries, Peaches	30	10	2004
	Plums, Raisins	40	10	
	Grapes	40	13	
	Wine	65	20	
	Other Fruits and Nuts	30	20	
	Grape Juice	35	20	
	Water-based Drinks with Sugar	65	20	
Other Products	Ginseng	40	10	2004
	Cigarettes	65	25	

Source: USTR(1999).

**Table III-3 Schedule of TRQs on Grains**

(Unit: mt)

Items		Initial TRQ	2004 TRQ	Private Share	1998 Total Imports
Wheet		7,300,000	9,636,000	10%	2,000,000
Corn		4,500,000	7,200,000	25%, grows to 40%	250,000
Rice	Total	2,660,000	5,320,000		250,000
	Short/Med Grain	1,330,000	2,660,000	50%	
	Long Grain	1,330,000	2,660,000	10%	

Source: USTR(1999).

### Industrial Products

China has made a comprehensive commitment to reduce tariff or non-tariff barriers in the industrial sector. The average tariff rates are to be reduced to 9.4% with some

major items to be lowered to 7.1% (Table 4), and the quotas in general will be eliminated by 2002 or at least by 2005. The most remarkable changes were seen in the areas of autos and information and technology products. According to the agreement, China will lower the tariff rates of automobiles from 80-100% to 25% by 2006 after the WTO accession (Table 5), cutting those of related major components from 23.4% down to 10%, and eliminate import quota system by 2005. In particular, quotas on autos will be phased out by 2005, growing 15% annually until eliminated. China also agreed to sign on the Information Technology Agreement(ITA) on accession, thereby committing to eliminate tariffs on all products covered by the ITA by January 1, 2005 .

**Table III-4. Schedule of Tariff Reduction on Industrial Products**

Items	Current Rates(%)	Rates to be Reduced(%)	Due Years
<b>Averages</b>	17	9.4	2005
Automobiles	80-100	25	2006
Auto Parts	23.4	10	2005
Information Technology Products	13	0	Jan. 1, 2005
Civil Aircraft	14.7	8	Jan. 1, 2002
Construction Equipments	13.6	6.4	Jan. 1, 2004
Medical Equipments	9.9	4.7	Jan. 1, 2003
Scientific Equipments	12.3	6.5	Jan. 1, 2003
Pharmaceuticals	9.6	4.2	Jan. 1, 2003
Chemicals	14.74	6.9	Jan. 1, 2005
Fertilizers	6	4	Upon accession
Cosmetics	45	10 or 15	2004 or 2005
Textiles & Apparels	25.4	11.7	Jan. 1, 2005
Steel Steel Products	10.3	6.1	Jan. 1, 2003
Furnitures	22	0	Jan. 1, 2005
Lumber	15-25	12-18	Jan. 1, 2005
Paper & Paper Products	14.2	5.5	Jan. 1, 2005

Source: USTR(1999).

**Table III-5 Schedule of Tariff Reduction on Autos**

(Unit: %)

Rate	2000	2001	2002	2003	2004	2005	1/2006	7/2006
100%	77.5	61.7	50.7	43.0	37.6	30.0	28.0	25.0
80%	63.5	51.9	43.8	38.2	34.2	30.0	28.0	25.0

Source: USTR(1999).

Other items in which mostly developed countries are concerned such as air craft, equipments, and pharmaceuticals will also go through a substantial tariff reduction. For civil aircraft, tariffs on all items in Annex 1 of the Agreement on Trade in Civil Aircraft will be bound and reduced from the current average rate of 14.7% to a final average rate of 8% starting upon China's accession and with most restrictions completed by January 1, 2002. In particular, quotas and licenses will be eliminated

upon accession for all items in the Agreement on Trade in Civil Aircraft. Tariffs on equipments such as construction equipments, medical equipments, and scientific equipments are to be reduced from 13.6% by over 50 percent to 6.4% by January 1, 2004, from 9.9% to 4.7% by January 1, 2003, and from 12.3% to 6.5% by January 1, 2003, in respected orders. China will reduce its average tariff on pharmaceuticals by 60% from its current average tariff of 9.6% to 4.2% by January 1, 2003.

Besides, tariffs on the products such as chemicals, furniture, paper, steel, and textiles may be of developing countries' concern in general but at somewhat varying degrees. According to the agreement, China will reduce tariffs on chemicals by more than 50% by January 1, 2005, with the average rate of 14.74% being reduced to a final average rate of 6.9%. In specific, China will reduce its tariffs on fertilizers and cosmetics, from 6% to 4% upon accession and from around 45% to 10% or 15% by 2004 or 2005, respectively. Tariff reductions on chemicals involve full implementation of more than two-thirds of the products in the Tariff Harmonization Agreement of the Uruguay Round. Probably, products of the developing countries' greatest concern may be textiles and apparel which will also go through a substantial tariff reduction. Average tariff on those items will be reduced from 25.4% to 11.7%, which will commence upon accession and will be completed by January 1, 2005. Most quotas on priority U.S. exports will be eliminated upon accession, except that those on thirty yarn, synthetic filament tow, and fiber products will be eliminated after one year. Tariffs on steel and steel products, another important item to some developing countries, will be reduced from 10.3% to 6.1% by January 1, 2003. A striking tariff reduction is to be made on furniture items, too. China has committed to reduce its current average tariff rate of 22% to 0% on all furniture items covered by the Uruguay Round sectoral initiative. Reduction will commence upon accession and will be fully implemented by January 1, 2005. While tariffs on lumber will be lowered from 15-25% to 12-18%, those on paper and paper products will be reduced from 14.2% to 5.5% by January 1, 2005.

### **Services**

China's accession to the WTO will certainly contribute to the removal of various restrictions in service sectors. In the agreement with the United States, for example, China has made commitments to phase out most restrictions in a broad range of

service sectors, including telecommunications, distribution, banking and insurance, professional services such as accountancy and legal consulting, and audiovisual services, etc (Table III-6).

For telecommunication services, the Chinese government has decided to lift geographical limitation of beepers and value-added services within 2 years, PCS within 6 years following China's accession to the WTO. Foreign service suppliers are allowed to hold 30% foreign equity share upon accession, 49% after one year, 50% after two years in the area of value-added services. Foreign service suppliers will be also able to provide all analogue/digital cellular services and PCS, and they are allowed to hold 25% foreign equity share one year after accession, 35% after 3 years, and 49% after 5 years of accession. While there is no specific commitment or relevant domestic rules on regarding portal-site management and contents provider, the Chinese government has been publicizing the plan to open those markets in the form of joint-ventures.

**Table III-6 Liberalization Schedule of Major Service Sectors**

Sectors	Foreign Equity Shares	Geographical Limitations
<b>Telecommunication</b>		
Value-added Service	30% upon accession, 49% after 1 year, 50% after 2 years (of accession)	No restrictions after 2 years (of accession)
Mobile Voice and Data Services	25% after 1 year, 35% after 2 year, 49% after 5 years	No restrictions after 5 years
Domestic and International Services	25% after 3 years, 35% after 5 years, 49% after 6 years	No restrictions after 6 years
<b>Distribution</b>		
Wholesale and Commission Agents Services	Joint ventures within 1 year, foreign majority equity share within 2 years, wholly owned subsidiaries within 3 years	No restrictions within 2 years
Retails	No restrictions within 3 years	No restrictions within 3 years
Franchising	No restrictions within 3 years	No restriction within 3 years
<b>Banking</b>	Licensed with certain thresholds and choose legal form after 5 years	
<b>Insurance</b>		
Non-Life Insurance	Branch 51% upon accession, wholly-owned subsidiary within 2 years	No restrictions within 3 years
Life Insurance	50% upon accession	No restrictions within 3 years

Source: USTR(1999)

China also agreed to phase out restrictions for all products in distribution services within 3 years. Foreign service suppliers will be permitted to establish joint-ventures within one year of accession, and foreign majority equity share will be allowed, with

all geographical and quantitative restrictions eliminated, within two years after accession.<sup>6</sup> Even in retailing services, within 3 years from the date of accession, there will be no restrictions on equity, geographic areas, or on the number of service suppliers.

According to the agreement, China will gradually expand the scope and geographic opportunities for foreign banks to conduct local currency business. For example, local currency business with foreign clients will be permitted upon accession, with Chinese enterprises two years after, and with Chinese individuals five years after accession. For geographic restrictions, local currency banking will be permitted in four cities upon accession, four additional cities will be permitted each year thereafter, and nationwide access five years after accession. However, foreign currency business will be allowed without geographic restrictions on accession. On the other hand, China will phase out all geographic restrictions on the insurance market within 3 years of accession. In particular, joint-ventures with partner of choice at 50% equity share will be permitted upon accession for life insurance. While foreign service suppliers of non-life insurance will be permitted to establish branches and joint-ventures at 51% equity share upon accession, wholly-owned subsidiaries will be permitted within a year from date of accession.

China has agreed on market access and national treatment for accounting, auditing, and bookkeeping services. Foreign accounting firms will be permitted to affiliate with Chinese firms and enter into contractual agreements with their affiliated firms in other WTO member countries. These firms must be represented by Certified Public Accountants(CPA) licensed by Chinese authorities; however, existing accounting firms are exempted from this requirement. CPA licenses will be issued on a national treatment basis where applicants will be informed of results in writing no later than 30 days after submission of their application. For legal services, foreign firms will be able to provide services in the form of a profit-making representative office, giving advice on international conventions and practices, and the law of other WTO members in which the lawyer is licensed to practice. While they are not allowed to

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<sup>6</sup> Within three years from the accession, foreign service suppliers may establish wholly owned subsidiaries.



employ Chinese nationals as lawyers for the practice of Chinese law, it can enter into long-term “entrustment” contracts providing for close working relationship with firms practicing Chinese law.<sup>7</sup> All geographic and quantitative restrictions will be phased out within one year of China’s accession, which means that foreign firms can open more than one office anywhere in China.

An agreement was also made to open the Chinese audiovisual market. Foreign service suppliers will be permitted to establish joint ventures with equity share up to 49% which will distribute audiovisuals. Furthermore, 40 movies will be imported upon accession, while 50 movies will be imported within 3 years.

### **Others**

China’s commitments to eliminate non-tariff measures and certain conditions on exports and investment all enter into effect immediately upon China’s accession to the WTO. According to the commitments, China will eliminate the requirements of foreign-exchange balance, local contents and export performance, implementing the WTO Agreement on Trade-Related Investment Measures(TRIMs). China has also agreed that the government will not condition its approval of an investment on whether a company provides offsets, transfers technology, uses locally produced goods, or conducts research and development in China.

In addition, China has confirmed the application of WTO rules to state-owned enterprises and extended those disciplines to state-invested enterprises where the government has an equity interest. Under these commitments, China’s state-owned and state-invested enterprises are required to buy and sell based on commercial considerations, such as quality and price.

### **3. Assessment of Liberalization Schedule**

A landmark deal on U.S.-China trade promises to open up one of the world’s largest economies to unprecedented foreign competition. First of all, China has committed to

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<sup>7</sup> The Chief representative of a foreign law firm must be a partner or equivalent in a law firm from a WTO member country. All representatives must be a member of the bar in a WTO member country, possess three years experience outside of China, and reside in China no less than six months each year.

conduct a substantial reduction in tariffs and remove most quotas on both agricultures and industrial products. Many sectors previously considered off-limits, including banking and telecommunications, will be forced to prepare for competition from bigger and stronger foreign companies in two to five years.

While China maintained high tariff rates of 40% or higher in early 1990s, they were substantially reduced to the average rates of 16.8% by 1999. The tariff rates will be further reduced to 10% by 2005 according to the agreement. Some researches have estimated that such tariff-cuts will bring about an additional increase in China's imports by about 18-20 billion U.S. dollars in 2005.<sup>8</sup> So, the China's trade volume is expected to reach more than 600 billion U.S. dollars in that year, which is almost twice as big as the level of 1998. Furthermore, as China will establish a "tariff-only" import regime by eliminating quotas on most products, price mechanism will work effectively through the market in which consumers benefit from a wider choice of products at cheaper prices.

A more striking and surprising outcome from the deal is China's comprehensive commitments to phase out restrictions in a broad range of service sectors over a relatively short period. It is striking because foreign service business in China is strictly limited. For example, China currently not only limits foreign banks to foreign currency business in selected cities and to foreign customers only, but also permits foreign securities firms to trade only a limited number of stocks. Similarly, China allows selected insurance companies to operate in China on a limited basis in two cities. Furthermore, foreign service suppliers are prohibited from providing telecom services in China, and companies are generally prohibited from distributing imported products or providing related distribution services such as repair and maintenance services. Such restrictions on service sectors will start to be removed right upon accession to the WTO, being phased out over the 5 year-period in general.

While these liberalization measures, removing or relaxing tariff or non-tariff barriers,

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<sup>8</sup> Yoo, Jin-Seok, "China Accession to the WTO and Its Impacts", Issue paper, Samsung Economic Research Institute, 1999.

Rosen, Daniel H., "China and the WTO: An Economic Balance Sheet", International Economic Policy Briefs, Institute for International Economics, 1999.

will certainly benefit almost all trading partners of the world, it is highly likely that developed countries, in particular, the United States will gain the most benefits. This is so, because the commitments were made to favor the products or services of U.S. priority interest. For example, the average tariff rates on agricultural products of U.S. priority interest are to be reduced from 31% to 14%, compared to the overall average rates declining from 22% to 17.5%. Furthermore, China will be required to eliminate export subsidies and provide increased import quotas on wheat, corn, rice and cotton for the United States. Similarly, while the average tariff rates on overall products are to be reduced from 17% to 9.4%, the major products in which the United States has the priority interest will fall to 7.1%. Autos, aircraft, medical or scientific equipments, and pharmaceuticals may be typical examples. China's liberalization schedule will certainly favor the United States even in relation to service sectors, because China committed to open up the service sectors mostly in which the United States have comparative advantage. As a result, it is expected that the U.S. banks, insurers, telecommunication firms, and film exporters will rush to China after its accession to the WTO in order to preoccupy its huge market. However, other developed countries will also gain from China's market-opening because they have, in general, similar industrial structure with the United States.

It should be also worth mentioning that even developing countries will obtain benefits directly or indirectly from such liberalization. As the United States and other developed countries accelerate their exports of value-added products to China, demand for raw materials will surge, from which developing countries can expand exports of raw materials or related intermediate goods. It is quite plausible that the price of those materials or intermediate goods may rise as the issue of environmental protection or preservation of natural resources become their priority concerns. This will also provide developing countries with the favorable terms of trade in international markets. Such effects are expected mainly for the products such as textiles, steel, lumber, paper, and furniture. They can also expand the exports of some agricultural products, in particular, the specialty crops to China.

However, China's liberalization in service sectors may not directly affect developing

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economies at least in the short run. The only possibility is that they can induce more foreign direct investment from developed countries who are willing to take advantage of cheaper rents or labor costs as well as geographical condition. The industrial structure of South Asian economies supports this view. The shares of primary products in total value added are 32%, 25%, 22% and 18% in the order of Bangladesh, India, Pakistan and Sri Lanka. On the other hand, the shares of financial sector, one of the major areas of service trade, and transportation and communication take less than 10% in total. Since exports by South Asian countries are centered mostly on some primary and manufactured products, the benefits from China's liberalization would be greatest in the related areas. For example, more than a half of exports by Pakistan are cotton-based exports. The situation is more or less similar in other South Asian countries; exports of some manufactures take a dominant share, being in particular concentrated on several light industrial products.

While the situation is quite different in some countries of other Asian regions such as Singapore, Chinese Taipei, and Korea, it is expected that China's liberalization in service sectors will have minimal impacts on most developing economies when the competitiveness of their service industries is considered.

There is another challenge against AP developing economies in general. China's accession to the WTO ensures that MFA quota imposed annually will be abolished by 2005. Though it is not clear who will be the winner in the freer trading environments for textile and clothing, major exporters of these products in this region will be exposed to a fiercer competition with China. While MFA quota is already in the process of elimination, it is still too early to assess the effects because no meaningful liberalization is made yet. Presumably, the elimination of the MFA quota would divide the developing countries into higher cost and lower cost supplier. For instance, Korea, Chinese Taipei and Hong Kong will be most negatively affected because they currently have fairly sufficient quota for exports and relatively high wage rates. Of course, it is also possible that the new and small suppliers would be squeezed out with abolition of protection provided by MFA quota. This argument is based on the productivity difference between large quota holders and small suppliers.<sup>9</sup>

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<sup>9</sup> John Whally(1995)

In these respects, our focus in the following chapter will be made on somewhat detailed analyses on the impacts of China's accession to the WTO on AP developing economies. First, we will see which areas or commodities are of major export interests for AP developing economies. For that purpose, the shares in the world major export markets and comparative advantages of AP countries will be analyzed. Secondly, we will analyze the details of how the tariff liberalization affect exports of AP developing economies to the Chinese market. The analyses will be based on the U.S.-China bilateral agreement. Thirdly, we will consider the issue of trade in textile and clothing because MFA quota elimination will take one of the most immediate and foreseeable impacts on the exports of AP developing economies in coming years.

## IV. Impacts on AP developing economies

### 1. Areas of Export Interests for AP Developing Economies

Few suppliers such as Japan, U.S., Chinese Taipei and Korea dominate China's import market. The aggregated import share of these economies is over 60% of total Chinese imports. Compared with the import structures of other major markets, this is a striking feature. In the markets of the U.S., EU and Japan, top 5 suppliers' shares are around 50%. It is most attributable to significantly high shares of Japan, Korea and Chinese Taipei, which are the geographically nearest economies to China, implying that explanation based on the gravity model of trade flows may be relevant than the traditional resource based international trade theory.

**Table IV-1. Top 5 Suppliers in Major Markets (1998)**

Markets	Top 5 Suppliers(shares in Chinese Market)				
United States	Canada (18.41%)	Japan (13.44%)	Mexico (10.15%)	China (8.17%)	Germany (5.39%)
European Union	U.S (17.56%)	Japan (10.31%)	China (6.99%)	Germany (5.42%)	Canada (5.30%)
Japan	U.S (23.99%)	China (13.35%)	Australia (4.68%)	Korea (4.30%)	Indonesia (3.90%)
China	Japan (20.16%)	U.S. (12.03%)	Chinese Taipei (11.85%)	Korea (10.7%)	Germany (5.0%)

Source) UNCTAD Trains 2000

Performances of AP economies in the Chinese market are greatly different from each other. While India takes 1.39% of total EU market and 0.94% of total U.S market, it takes only 0.64% in the Chinese market. Many South and Southeast AP economies take significantly higher shares in major export markets than those in the Chinese market. In contrast, Korea and Chinese Taipei show dramatically different bilateral trade flows with China from those of other AP developing economies. The import share by Korea in Chinese market is 10.7% while it is less than 3% in the U.S. market, and Chinese Taipei's share reaches almost 12% while it's share in the U.S remains at the level of 3.7%. This pattern of bilateral trade flow between AP developing economies and China shed some lights on the possible effects of China's liberalization

policy.

**Table IV-2. Market Shares of AP Economies in Major Markets(%)**

	Bangladesh	India	Pakistan	Indonesia	Malaysia	Philippines	Thailand	Taipei	Korea
U.S	0.21	0.94	0.20	1.09	2.12	1.32	1.52	3.70	2.68
EU	1.39	1.39	0.34	1.27	1.62	0.63	1.33	2.65	2.17
Japan	0.04	0.79	0.11	3.90	3.04	1.56	2.83	3.53	4.30
China	0.02	0.64	0.28	1.75	1.90	0.37	1.72	11.85	10.7

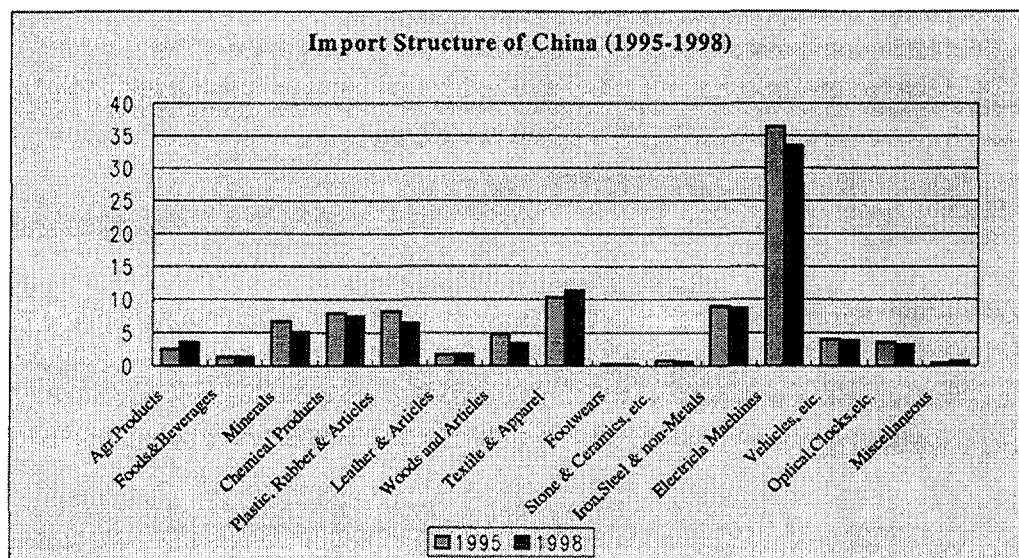
Source) Same as the Table IV-1

Small suppliers in the South Asian economies may expect greater opportunities in the Chinese market. If, for example, Bangladesh takes 0.21% of market share in the U.S., it would be simply unreasonable to assume that its share will remain at the current level after the liberalization of the Chinese Market. It is a price-elasticity issue; exports by these economies competing with the Chinese domestic suppliers will have better price competitiveness after China's tariff cuts. However, in our discussion in chapter II, we have noted that the world economy is fast concentrating on high value-added and capital-intensive products. As seen in Figure II-1, the Chinese import structure seems to follow the global trends. Therefore, for AP developing economies to catch up with the development process of advanced economies, these countries may have to align their industrial and export structures to be consistent with changes in world trade structure in a longer term. In order to examine to what extent China's accession to the WTO would create export opportunities for AP developing economies, we may have to consider China's liberalization plan with regard to product specific performance of these economies in China.

Table IV-3 shows that groups of AP developing economies have different stakes in the Chinese market compared to the U.S market. South Asian economies have very limited market shares in industrial products(SITC 6-8) in China, while they have meaningful shares in the U.S. India's market shares in the U.S are 3.24% and 1.59% for SITC 6 and 8, respectively. However, its export shares of these categories in China are almost insignificant. Even in the category of SITC 7(machinery and transportation equipment), India's relatively limited share in the U.S. is four times bigger than that in China. On the contrary, India's share of primary imports in China is about four times

bigger than its share in the U.S. It implies that these countries would gain much benefit from the liberalization of markets for primary products. Undoubtedly, manufacture is another area of interests for India considering its significant increase of shares in both markets.

**Figure IV-1. Import Structure of China**



**Table IV-3. Market Shares of AP economies in China and USA by Commodity**

China	0	1	2	3	4	5	6	7	8	9
Bangladesh	0.17		0.13				0.03		0.03	
	0.14		0.04			-0.07	-0.04	0.00	0.01	
India	6.50	0.01	2.99	0.05	2.18	0.24	0.71	0.02	0.19	0.02
	6.04	0.01	1.25	-0.13	1.08	-0.02	0.42	-0.01	0.13	0.02
Pakistan	0.22		0.15	0.04		0.00	1.16	0.00	0.00	
	0.01		-0.04	-0.14		0.00	0.54	0.00	0.00	
Indonesia	2.35	0.05	4.20	6.83	8.41	1.16	3.14	0.18	0.18	
	1.02	0.05	2.07	-7.99	5.74	-0.47	1.38	0.12	0.04	
Malaysia	0.69	0.29	2.71	1.85	32.81	1.27	1.77	1.55	0.47	0.01
	0.03	0.06	0.36	-0.09	4.81	0.23	0.60	1.01	0.33	-0.01
Thailand	5.89	0.82	2.71	0.87	0.07	2.51	1.08	1.66	0.53	0.01
	-6.13	0.39	-0.13	0.72	-0.06	1.48	0.33	1.66	0.29	0.01
Philippines	1.89	0.03	0.19	0.67	2.19	0.13	0.30	0.38	0.11	
	1.35	-0.08	-0.22	-1.56	1.80	-0.27	0.16	0.34	0.05	
Singapore	0.28	1.82	0.19	13.82	0.63	2.93	0.52	3.96	2.23	8.22
	0.00	1.62	-0.27	-9.98	-1.30	0.90	-0.09	1.32	1.24	-4.99
Korea	1.96	0.63	4.88	16.01	0.29	18.36	18.28	5.77	7.60	0.49
	0.88	0.51	-0.16	8.31	0.26	4.78	4.94	1.33	1.17	0.49
Chinese Taipei	0.68	0.67	4.64	0.60	0.28	16.22	19.96	9.95	10.57	0.48
	-0.01	0.09	-0.16	-0.11	0.03	-0.21	-2.42	-0.77	-4.09	-5.84



United States	0	1	2	3	4	5	6	7	8	9
Bangladesh	0.26	0.01	0.01			0.00	0.08	0.00	1.02	
	0.03	0.01	0.00			-0.03	-0.01	0.00	0.11	
India	1.77	0.20	1.49	0.00	2.63	0.84	3.24	0.12	1.59	0.00
	0.25	0.04	0.57	-0.07	0.21	0.19	0.37	0.03	0.05	0.00
Pakistan	0.09	0.00	0.05			0.00	0.69	0.00	0.53	
	0.01	0.00	-0.03			0.00	0.19	0.00	-0.05	
Indonesia	2.85	0.40	3.36	0.79	4.71	0.23	1.19	0.49	2.22	0.00
	0.86	0.10	-1.55	-0.37	1.54	0.10	0.15	0.13	-0.18	-0.01
Malaysia	0.32	0.03	0.97	0.38	12.88	0.46	0.48	3.46	1.55	0.27
	0.00	-0.02	-0.42	0.25	1.76	-0.11	-0.03	-0.43	-0.28	0.06
Thailand	5.39	0.55	1.41	0.76	0.06	0.16	1.02	1.48	4.08	0.00
	-0.74	0.02	-0.57	0.74	-0.01	0.02	0.01	0.08	-1.84	0.00
Philippines	1.38	0.10	0.16	0.00	19.07	0.06	0.25	1.80	1.77	0.01
	-0.02	0.00	-0.02	0.00	-2.90	-0.03	0.01	0.84	-0.38	-0.01
Singapore	0.36	0.02	0.11	0.31	0.44	0.67	0.12	3.66	0.66	
	-0.06	0.00	0.01	0.09	0.44	-0.65	0.01	-0.88	-0.25	-0.32
China	2.24	0.48	2.59	0.71	0.53	2.82	6.37	5.19	23.85	0.13
	-0.02	0.04	0.79	-0.07	0.35	0.58	1.48	1.70	1.94	0.07
Korea	0.39	0.24	0.88	0.35	0.07	1.35	3.15	3.53	2.37	0.14
	-0.16	-0.04	0.13	0.07	-0.01	0.23	0.61	-1.18	-1.00	0.12
Taiwan	0.98	0.23	0.60	0.76	0.24	0.87	3.80	4.90	4.08	0.01
	-0.05	-0.01	0.05	0.74	0.00	-0.14	-0.44	0.08	-1.84	-0.13

Export structures of Southeast Asian economies show an interesting feature. That is, Indonesia, Thailand, Malaysia and Philippines have higher market shares in China than in the U.S. for most products except for SITC 7 and 8. For instance, Malaysia has higher shares of machinery (SITC 7) and other manufactured goods(SITC 8) in the U.S. market, while the market shares of all others products are lower than those in China. Also, these economies have generally increased their shares of these products in China during the same period.

Table IV-4 reports export competitiveness of AP developing economies measured by revealed comparative advantage(RCA) of 1998 at SITC 1 digit level, which indicates AP developing economies interests in the Chinese market. As an RCA of unity implies better export performance of a product relative to overall exports of an exporting country, products with RCA higher than 1 can be said to 'reveal' comparative advantage in the export market in question. Overall, Southeast and South Asia economies have a similar group of products in which they reveal comparative advantages. Common areas in which they have RCAs higher than unity includes;

Food & Animals(SITC 0), crude materials(SITC 2), animal and vegetable oils (SITC 4). The main difference between these two country groups is that Indonesia and Philippines reveal comparative advantage in mineral fuel while South Asian countries show strong competitiveness in manufactured goods. However, the difference needs more scrutiny because this group includes wide variety of industrial products from textile and apparel to iron and steel. For Korea and Chinese Taipei, products of RCA higher than 1 are limited to SITC 5 and 6, while RCAs of SITC 7 and 8 are far below 1. Comparing to their export shares of SITC 7 and 8 in the U.S., they do not seem to fully exploit their export potentials in the Chinese market.

**Table IV-4. RCA's of AP economies in China(1998)**

SITC	0	1	2	3	4	5	6	7	8	9
Bangladesh	8.50	0.0	6.5	0.0	0.0	0.0	1.50	0.0	1.50	0.0
India	10.1	0.02	4.67	0.08	3.41	0.38	1.11	0.03	0.30	0.03
Pakistan	0.79	0.0	0.54	0.14	0.0	0.0	4.14	0.0	0.0	0.0
Indonesia	1.34	0.03	2.40	3.90	4.81	0.66	1.79	0.1	0.10	0.0
Malaysia	0.36	0.15	1.43	0.97	17.27	0.67	0.93	0.82	0.25	0.01
Philippines	5.11	0.08	0.51	1.81	5.92	0.35	0.81	1.03	0.30	0.0
Thailand	3.42	0.48	1.58	0.51	0.04	1.46	0.63	0.97	0.31	0.01
Korea	0.18	0.06	0.46	1.50	0.03	1.72	1.71	0.54	0.71	0.05
C. Taipei	0.06	0.06	0.39	0.05	0.02	1.37	1.68	0.84	0.89	0.04

RCAs reported in Table IV-4 conceal real export interests because SITC one-digit level data is so aggregated that AP economies may not export some products at all. Also, economies may have a great interest in some products even though they reveal relatively lower level of comparative advantage in China if their export performance of those products is relatively good in other major export markets such as the U.S. In order to evaluate the effects of China's accession to the WTO, it is necessary to list up products for which either those economies have RCAs higher than unity or have a relatively high level of exports. For example, though RCAs of Korean exports for SITC 7 and 8 are considerably low in China, it is clear that those are Korea's major exports in general. In this context, we identify products of SITC at a double-digit level for which AP economies might have interests in the Chinese market. The products and

associated economies are presented in Table IV-5. Either these products have RCAs greater than 1 or their export shares are relatively large. The numbers in the first column denotes SITC one digit level of classification and those of first row indicates second digits associated with first digit numbers.

**Table IV-5. Major Areas of Export Interests**

	-1	-2	-3	-4	-5	-6	-7	-8
0			Bang. India	Thai	Philip. Thai	Thai		India
1								
2			Indo. Malay. Thai	Indo. Malay. Thai	Indo. Thai	Bang. India Indo. Malay. Thai	India	India Thai
3			Indo. Philip.. Sing. Korea Taiwan	Indo. Philip. Sing. Korea Taiwan				
4		India Indo. Malay. Philip.						
5	Korea Taiwan		Korea Taiwan				Korea Taiwan	
6	Bang. India Korea Pakistan Taiwan		India Indo.	Indo. Korea Taiwan	Bang India Pakistan Indo. Korea Taiwan	India	Korea Taiwan	
7		India Malay. Indo. Thai Philip. Korea Taiwan	Malay. Thai Philip. Korea Sing. Taiwan	Malay. Thai Philip. Korea Sing. Taiwan	Malay. Thai Philip. Korea Taiwan		Malay. Indo. Thai Philip. Korea Sing. Taiwan	
8	Indo. Malay. Thai Korea Taiwan			Bang.	Indo. Thai Korea Taiwan			

Note. Each row represents SITC one-digit classification and each column represents SITC two-digit classification. Thus the cell of column 2 & row 2 represents SITC 01.

Several patterns appear in this table. First, South Asian economies appear to have comparative advantages in primary products and light industrial products like leather

and textile products(SITC 61, 65). Also, Bangladesh recorded some exports of apparel(SITC 84), while India exported limited amount of industrial machines. Second, Southeast Asian economies' major exports include rubber, cork and wood, pulp, and various kinds of machineries. Particularly, Malaysia and Thailand recorded a significant amount of industrial equipment and data processing machines. As far as Indonesia and Philippines are concerned, petroleum and products thereof, natural gas and vegetable oil are important areas of exports in the Chinese markets. Third, exports of Korea and Chinese Taipei to China are mostly consisted of industrial products ranging from SITC 61 through SITC 85. Also, petroleum products and manufactured natural gas are important export products for Korea.

## **2. Impacts of Tariff Liberalization on AP developing Economies' Exports**

There are many technical difficulties in evaluating China's tariff liberalization in detail. Since the U.S.-China agreement for tariff reduction is based on HS 8 digit level of data, it is almost impossible to evaluate the tariff reduction schedule of all individual products. As we focus on products of export interests for AP developing economies at SITC 2-digit level, it is necessary to measure representative tariff levels for each category. For this purpose, we first gathered HS 8 digit data for tariff liberalization schedule, falling under the SITC 2- digit category for which AP economies have export interests. Then we compiled trade-weighted MFN average tariffs for each SITC 2 digit level from the trade and tariff data of HS 6 digit level, whose import values ranked at top 10 in each category of SITC 2.

Table IV-6 illustrates China's tariff liberalization schedules and its impacts on Chinese imports for selected products in which AP developing economies seem to have interests. Both current and bound Tariff rates are weighted averages. Products of most significant tariff reduction include; machinery and electrical machinery (SITC 72, 74, 75, 77, 78), agricultural product(SITC 03), textile fibers(SITC 26) and other products of light industry such as wood manufactures, paperboard, textile yarn and fabric, iron and steel(SITC 63,64, 65, 67), and miscellaneous manufactured articles like building fixtures, apparel and footwear(SITC 81, 84). Some items are missing in the China-U.S. agreements such as SITC 04, 05, 06,08 and 23 in which AP developing economies have some export interests. However, as the list of AP developing economies'

interested products includes most of the above items, China's liberalizations schedule seems to be in conformity with export interests of AP developing economies.

**Table IV-6 Trade Weighted Tariff Reduction Schedule and Expected Import Expansion for Selected Product Groups** (1,000 U.S.\$, %)

SITC	Import Value	Import Expansion	Current Rate	Bound Rate	SITC	Import Value	Import Expansion	Current Rate	Bound Rate
00	54,417	0			53	1,122,383	n.a.		
03	667,363	1,001.04	22.79	10.17	57	8,182,055	29,864.5	16.51	6.50
04	735,398	n.a.			61	1,991,442	9.5	10.44	7.47
05	353,673	n.a.			63	1,001,968	2,655.2	13.09	4.93
06	172,263	n.a.			64	3,423,184	22,079.5	14.09	5.61
08	1,405,060	n.a.			65	11,081,885	40.94	18.59	8.97
23	790,154	n.a.			66	1,409,532	19,592.4	11.74	9.96
24	975,363	2,389.6	3.40	1.22	67	6,488,848	6,164.4	10.05	5.81
25	1,094,518	1,587.1	1.00	0.10	72	8,294,663	116,954.7	12.11	2.50
26	2,401,785	81.7	14.48	7.14	73	2,596,283	36,607.5	10.64	8.25
27	270,754	1,827.6	3.73	3.70	74	6,284,194	88,607.1	14.98	6.98
28	3,293,609	6,587.2	2.00	1.37	75	6,036,217	150,301.8	10.31	0.45
33	5,882,205	16,470.2	4.53	3.19	77	16,683,891	83,419.4	9.97	3.70
34	824,040	1,112.4	6	3	78	1,986,130	9,930.65	26.14	11.49
42	1,384,565	18,553.17	25	15	81	108,417	64.9	20.20	13.68
51	3,491,868	19,379.8	10.33	5.57	84	1,071,925	1,822.2	32.82	15.77

The expected expansion of imports are measured by applying implicit long-term price elasticity to the base year(1998) import values of individual products.<sup>10</sup> Significant increase in imports are expected for industry special machines(SITC 72), office and data processing machines(SITC 75) and electrical equipment(SITC 77). Most of East and Southeast Asian economies have great export interests in these products. Except for Thailand and Indonesia, all economies have higher market shares of SITC 7 in the U.S. than in China. Although RCAs for these products are less than 1 currently, significant tariff reduction on these products would provide good opportunities for East and Southeast Asian economies. On the contrary, the import expansion for which some South and Southeast Asian economies have interests turns out to be of limited sizes. For example, the sizes of expansion for fish(SITC 03), cork and wood(SITC 24)

<sup>11</sup> Elasticity for each product are calculated from dividing changes of import value by changes in trade-weighted tariffs between 1995-1998. We divided (arbitrary) the elasticity by 2 to remove income effects on the import expansion during this period. So our evaluation of the effects from the tariff reduction is subject to relative importance of price and income effects on imports.

and pulp(SITC 25) are estimated to be in the range of 1-2million U.S\$. It seems that the liberalization schedule of China is biased to capital-intensive products and hence to relatively advanced economies in the region.

Table IV-7 summarizes impacts on exports by individual AP developing economies for each SITC 2-digit products. The extent of expected import expansion is of limited size for South Asian economies, mainly due to limited transaction between South Asia and East Asia in general. India is expected to have considerable opportunities only for the export of fixed vegetable oils (SITC 42) and non-metal mineral manufactures(SITC 66). However, it should be noted that the assessment of import expansion effects for individual economies could underestimate export opportunities because it is based on the current levels of market shares. Insignificant export performance in the Chinese market is one reason for the limited size of expected import expansion for these economies. Considering South economies' significantly higher shares in the U.S. markets of their major exports, these economies may have bigger potential for exports than the current presence in the Chinese markets for light-industry manufactures. For instance, while Bangladesh lost its share in the Chinese market for the export of manufactured goods of SITC 6, India and Pakistan's shares increased their shares noticeably during the period of 1995-1998.

Greater export opportunities are expected for Southeast and East Asian economies. First, Malaysia and Philippines share the same interests with India for exports of fixed vegetable oils. The expected increases amount to 96 million U.S \$ for Malaysia and 65 million U.S \$ for Philippines. Second, all Southeast Asian economies are expected to gain from increased export of electrical equipment(SITC 77). Also, Malaysia and Thailand will be able to increase exports of industrial equipment(SITC 74) considerably.

Korea and Chinese Taipei seem to be the greatest beneficiaries from China's tariff liberalization. The markets in which both economies can expect considerable export opportunities include; plastics(SITC 57), paper(SITC 64), textile yarn, fabrics(SITC 65), metalworking machinery(SITC 73), industrial equipment(SITC 74). As far as Korea is concerned, organic chemicals(SITC 51), industry special equipment(SITC 72) and electrical equipment(SITC 77) are important areas for exports.

**Table IV-7. Export Opportunities for Individual Economies by Product(1,000 U.S \$)**

SITC	South Asia			Southeast Asia				East Asia	
	Bangladesh	India	Pakistan	Malaysia	Thailand	Philippines	Indonesia	Korea	Taiwan
03	11.0	26.5							
04									
05									
06									
08									
23									
24				596.6	36.4		288.9		
25					1.7		37.65		
26	2.0	9.5		10.6	27.5		9.8		
27		554.0							
28		762.0			30.8				
33						156.8	3,903.1	8,624.7	359.9
34						112.4	104.4	483.3	
42		654.2		96,853.0		6,305.9	24,404.4		
51								27,246.3	4,388.6
53									
57								50,517.7	40,731.1
61	2.3	10.5	3.5					255.5	191.5
63							5,128.1		
64							12,964.9	25,691.9	13,282.0
65	9.7	669.8	71.4				38.4	85.7	11.5
66		4,582.3							0
67								7,137.6	5,773.6
72				1,126.9	243.9	102.3	214.7	14,323.4	
73				899.4	397.0	136.7		15,983.1	40,501.3
74				4,761.6	6,356.1	186.9		36,039.4	58,011.1
75				735.5	3,174.9	369.6		766.04	2,018.3
77				17,324.6	4,213.	3,644.8	1,585.	59,668.5	
78								1,719.1	4,210.3
81				14.9	12.4			13.4	22.5
84	60.4								

**3. Competition between AP developing economies and China in overseas market:  
Some Implications on Textile and Apparel Exports.**

The Uruguay Round produced an agreement to eliminate quantitative restrictions on trade in textile and clothing imposed by MFA. The phase-out of MFA by 2004 is

generally expected to expand exports from developing countries. However, China's accession to the WTO poses one major challenge to AP developing economies because China and other textile exporting economies will have to face increased competition with the abolition of bilateral MFA agreements. So far, the quota system of MFA has protected, at least, each allocated shares of textile and apparels exports of individual exporting countries, despite of its intrinsic restrictive effects. Therefore the abolition of MFA quotas poses a new uncertainty. That is, it can expose small but protected textile and apparel suppliers to additional competition from other currently restrained but competitive exporters like China. Therefore, it is difficult to predict exactly what will be the consequence of MFA abolition.

Table IV- 8 shows trends of import shares(in terms of volume) in the U.S. textile market of major suppliers. Most top suppliers lost their shares except Mexico and Honduras of which exports are preferentially treated in the U.S market. As far as total market shares are concerned, Asian developing economies' performances are still impressive. For example, while Bangladesh's overall market share in the U.S. is far less than 1%, export share of textile and clothing recorded over 5% in 1999 .

**Table IV-8 Major Suppliers of Textile and Clothing to the U.S (Million M2)**

Suppliers	Exports			Shares		
	1997	1998	1999	1997	1998	1999
Mexico	1555.103	1984.572	2253.946	13.70%	15.40%	16.35%
China	947.376	910.229	905.285	8.35%	7.06%	6.57%
Honduras	725.982	798.962	889.254	6.40%	6.20%	6.45%
Hong Kong	736.450	862.439	825.912	6.49%	6.69%	5.99%
Bangladesh	671.763	743.516	761.217	5.92%	5.77%	5.52%
Chinese Taipei	589.586	620.643	629.124	5.19%	4.82%	4.56%
Korea	320.484	460.075	521.518	2.82%	3.57%	3.78%
Indonesia	393.554	433.677	429.858	3.47%	3.37%	3.12%
India	315.584	364.260	378.998	2.78%	2.83%	2.75%
Thailand	283.767	334.885	367.966	2.50%	2.60%	2.67%
Sri Lanka	322.046	332.451	329.720	2.84%	2.58%	2.39%
Pakistan	193.656	214.783	225.526	1.71%	1.67%	1.64%
Malaysia	134.984	162.381	182.008	1.19%	1.26%	1.32%

Source) U.S Department of Commerce

In order to assess the impact of MFA phase-out and China's accession to the WTO on exports of AP developing economies, we may have to consider those issues involved in textile trading under MFA such as quota utilization ratio, quality upgrading, and



production sharing activities.<sup>11</sup>

**Table IV- 9 MFA Quota Utilization Ratio, Asian Suppliers**

Suppliers	Quota Utilization Ratio		
	1997	1998	1999
Korea	49.45	62.07	62.29
China	81.74	77.23	76.63
Hong Kong	54.08	65.82	61.26
Chinese Taipei	57.31	59.34	59.02
Singapore	23.76	22.31	25.12
Indonesia	82.00	89.75	79.30
Thailand	67.23	75.17	73.43
Malaysia	46.63	51.50	45.95
Philippines	61.94	61.90	65.14
Bangladesh	82.96	91.14	85.03
India	90.44	91.96	88.60
Sri Lanka	59.34	65.25	59.36
Pakistan	62.06	61.03	61.94

Source) U.S Department of Commerce

Quota utilization ratio represents the extent to which the MFA actually restrict trade. Typically, quota utilization ratio is less than 100%. However, it would be misleading to conclude that the MFA is less restrictive because quota is not binding. First of all, quota is usually allocated on the basis of historical export performance, disregarding changes in demand structure. It results in disparities in quota utilization among suppliers. For example, the utilization ratios of Korea and Chinese Taipei remain at around 60%, while the ratios tend to be high in economies of other parts of the Asia Pacific. Also, the MFA allows limited flexibility among categories of textile and clothing, which leads to lower utilization ratio. Therefore, lower ratios themselves may reflect restriction imposed to textile trade by the MFA. The fact that utilization ratio of China continued to decrease past 3 years may be a sign of advancement of Chinese textile industry and its competitiveness, which could take effects after the total phase-out of the MFA. Quality upgrading and product diversification under quota through changes in product mix is easily found when suppliers are faced with volume restrictions. For instance, the Chinese apparel industry is moving toward the

<sup>11</sup> The U.S. negotiated that safeguard is available upon China's accession to the WTO until 2008, four years after the last quotas are set to be lifted by importing countries under the ATC. This will give some time for other developing economies to enhance their export competitiveness.

production of quality oriented and high value added products. The change is led by producers in Hong Kong. And Hong Kong's return to Chinese ruling in 1997 has boosted China's textile and apparel industry greatly.<sup>12</sup>

Recently, the United States enacted the Trade Promotion Act(TPA) which is intended to apply preferential tariff to Central American countries in lieu of Caribbean Basin Initiatives. As a result, apparel imports from these areas will be subject to the same rates as the import from Mexico. It is expected that U.S. exports of yarns and fabrics will expand, and production sharing activities(PSA) among the U.S wholesalers, producers and assembly lines in Central American countries will increase. It is therefore expected that the competitiveness of apparels produced by the production sharing activities will greatly be enhanced. Particularly, the Act is expected to help compete with imported apparels from Asian region. Since the launch of NAFTA, apparel imports from other NAFTA economies increased 585% while imports from CBI and Asia region increased about 250%. Apart from China's accession to the WTO, the TPA has an important implication on AP developing economies. That is, it is plausible that foreign direct investment activities may dramatically respond to this Act. It does not necessarily mean that production capitals move from Asia to Central America. Rather, more foreign direct investment search for other areas of Asia like Cambodia, Laos and Myanmar which have strong comparative advantages in labor cost and labor quality.

In order to assess the competitiveness of AP developing economies in textile and apparel trade in the U.S. market, we conducted a constant market analysis(CMS) for the period of 1997-1998, of which results are reported in Table IV-9 and IV-10 . According to the CMS model, the proportionate increase in exports of a commodity over time is composed of following factors; market growth effect, production mix effect and residual effects which might reflect price competitiveness, quality changes and other managerial skills.

According to Table IV-10, there seems to be a common pattern. All suppliers responded quickly to the growth of demand. On the other hand, the negative signs of

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<sup>12</sup> USITC(1999)

the product mix effect imply that Asian economies did not catch up with changes in demand structures very well. Economies differ from each other with respect to the residual 'competitiveness' effects. The positive signs for Korea and Chinese Taipei seem to be attributable to price competitiveness benefited from drastic depreciation of their currencies after the crisis. One of the most interesting aspects of this table is that the less developed Southeast Asian economies demonstrated impressive competitiveness. Actually, the competitiveness factor contributed to most of export growth. On the contrary, South Asian economies are heavily dependent on growth of demand. It is not clear yet whether geographical diversification of production activities in this sector, which is occurring in Southeast Asia, will accelerate in the future. However, increased competition in the world textile and clothing market with the phase-out of the MFA would lead to AP region-wide reorganization of production activities.

**Table IV-10 Factors of Export Growth: MFA Category Total(U.S)**

	<b>Total Growth</b>	<b>Grwoth Effects</b>	<b>Product Mix</b>	<b>Competitiveness</b>
<b>Korea</b>	177.377	107.552	-35.308	105.134
<b>China</b>	92.322	200.148	-70.061	-37.669
<b>Chinese Taipei</b>	80.033	122.559	-37.88	-4.586
<b>Indonesia</b>	-67.442	100.399	-29.133	-138.658
<b>Thailand</b>	120.457	102.693	-32.699	50.512
<b>Malaysia</b>	58.004	27.14	-7.81	38.687
<b>Philippines</b>	109.682	81.945	-26.022	53.8
<b>Cambodia</b>	67.380	11.111	-3.03	58.669
<b>Myanmar</b>	27.394	4.709	-1.392	23.907
<b>Vietnam</b>	6.263	1.784	-0.33	6.82
<b>Macau</b>	51.662	23.279	-6.74	35.134
<b>Bangladesh</b>	44.982	89.15	-24.024	-20.1
<b>India</b>	65.784	111.616	-28.108	-17.667
<b>Sri Lanka</b>	32.402	54.347	-15.874	-6.044
<b>Pakistan</b>	61.125	152.786	-34.896	-56.761

In Table IV-11, results of CMS analysis on apparel are reported. The results from apparel exports are similar to those of total textile trade. Again, AP developing economies do not seem to have rapidly responded to the changes in demand structure.

The product mix effects are all negatively signed. However, the South Asian economies have positive signs in competitiveness factor although the extent of contribution by this factor to export growth is far below Southeast Asian less developed economies. This fact could answer the question why Hong Kong manufactures are moving to Vietnam, Laos and Cambodia recently, when a massive restructuring is expected with more liberalized trade environment for textile and apparel trade in coming years

**Table IV-11 Factors of Export Growth : Total Apparel (U.S)**

	Total Growth	Grwh Effects	Product Mix	Competitiveness
<b>Korea</b>	404.429	204.412	-47.451	247.566
<b>China</b>	-59.434	523.736	-71.181	-511.74
<b>Chinese Taipei</b>	72.528	299.349	-112.251	-114.428
<b>Indonesia</b>	52.258	213.762	-99.686	-61.715
<b>Thailand</b>	228.442	192.144	-87.006	243.853
<b>Malaysia</b>	83.013	59.623	-28.405	51.823
<b>Philippines</b>	246.191	164.768	-76.582	158.083
<b>Cambodia</b>	145.089	7.541	-4.258	140.559
<b>Myanmar</b>	42.76	7.589	-3.382	38.311
<b>Vietnam</b>	8.841	3.686	-2.22	6.58
<b>Macau</b>	101.197	44.119	-21.58	78.68
<b>Bangladesh</b>	146.009	191.128	-105.058	60.03
<b>India</b>	163.693	246.435	-157.02	74.395
<b>Sri Lanka</b>	80.663	119.844	-53.034	13.91
<b>Pakistan</b>	418.637	281.461	-169.169	306.332

## **V. Policy Implications**

### **1. Trade and Investment Liberalization**

With trade and investment liberalization, developing countries are given the opportunity to improve the most favorable comparative advantages in natural resources and cheap labor. When opening domestic markets, countries tend to make a better use of cheap labor and natural resources in response to competition. Therefore, they will strengthen international competitiveness in sectors where they have comparative advantage. Developing countries can also gain technology transfer from developed countries and improve corporate management; that is, they acquire by-products, such as advanced technology and managerial skills to be used for high value-added items. As a result, developing economies will become more stabilized and competitive, which will lead to sustainable economic growth. This is a major reason why developing countries should proceed trade and investment liberalization in more progressive way. In specific, policy guidance should be made as follows.

First, they should actively react and adjust to the multilateral trading system. Under the system where some advanced countries such as the United States, EU, Japan, and Canada have led the world economy, developing countries have responded to the system in a passive and inactive way. However, with the China's WTO entry, developing countries will exercise stronger influence under the auspice of China such that they can devote to multilateral trading system more actively, thereby contributing to expansion of world trade. In doing so, rather than negatively responding to trade and investment liberalization, they have to suggest productive ideas for a better scheme for trade and investment liberalization so that they can be benefited from the system. In addition, they will have to comply with international norms related to trade and investment liberalization. It should be worth emphasizing that they have to react to the multilateral trading system positively not only when establishing international norms but also when implementing them.

Second, it seems desirable for developing countries to actively participate in regional economic cooperation programs which are designed to promote trade and investment

liberalization. As well known, recently, regional trade agreements are on the increasing trend in number. According to the WTO, trade agreements within GATT/WTO recorded 107 as of April, 1994. Among them, 77 newly established agreements were made during nine years since 1990, occupying 72% of total regional trade agreements. Moreover, assuming that the number of agreements not yet reported to the GATT/WTO exceeds 100, regionalism tends to become fairly universal. In the past, free trade agreements were made mainly either among developed or among developing countries. In recent years, however, the free trade agreements between developed and developing countries are prevailing. Thus, it seems that the development stage is not a matter for forming such agreements. While there exist controversies over the relationship between regionalism and multilateralism, it becomes better known that regionalism is not detrimental but rather complementary to multilateralism in achieving trade liberalization. Regional trade agreements usually contain higher level of obligations for liberalization than the multilateral trade agreements do. Thus, they can pursue more advanced liberalization scheme with smaller number of nations.

Third, bilateral investment treaties(BIT) are also worth mentioning for similar reasons; they may help the developing countries attract foreign investment and adopt technology from developed countries in a more stable manner. With China's entry to the WTO, developed countries may possibly desire to contract FTA or BIT with countries neighboring to China in order not only to make use of their cheap labor and natural resources, but also to penetrate more aggressively into the Chinese market in the future. Developing countries need to take this chance for attracting foreign capital and advanced technology.

Lastly, it should be emphasized that domestic regulatory reform is one of fundamental and necessary conditions for trade and investment liberalization. The prior notion should be given that developing countries should make domestic regulations consistent with international norms. They have to realize that such liberalization is to ensure not only better market access but also fair competition between domestic and foreign competitors. They can pursue trade and investment liberalization successfully by complying with international norms and ensuring transparency in domestic institutions.

## 2. Response to New Trade Issues

It is very difficult to predict exactly when the new trade issues will be incorporated into the multilateral trading system. Following up the recent discussions in various international fora, considerable work seems to remain at the WTO to reach an agreement on those issues. The most immediate priority is to narrow down the differences in the views on new trade issues between developed and developing countries. Even though multilateral rules on the new trade issues are expected to contribute to enhancing the world economic and social welfare in the long run, they may have negative economic impacts on the developing countries in the short run.

First of all, strengthening of environmental disciplines by multilateral environment standards will raise production costs of firms requiring a substantial change in the production process and technology. Furthermore, a part of those costs may be transferred to consumers, ultimately raising the consumer price as well. Similar effects are expected in relation to the issue of labor standards. Upward adjustments of labor standards may cause shortages in labor supply, raising labor costs. Ensuring the core labor standards may induce higher wages through enforcement of workers' collective bargaining status *vis-a-vis* employers.<sup>13</sup>

Multilateral rules of competition policy and transparency in government procurement related with anti-corruption are also difficult for developing countries to accept at least in the short run when their domestic system and practices are considered. Not many developing countries have yet adopted competition policy in their domestic economy. Much opaqueness remains in their businesses as well as in their public sectors. Reform of systems and practices in those areas will certainly cause huge social as well as economic adjustment costs. Even liberalization in investment will be a very difficult task for some developing countries. They want to selectively open areas of foreign investment which are consistent with their development strategy. Protection for certain domestic industries may be another reason why they are

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<sup>13</sup> The relationship between labor standards and trade has been examined by Rodrik (1997). The study shows that lax labor standards are highly associated with lower costs in a cross-section of countries.

unwilling to liberalize investment.

Considering all of these, developed countries should give sufficient time for developing countries to adapt to new trade issues and assist them with relevant technology and know-hows. Developing countries, in exchange, should prepare for taking measures and implementing them.

Primarily, developing countries should expand investment in the protection of environment. It is obvious that the issue will become more important as overseas sales of unqualified commodities to environment standards are not permitted. They should make preventive environment policy and assist domestic firms to the greatest extent in building up environment-friendly workplace. The government should set up rules or administrative guidelines to implement even with some reservation period.

It is likely to take a great deal of time to set international norms over labor issues because developing countries are still strongly opposing to it. However, it may be possible that a minimum level of guideline for labor standards could be set up based upon careful research results. Developing countries should take more progressive actions for labor issues in order that they continue to be able to export commodities where they have comparative advantage. It should be admitted that adjustment to international labor standards will lead to higher productivity, better quality control and export competitiveness.

It is also likely that international norms and standards will be adopted in the area of competition policy, anti-corruption, and corporate governance. It is certainly not easy task for developing countries, but they may not be able to refuse adoption of such issues for long because these areas are directly inter-linked with nation's overall images. Since those issues are highly co-related with globalization, developed countries can not give them up easily either. Core parts of those issues will remain persistently controversial in various international fora as long as China retains unfair and intransparent competition structure in private as well as public sectors. When international norms are made over those issues, monopolistic business practices and intransparent government procurement procedures, which are fairly typical in developing countries, will be strictly governed.



### **3. Industrial Restructuring**

As the world economy becomes globalized and Chinese economy is integrated into the multilateral trading system, developing countries may experience much difficulties in the short run. Their economies will stagnate in poverty unless they can overcome problems of lack of industrial technology, over-supply of labor force, inconsistencies with international norms, and inefficiencies in economic management. In order to resolve those problems, they have to pursue a dramatic industrial restructuring.

In principle, they have to strengthen export competitiveness, building up knowledge-based industries. Technology should be developed to improve non-price competitiveness. In many areas, Chinese major exports compete with those of developing countries. Such competition can cause dilemma for developing countries not only in their exports to China or to developed countries, but also in their domestic sales. Their major exporting products such as agricultures, textiles, raw materials and cheap manufacturing commodities are already price-competitive. However, the problem is that Chinese products are also fairly price-competitive as well. Unless developing countries improve competitiveness in non-price factors such as quality, function, design, packages, etc., their export market will be rapidly enroached by Chinese products. That is why developing countries should promote industrial restructuring, building up knowledge-based industries. At present, developed countries are already moving towards the economy of knowledge-based industries. It is no doubt that the gap of technology and wealth will deepen between developed and developing countries unless developing countries try to build up knowledge-based industry. There exists no clear definition of knowledge-based industry yet. However, it is perceived that knowledge-based industries include conventional industries as well, if they can commercialize high-value added items such as fashion-clothing and special footwear. Thus, developing countries can establish knowledge-based industry structure, first by utilizing their conventional industries, and then by moving towards industries with higher class of technology.

Second, developing countries have to foster the service industry. The service industry

can be fostered not only by developing their own national service sectors but also by inviting foreign direct investment in their service industry. Although the service industry features difference depending on economic development levels, it is, in general, highly co-related with manufacturing sector. So, it can contribute greatly to economic growth, production expansion, and international competitiveness. The service sectors on which the agricultural or manufacturing industry is highly dependent are as follows: distribution services such as transportation, storage, telecommunication, retails / whole-sales, financial services such as banking and insurance, and professional services such as engineering, construction, and legal services. As an economy develops in higher levels, service industry and other industries tend to become more dependent on each other. In consequence, without development of the service industry, economies as a whole can not obtain international competitiveness in the future.

Third, developing countries should restructure industries in order to effectively respond to new trade issues. In case where international norms on new trade issues are made in the short run, it is certain that developing countries should pay expensive adjustment costs. Therefore, they should make restructuring plans as early as possible and implement them sincerely. In specific, they should put great efforts on constructing a structure of environment-friendly domestic industries, considering it as a fundamental survival issue. And, at the same time, they have to establish business environments consistent with the market economy. In particular, they should consolidate business practices where small and medium-sized enterprises enjoy free competence and fair market condition. In doing so, they have to make rules and promote effective competition policy. They should also dramatically reform the public sector which is considered as a somewhat problematic area in developing countries. The major task is how to eliminate corruption networks between the government and firms, and to privatize public firms for efficient management.

Lastly, developing countries should realign their industrial support system so that it can perform a proper function of facilitating the sustainable economic growth. If the system functions properly, developing countries may be able to explore new industry areas, driving the economic growth with dynamic comparative advantages. In reality, the industrial support policies have been severely restrained since the launch of WTO

under the 'Agreement on Subsidies and Countervailing Measures'. According to the Agreement, all but least developing countries are prohibited to use industrial support policies which directly affect export. Furthermore, even in the case that certain subsidies do not affect export, those granted to a particular industry to improve competitiveness are restrained in their use if they cause injuries to trading partners. In consequence, developing countries should reform their industrial support system so that they avoid an intensive support for a particular industry which may lead to distorting trade structure directly or indirectly. Rather, they should give a limited support under the guidance of international norms either when the industry concerned is at an initial or declining stage. And, they have to pay more attention to the areas such as social infrastructures, R&D, regional development, and environmental protection so that overall industrial sectors gain benefits. Summing up, it is important to understand that even if certain subsidies need to be provided to achieve a specific development goal, they should be granted to the extent not to distort trade structure.

#### **4. Human Resource Development**

Abundant labor of developing countries in the Asia and Pacific region certainly plays a major role in achieving economic growth. While their potential economic growth lies in rich human resources, they remain quite underdeveloped; they are not fully utilized with over-supply of labor force but short of skilled labor. Well-qualified labor force can be secured only through systematic education and job-training.

Developing countries need to secure the capacity to adjust to changes of the world economy by expanding investment in education. Taking it into account that the agricultural sector takes the biggest portion of the economy of developing countries in the Asia and Pacific region, they should provide rural areas at least with basic education, primary or secondary education, so that the labor force can move to manufacturing or service sectors of higher productivity. Then, the labor force will be easily nurtured with skills in various sectors, raising labor productivity in the agricultural sector as well. It is, of course, necessary that vocational training course should be provided to the workers so that they can be cultivated as professionals in the related fields. Constant vocational training should help firms improve ability to

develop new items and to meet with consumers' needs more quickly than other firms in competition. They also have to enhance the skills or knowledges of managers and entrepreneurs. Well-skilled managers or entrepreneurs will bring out more creative ideas not only in managing firms but also in establishing legal and institutional infrastructure. In that respect, it is important to provide various programs where they are educated not only on expertise or managerial skills in the related areas but also the world economic issues in general.

In order to support all of these, flexibility of labor market should be ensured. The newly industrialized countries of Asia such as Korea, Malaysia, Taiwan and Thailand could have achieved the high economic growth because millions of farmers have moved into industrial and other non-agricultural sectors of higher productivity over the past quarter century. There are tens of millions more working on farms in India, Indonesia, and Vietnam, implying that the growth potential from the transfer of rural labor to more productive jobs remains strong in those countries.<sup>14</sup> The labor flexibility will be ensured when workers are well informed of labor market. Employees should be informed of the best employment opportunity to their abilities, and employers should acquire in-time information of proper workers in need. For that purpose, institutional framework should be established so that such information may be available all the time to employees and employers.

Lastly, the importance of trade and investment liberalization should be re-emphasized in relation to human resources development. Trade and investment liberalization can work as an instrument to improve labor productivity of a nation through intensified international competition. Advanced technology, ideas, institutions, and practices can be transferred from foreign firms or consumers only when the economies are open. Domestic firms can acquire technologies embodied in import materials and components, which will contribute to human resource development in the end. Foreign direct investment, in particular, can bring up skilled labor and professional managers in more direct ways.

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<sup>14</sup> OECD, *Towards a New Global Age: Challenges and Opportunities*, Draft Analytical Report, 1997, p.64.

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UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION  
Vienna International Centre, P.O. Box 300, A-1400 Vienna, Austria  
Telephone: (+43 1) 26026-4789 or 5521, Fax: (+43 1) 26026-6821, E-mail: [cchua@unido.org](mailto:cchua@unido.org)

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UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION  
Vienna International Centre, P.O. Box 300, A-1400 Vienna, Austria  
Telephone: (+43 1) 26026-4789 or 5521, Fax: (+43 1) 26026-6821, E-mail: [cchua@unido.org](mailto:cchua@unido.org)