15. China's Trade Negotiation Strategies

Matters of growth and regional economic integration

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Introduction

China's opening and reform process that began in the late 1970s has induced a great era during which the Chinese economy has been incrementally integrating with the world economy. Outbound trade and inbound foreign direct investment (FDI) served as the twin engines of growth. China's contemporary economic story is 'a classical demonstration of the potential of export-oriented industrialization' (Krugman and Obstfeld 1991: 247). An acceleration of that process arrived with China's accession to the World Trade Organization (WTO) in 2001. China enjoyed tremendous gains by facing lower tariffs and fewer trade restrictions in accessing the extensive markets of WTO member countries and by reducing its own restrictions on trade. China became the 'factory of the world'.

China's reliance on export-oriented growth now faces challenges. The global financial crisis (GFC) of 2008 hit developed countries—the most important markets for Chinese export goods. The consequent sluggish demand for Chinese products forced many small and medium enterprises to close, especially in south-eastern China where most light manufactured goods for export are made. Guangdong was hit especially hard, as was China's aggregate export level. While the US economy has somewhat recovered from the turmoil that began in 2008, structural challenges in the European Union paint a gloomy economic picture. External demand for Chinese products has not rebounded to pre-GFC levels. On the supply side, too, wage gains in China are making labour-intensive production more expensive. Manufacturing industries seeking lower labour costs have already begun to move to other Asian countries, such as Vietnam and Indonesia. The 'world's factory', therefore, faces overcapacity within many export-oriented industries.

1 The views expressed in this chapter do not necessarily represent the views of the institutions for which the authors work. The authors are responsible for any errors.

In terms of its continuing economic development, China also faces the 'middle-income trap'—few countries have smoothly transitioned from middle to high-income status. Acknowledging the need for a change of growth model, the Third Plenary Session of the Eighteenth Communist Party Central Committee in November 2013 clearly highlighted that China will need to shift from a fast-growing economy that is essentially dependent on 'investment in heavy industry and low-cost, manufactured exports to a more mature economy driven by domestic consumption and the production of higher-value goods and services' (Wharton Business School 2015).

In addition to the endogenous challenge of a growth model transition, China is also facing an exogenous international dynamic where the current international trade rules are under negotiation. New rules are being called for so as to adjust for the expansion of global value chains. Thanks to the more than a decade-long stalemate of the WTO's multilateral Doha Round negotiations, countries are now seeking to reform current trade rules through mega-regional negotiations. This is the first time regionalism has prospered over multilateralism since the establishment of the WTO in 1995. The negotiations for mega-regional trade agreements—especially the Trans-Pacific Partnership (TPP), the Transatlantic Trade and Investment Partnership (TTIP) and the Regional Comprehensive Economic Partnership (RCEP)—have attracted a lot of attention. These delineate the general outlook of international trade rules in the twenty-first century. While these persist with seeking to liberalise trade in goods, they involve trade discrimination and therefore rules of origin. There is greater focus on liberalisation of services and investment protection. They also expand the current trade agenda by incorporating new issues—such as the environment and labour—into negotiations.

Given these potential shifts in trade governance, as part of the transition to a new growth model, China must also reconsider its approach to trade agreements. Under the old growth model, trade agreements played a critical role in facilitating the export of goods made in China and also in allowing Chinese manufacturers to successfully plug into East Asian production networks. China could reconsider its entire negotiation approach in the face of a weakening WTO-based multilateral trading system and the emergence of exclusive mega-regional negotiations. Fully utilising multilateral and regional trade negotiation platforms and participating in the process of international trade rule-making are significant to how China defines its role in international economic governance. A comprehensive and sophisticated negotiation strategy will help China to confront domestic economic challenges and to accelerate its steps to further integrate with the world economy.

This chapter explores Chinese trade negotiation strategy in response to its domestic reform as well as its changing role in the world economy. Section two briefly introduces China's export-oriented economic model and points to the need for new methods of navigation in the world economy. Section three discusses the changing dynamics of the international trading system and the implications for China in a geopolitical context and with regard to its trade negotiation agenda. Based on the analyses of China in the world economy and international trade rule-making process, section four focuses on the discussion of Chinese trade negotiation strategies. Given the three perspectives discussed—the failure of the Doha Round, the proliferation of regional trade agreements and calls for new trade rules in the Pacific Rim—this chapter offers a comprehensive overview of Chinese trade negotiation strategies. The chapter finally suggests that China will work with other countries towards convergence of the different trade agendas of mega-regional agreements and in so doing play a bigger role in shaping the international trading system.

Changing relations between China and the world economy

Challenge for the traditional export-oriented growth model

The opening-up policy from the late 1970s transformed China from a planned economy towards a market-oriented economy. In the early stages of that process, a fundamental policy element was the pioneering opening up of selective coastal areas of China, which in turn helped to fire up the economic growth of other regions in the country.

First, China's government boosted its investment in these coastal regions. The share of the central government's investment in these regions increased from 39.5 per cent during 1953–78 to 53.5 per cent during 1979–91 (Yao 2008). That surge in investment was used mainly to construct infrastructure. Favourable policies also sought to attract FDI. The rapid development of infrastructure and favourable treatment for foreign investors, together with cheap local labour, helped China to become the largest developing country FDI destination. During these years, China received about 20 per cent of total inbound FDI into developing countries. Through 2006–10, FDI accounted for nearly 2.5 per cent of China's average gross domestic product (GDP) (World Bank 2010). The majority of foreign companies that flooded into China set up factories that produce goods for export. In turn, foreign-invested enterprises came to produce nearly half of all China's exports. China in turn rose to become a significant global trade participant.

Figure 15.1 displays the evolution of the trade volume of China, from 1978 to 2013. It illustrates that the levels of imports and exports have risen since 1990. The year 2001, when China joined the WTO, marks an acceleration point, especially in China's exports. The financial crises of 1997 and 2008 each reduced demand for China's exports. China was, however, hit more severely by the latter than the former. Having experienced a temporary fall in demand in 2009, Chinese exports have, however, continued to increase, helped by the post-GFC economic stimulus package. The graphs of both imports and exports are less steep in the period after 2011.

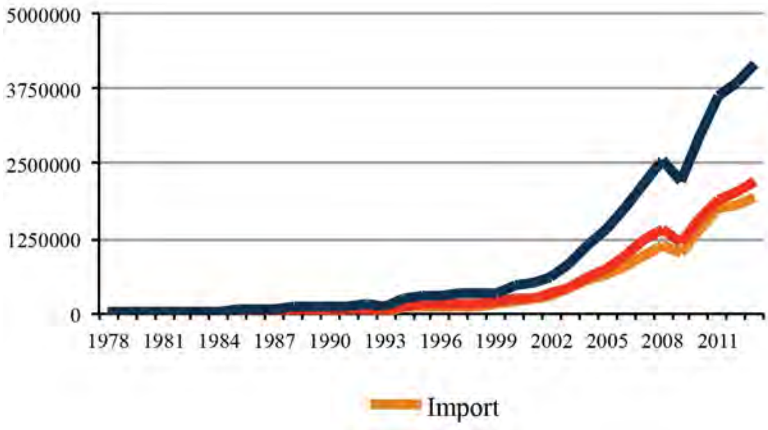

Figure 15.1 Chinese trade volume, 1978–2013 ($ million)

Source: NBS (2015).

Figure 15.2 illustrates the share of GDP in exports since 1978. The mainly rising trend demonstrates how trade became an important endogenous component of China's economic growth, especially from the mid-1990s. The importance of exports to China's economy, in particular, was accentuated after China's accession to the WTO. During 2002–07, the average share of exports in GDP peaked at 30 per cent, in 2007. Exports became the 'engine' of Chinese economic growth. Since the GFC in 2008 exports have not returned to pre-crisis levels, and instead have contributed less and less annually to GDP. In 2013, the ratio of exports to GDP reached 23.3 per cent—close to the ratio of 2003. While still making a great contribution to GDP, exports evidently no longer serve as China's economic engine.

Figure 15.2 Export trade share of GDP, 1978–2013

Source: NBS (2015).

Sluggish world demand is one of the main explanations for China's export slowdown. While the uncertain recovery of the US economy is somewhat positive news for Chinese exporters, the US Government's measures to minimise its trade deficit with China serve to curb the scale of rebound in demand for Chinese exports. The pace of export increase is slow. In contrast, China's demand for US exports is rising relatively rapidly. China became the United States' largest export destination in 2013. That year, China imported goods to the value of $122.1 billion—up 10.4 per cent year-on-year (US Trade Representative 2015). China's exports to the United States in 2013 increased $14.9 billion, with a more moderate rate of 3.4 per cent from 2012.

China's exports to the European Union face challenging conditions. A stalled recovery, ageing population, monetary challenges and high unemployment prevent the European Union from rebounding as a major importer. According to EU statistics, from 2009 to 2013, the average growth rate of imports from China was 6.8 per cent, against an average growth rate of its exports to China of 15.6 per cent. In fact, the growth rate of imports from China was negative in 2009, 2012 and 2013, at –13.6 per cent, –1 per cent and –4.1 per cent respectively (EC 2015). The drawn-out economic recovery of the European Union hardly offers a promising future for bilateral trade.

Emerging economies' growth has decelerated to their slowest pace since 2008, or pre-GFC. Weak domestic demand and currency depreciation since May 2013 leave even emerging economies unable to import at previous levels. In sum, China's export-oriented growth model faces an unprecedented challenge in the face of shrinking global demand.

Domestically, China also faces the challenge of adjusting to a new balance between investment and consumption. In the past three decades, investment has served as the other engine of Chinese economic growth. Investment currently accounts for nearly half of GDP—well above the peak of about 40 per cent at a similar stage in South Korea and Taiwan. While investment remains high, 'the marginal contribution of an extra unit of investment to growth has been falling, necessitating ever larger increases in investment to generate an equal amount of growth' (Lee et al. 2012: 16). Over-reliance on investment offers diminishing returns, and is unsustainable especially following the excessive investment induced by the RMB400 trillion stimulus program implemented in the aftermath of the GFC in 2008.

While greater domestic consumption is being encouraged, this will hardly ignite economic growth. Household final consumption in China in 2012 was 38.2 per cent of GDP—up only marginally from 36.7 per cent in 2006, despite rapid economic growth (OECD 2014: 39). This level is much lower than the average for OECD countries. Striking a sustainable balance between investment and consumption is a focus of China's ongoing domestic economic reforms.

In light of this challenging set of conditions, official figures suggest China's economic growth rate in 2014 was 7.4 per cent—the lowest since the 1990s. The current economic slowdown, however, could benefit China in the long run if it is used as a springboard for reforms that successfully and sustainably shift the country's growth model. In this way, the 'new normal' era requires adjustments in domestic economic policies and also in externally oriented trade policies and strategies. Moreover, trade strategies that are compatible with these domestic conditions will help China to achieve a stable and successful growth model shift. Areas of relevance to these adjustments are explored in the next section.

Changing facets of the Chinese economy

The GFC in 2008 has deeply changed the shape of the global economy. For China, it forced a reconsideration of its growth model and pushed forward related domestic reforms. Indeed, it is also offers a turning point through which China is renavigating its role in the world economy.

Moving up global value chains

The proliferation of multinational companies investing in China not only drove China's economic growth, but also created opportunities for Chinese businesses to plug into global value chains (GVCs). Components were exported to China and final products were cased in China, and vice versa. As a result, China has become an integral part of Asia's regional production networks.

Early in China's broader economic transition, Chinese exports were famously characterised as cheap clothes, shoes and low-value-added products. Chinese industries were therefore positioned at the low end of the GVCs, with the interest margin for Chinese companies being accordingly minimal; however, 'benefiting from GVCs depends on how much value a country creates in the GVCs' (OECD 2013). In the face of sluggish demand for those products, the Chinese economy and Chinese companies now need to figure out how to add more value to the GVCs.

Innovation is part of the story of moving upwards in GVCs. This also helps Chinese companies maintain competitive advantage in the face of increasing pressure from labour costs. Chinese companies are already successfully taking action in pushing for higher status within GVCs. The 2014 world intellectual property report, the flagship publication of the Geneva-based World Intellectual Property Organization (WIPO), notes that China filed 32.1 per cent of the 2.6 million global patent applications in 2013, making it the greatest total patent filer in the world, followed by the United States (22.3 per cent) and Japan (12.6 per cent) (WIPO 2014: 12). In addition, Chinese foreign-oriented patents have surged since 2000, by an average annual growth rate of 40 per cent between 2000 and 2005, and 23 per cent since 2005 (WIPO 2014: 2).

The significance of innovation has, in fact, been written into China's national economic strategy. Innovation is intended to be a new driving force for growth and for increasing Chinese competitiveness in the world economy. Accordingly, subsidies and policy support from both the central and local governments are intended to encourage companies to increasingly engage in research and development (R&D) activities.

Becoming an outbound investor as well as a recipient investor

Inbound FDI has served as an important driver of China's economic growth in the past three decades. China became one of the hottest investment destinations in the world. In 2014, China attracted US$128 billion in foreign investment, reflecting a moderate increase of 3 per cent on the previous year. That year, China also surpassed the United States to become the largest recipient of investment in the world (UNCTAD 2015: 1).

In parallel, the recent rapid increase in Chinese outward foreign direct investment (OFDI) is also striking. In 2014, Chinese OFDI reached US$102.9 billion—up 14.1 per cent on the previous year. At this rate, Chinese OFDI will soon exceed its FDI. Having been a large capital-recipient country, China has become an important investor in the world economy.

Within that broader trend are tendencies that reflect Chinese companies seeking to develop advanced technologies through a merger and acquisition (M&A) process. For example, it is reported that PetroChina and China National Offshore Oil Corporation (CNOOC) have signed a few agreements with Western transnational corporations (TNCs), including Shell. Some of these agreements include articles on technological assistance and support (UNCTAD 2014b: 12). Concurrent with expanding market size and maximising business opportunities, Chinese companies are investing globally in a manner that emphasises narrowing the technology and management gaps with companies in developed countries. This is a critical step for Chinese companies undergoing a process of globalisation.

At the national level, Chinese OFDI is also expected to grow with the implementation of the 'one road and one belt' initiative. A $40 billion 'Silk Road Fund' has been founded to support investment in the infrastructure of developing countries. In general, Chinese companies are being encouraged to invest abroad and compete in the global market. It is hoped that massive investment by Chinese companies abroad will unlock opportunities for China to evolve from a country that is 'merchandise exporting' to one that is 'capital exporting'.

Free trade zones and other opening-up measures

Transition from export orientation poses many challenges for China's economy. There is no single prescription that can offer a detailed picture of what China's economy will become in the future, so China's government continues its usual practice of learning by doing.

One such area of experimentation is the practice of free trade zones (FTZs), which set aside an area for trial of innovative trade, investment and financial policies. The idea is to provide 'replicable experience' for other regions and the national economy as a whole for further liberalisation. The Shanghai Pilot Free Trade Zone, which was approved by the State Council in August 2013, is the pioneer for exploring approaches to achieving deepening reform and further opening in the current economic context. Its practices include granting investors 'national treatment' except for investment items listed in the 'negative list', and also simplifying customs procedures. These are novel policy instruments for both national and local governments.

Particularly noteworthy is the approach to the 'negative list', which has been explicitly written into the draft Foreign Investment Law. This approach fundamentally changes the traditional Chinese system of governing foreign investment. Under the new rules, foreign investors can enjoy pre-national treatment unless they fall into a category on the negative list. That is, a clear and transparent framework is now provided for foreign investment. In parallel, foreign investors can also benefit from a simplified registration system that removes the traditional lengthy approval process. Despite some criticism, the draft Foreign Investment Law indicates the arrival of a more transparent, stable and sophisticated system of governance of foreign investment (Pan 2015).

In the footsteps of Shanghai, Fujian, Guangdong and Tianjin are the recently announced second group of experimental FTZs. In addition to replicating the successful experience of Shanghai, these zones are expected to contribute to a more open Chinese economy, and to explore a new model of regional cooperation and a rule-based business environment. It is also hoped these three new FTZs will serve as hubs of regional economic growth and offer useful experience to facilitate regional development. In so doing, they should also be able to provide experience in responding effectively to the changing dynamics of international trade.

Changing dynamics of international trade rules

Failure of Doha Round negotiations in the WTO

At the end of the twentieth century, the establishment of the WTO was one of the greatest achievements of the international economic system. The agreements made under this multilateral trading system have had extensive influence on its 160 member countries. Under three pillars—trade in goods, services and intellectual property rights—the WTO has brought high-level liberalisation to international trade rules. In addition, the WTO's rule-based dispute-settlement system has earned a reputation for efficiency and effectiveness in settling trade-related disputes between member countries.

On the other hand, and as highlighted by Petersmann (2005: 649), multilateral trading is like a bicycle that has one wheel subject to regular negotiation. Through WTO negotiations, trade rules are updated and member countries can be motivated to seek changes in the multilateral trading system. The stalemate of Doha Round negotiations, however, has stalled that system. Confident of success more than a decade ago, negotiators proposed an agenda based on development issues for the Doha Round negotiations. Yet, the round has run into problems due to the divergent interests between developed and developing countries (Cho 2010: 574). Moreover, the 'single undertaking' principle—which requires universal agreement of member countries on an issue—makes the negotiations extremely difficult. At the ministerial conference in Bali in 2013, however, some modest progress was achieved on trade facilitation, reduction of import barriers from least-developed countries (LDCs) and on food security programs in developing countries. The reality is, however, that member countries are struggling to wrap up the Doha Round, and hope among members for agreement on substantial rules is slim. The multilateral trading system is struggling to provide new trade rules.

The proliferation of regional trade negotiations

In the last decades of the twentieth century, another remarkable, new phenomenon in the global economy was the emergence of GVCs. As they change the shape of global trade and investment, GVCs are now among the leading causes of the proliferation of regional trade negotiations.

With advances in technology reducing transportation and communication costs, multinational companies have in recent decades been able to operate with branches across countries, including developing countries. Specifically, production lines are split across countries with the location of each process based on comparative advantage, such as in cheap labour. In turn, a single product is no longer made within one country. Rather, production is an incremental process across many countries that provide different components of the production process.

Removing barriers to customs and investment, and facilitating the activities of value chains, is thus now essential to creating trade and bolstering the prosperity of the economy in the twenty-first century. It is estimated that reducing barriers in GVCs could increase global GDP by nearly 5 per cent and global trade by 15 per cent (World Economic Forum et al. 2013: 13). Existing trade rules, however, are built on the perception of trade 'at the border'. Concepts such as tariffs, rules of origin and so on reflect a way of thinking in which products are labelled as being from a single country, rather than the combined effort of many countries. In the twenty-first century, trade rules that advocate tariff reductions and quota elimination are important, but insufficient to bolster trade. The expansion of GVCs has thus led to calls for changes to create new rules that better suit the structure and needs of global trade (Baldwin 2011: 8–9).

Amid this dynamic, the deadlock of the Doha Round of negotiations has helped create a trend among member countries to turn to regional trade negotiations. The world's greatest traders—China, Japan, the European Union and the United States—have all sought solutions in regional talks. As noted earlier, there are three leading regional negotiation initiatives under way: the RCEP, TPP and TTIP. Two of them—RCEP and TPP—are concentrated on the Asia-Pacific, reflecting the well-developed and lucrative supply chains in the region, and creating common interest for countries to push for the negotiation of more sophisticated trade rules that are compatible with local production networks.

In contrast, the TTIP focuses on divergence within and duplication of regulatory policies. It seeks to create a more specific and subtle set of trade rules based on business sectors that reduce divergence and duplication across domestic laws. The European Union and the United States are already working on divergence within related issues, such as food safety and automobile parts. They hope to use the TTIP as the 'standard makers, rather than standard takers' (Bollyky and Bradford 2013). Through a more united regulatory approach, the European Union and the United States hope to ensure other countries gravitate towards their joint standards, despite the shift of economic power to emerging economies.

As of April 2015, none of these three negotiation platforms has borne substantial fruit. Although the TPP is moving towards a conclusion, its content is still unclear due to issues with the Trade Promotion Authority and disagreement within the US Democratic Party. The RCEP agenda also seeks to conclude negotiations by the end of 2015; however, there are many issues needing resolution before a final deal can be reached. The TTIP appears to be a secondary priority on the United States' trade agenda this year—after the TPP deal.

A call for new trade rules in the Pacific Rim

In the Pacific Rim, while RCEP and TPP complement each other in terms of their membership scope and issue coverage, they are in competition to be the first to offer an update to the international trade rules of the WTO. In turn, the outlook for international trade rules varies greatly, depending on whether the RCEP or the TPP is signed first.

RCEP negotiations include 10 Association of South-East Asian Nations (ASEAN) members and Australia, China, India, Japan, New Zealand and South Korea. These are big trading partners within the region. The negotiation agenda covers an extensive range of issues, such as tariff reduction, services, investment and intellectual property rights protection. RCEP's aim is to further reduce tariffs among member countries, to grant more market access within service sectors and to create a liberal, facilitative and competitive regional investment environment. Negotiations are taking place based on the current structure of the ASEAN+1, but with improvements in many aspects. The RCEP negotiations engage 16 countries so as to make RCEP rules comprehensive and of high quality, reflecting the collective determination to more deeply integrate the various national economies. The negotiation agenda incorporates sensitive issues, including competition. The competition issue was once raised in multilateral trade discussions in the Singapore Round of negotiations of the WTO. It was removed from the agenda, however, due to opposition from developing countries. It represents remarkable progress that it can now appear on the agenda of RCEP, even though most of the participants are developing countries. Despite the pursuit of comprehensive liberalisation, the guidelines of the RCEP also address the issue of flexibility by 'taking into consideration … the different levels of development of participating countries'.[2] The negotiations will consider country differences and allow special and differentiated treatment for LDCs.

Unlike the RCEP, the TPP purports to create 'twenty-first-century high-level international trade rules'. Led by the United States, the TPP is being negotiated by 11 other Asia-Pacific countries: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam. The TPP seeks comprehensive coverage of issues, including services, investment, intellectual property rights, state-owned enterprises (SOEs), the environment and labour. While improving the level of rights based on WTO rules, such as protection for investors and intellectual property rights, it also intends to reduce tariffs to zero and expand market access in service sectors.

More ambitiously, the TPP aims to write new disciplines into international trade rules. It addresses competitive neutrality and regulates SOEs. It also imports environmental and labour-related elements into trade law frameworks. Specifically, it attempts to add the environment and labour costs into the cost of products so as to factor these impacts into the competitiveness level of products. Developing countries have expressed concern that TPP negotiation areas will make them less competitive. Concerns have also arisen about selective rule proposals, such as the extension of intellectual property right protection to pharmaceutical products, which could favour developed countries. The TPP is being pushed by the United States, and this makes it a struggle for developing countries to protect their interests. Negotiators are still working towards a final deal.

If agreed by negotiating countries, the TPP could become the template for future international trade rules. By utilising the TPP, the United States could maintain its lead in international trade rule-making. In this way, the TPP serves as a critical instrument for the United States to achieve its goal 'to be involved in

2 Guiding Principles and Objectives for Negotiating Regional Comprehensive Economic Partnership, November 2013.

the discussions that could shape the future of this region and to participate fully in appropriate organizations as they are established and evolve'.[3] These rules are used to secure the competitiveness of American companies globally and to regain leverage for the US economy. In a geopolitical sense, the TPP also serves to unite the United States and its allies through economic ties and adds momentum to political bilateral and regional relationships. It is understood to be the economic pillar of the United States' 'rebalancing' policy in the Pacific Rim.

Despite its increasing trade power and enthusiasm to join international trade rule-making, China is currently excluded from TPP negotiations. Chinese high-level officials have expressed interest in joining the negotiations to deepen China's integration with other economies (Tiezzi 2014). Despite this, it is appears China will not be allowed to join in drafting the new international trade rules under the framework of the TPP.

The RCEP serves as an alternative for China, though China and other negotiating countries have a long way to go to reach an agreement. The rules of RCEP will be not as ambitious as the TPP's, but this could serve as a middle ground towards consensus on a more ambitious trade package like the TPP. In his address to the 2015 Boao Forum for Asia, Chinese President Xi Jinping re-emphasised the significance of concluding the RCEP deal by the end of 2015. Hopefully, Chinese facilitation can help to induce accelerated negotiation of the RCEP towards agreement. We will see which is the first agreement to update the trade rules in the Pacific Rim.

Chinese trade negotiation options

Cards in China's hands

Multilateral approaches

Joining the WTO in 2001 has significantly benefited Chinese economic growth in the past decade. It also saw China deepen its integration with the global economy. As the world's largest exporter, China should now be part of trade negotiations and write its will into the system of international trade rules. It wishes to seize the opportunity during this round of mega-regional trade rule negotiations by joining the various negotiating arenas.

3 Remarks of President Barack Obama at Suntory Hall, Tokyo, 14 November 2009.

The WTO is the fundamental platform for negotiating new trade rules. As a proponent of multilateralism, China supports the significance of the WTO's legislative function in evolving new rules. China has actively participated in the Doha Round negotiations. It has also worked closely with the United States and India on the divergence between developed country and developing country issues. It signed the agreement on trade facilitation at the Bali ministerial conference and pushed for its conclusion when the agreement was struck in 2014.

China is also an active participant of plurilateral agreement negotiations inside the WTO. Given the stalemate of the Doha Round, the plurilateral approach has emerged in the form of groups of like-minded WTO member countries negotiating on selected issues. Thus far China has entered into negotiations for the Information Technology Agreement and Government Procurement Agreement. China has also expressed its interest in the Trade in Services Agreement (TISA) and hopes to become a negotiating member. It has, however, so far been excluded due to the concerns of some developed countries, including the United States. Indeed, some of the issues covered in these negotiations are also sensitive for the Chinese economy and could pose challenges to the current structure of Chinese governance. The Chinese Government has realised that being among the rule-makers is essential to protecting its own interests in the global context. Being a signatory to negotiations within the WTO would allow China to be present when the important issues are being considered. The plurilateral agreements negotiated by a group of members will apply to all WTO members, if accepted by all the other WTO members. Multilateral negotiations, despite their slowness, can be effective instruments for advancing trade-related issues.

Regional approach

Given its core interest in the Asia-Pacific, China also actively participates in regional negotiations of new trade rules. It engages in discussions towards building free trade areas with neighbouring countries with a view to having a positive impact on both regional economics and geopolitics.

In East Asia, free trade agreement (FTA) negotiations between China, Japan and South Korea began in 2012. The seventh round of negotiations was completed in April 2015. China and South Korea were able to reap an early harvest by signing a bilateral FTA—China's most substantive FTA, covering the largest trade volume and the most comprehensive range of issues.

In addition, China is negotiating an FTA with the Gulf Cooperation Council, which consists of Bahrain, Oman, Kuwait, Qatar, Saudi Arabia and the United Arab Emirates (UAE). The negotiations were stopped after being launched in 2009, but resumed in 2013. Bilateral negotiations between China and each Gulf Cooperation Council country continue. FTAs serve as important instruments for strengthening economic ties between China and signatory countries. Under the 'one belt and one road' initiative, it could be expected that there will be a proliferation of FTAs and bilateral investment treaties (BITs) between China and its neighbours in the near future. Of course, preferential trade is not multilateral free trade and cannot substitute for its benefits.

The RCEP is another trade-related negotiating platform in the Asia-Pacific, incorporating 16 countries. Production networks within this region are tightly interconnected. China has put great emphasis on RCEP negotiations to facilitate further expansion of regional production networks and strengthen China's ties with South-East Asian countries in particular. It might not be easy to wrap up these negotiations quickly, however, due to the different development levels and interests of the countries involved. An alternative accelerated track lies in China having started negotiations with ASEAN countries on an upgraded version of the ASEAN–China FTA, which is at the top of the Chinese trade negotiation agenda.

At the 2014 Asia-Pacific Economic Cooperation (APEC) leaders' gathering in Beijing, China addressed the importance of building a free trade area among APEC member countries. The feasibility study on an FTA for the Asia-Pacific (FTAAP) will be launched in response. In addition to the RCEP, therefore, through the FTAAP and the ASEAN–China FTA, China could play a bigger role in shaping trade rules and the regional economic architecture in the ongoing process of Asia-Pacific economic integration.

China's FTAAP initiative also highlights that China is willing to work with the United States on drafting new trade rules towards broader Asia-Pacific economic integration. Although the original FTAAP idea was first proposed by the United States, the United States is now preoccupied with concluding the TPP. Even where the negotiations for an FTAAP are launched, the United States would have these built on the TPP negotiations—that is, with its clear emphasis on the TPP, the United States seeks to influence the general structure of the FTAAP and apply the TPP's rules to a larger group of APEC countries. Since the FTAAP's negotiation agenda has not yet been clarified, it will require a lot of collaboration between China and other countries to make the FTAAP a reality.

Bilateral approaches

Among 15 FTAs signed by China as of April 2015, almost all are bilateral agreements, except the FTAs agreed with Hong Kong, Taipei (China) and Macau (Table 15.1). China has signed FTAs with a broad range of Asian countries, including ASEAN, Australia, Korea, Pakistan and Singapore. China also has FTAs with Chile, Costa Rica, New Zealand and Switzerland. FTAs now in the pipeline will boost Chinese economic integration with Japan and Norway.

Table 15.1 FTAs signed by China as of April 2015

Asia-Pacific (1976)	Developing–developed
China–Thailand (2003)[a]	Developing–developing
China–Hong Kong, China (2003)	
ASEAN–China (2004)	Developing–developing
China–Chile (2006)	Developing–developing
China–Pakistan (2006)	Developing–developing
China–New Zealand (2008)	Developing–developed
China–Singapore (2008)	Developing–developed
China–Peru (2009)	Developing–developing
China–Macau, China (2009)	
China–Taipei, China (2010)	
China–Costa Rica (2010)	Developing–developing
China–Iceland (2013)	Developing–developing
China–Switzerland (2013)	Developing–developed
China–Australia	Developing–developed
China–Korea (2015)	Developing–developed

[a] It was later included in the ASEAN+China.
Source: Authors' compilation based on information from China's Ministry of Commerce.

Chinese experience as a WTO member, which helped to massively increase China's exports in the past decade, made it an enthusiast for free trade. While preferential trade agreements have few of the advantages of genuine free trade, and have disadvantages as well, China has tended to seek to replicate that success by gaining more market access and by further reducing tariff levels through bilateral FTAs with countries in the region. In the early days of these FTA negotiations, China applied an individual approach to negotiations on goods, services and investments to accelerate implementation, including in the ASEAN–China FTA's Early Harvest Program. During this period, Chinese FTA emphasis was on trade in goods, particularly tariff reductions. The more complicated Singapore Round issues—referring to an earlier WTO multilateral negotiation round, including government procurement, competition and trade facilitation—received little attention.

A more proactive stance by China emerged in FTAs signed with New Zealand and Singapore in 2008. These negotiations had multiple focuses in addition to the liberalisation of trade in goods. In particular, China put more emphasis on the negotiation of services and Singapore Round issues. The coverage of services and liberalisation steps was more vigorous and comprehensive compared with earlier negotiations. Several Singapore Round issues, such as trade facilitation, were on the negotiation agenda, although competition and government procurement proved too sensitive to address. China has, however, recently taken a more comprehensive and vigorous approach to FTAs signed with developed countries. For example, China's FTAs with Iceland and Switzerland, each signed in 2013, and with South Korea in 2015, have more comprehensive coverage in goods, services and investments, especially with respect to Singapore Round issues.

Chinese issue-related FTA strategies

Bilateral investment treaties

Following China's shift towards becoming an important outbound investor, it urgently needs to update its BITs with its trade and investment partners. As of April 2015, China has signed 145 BITs with a wide array of countries (UNCTAD 2014a). Many of these BITs—particularly those signed in the early days of China's opening-up—were drafted from the stance of protecting China's inbound investment recipient interests. For instance, the BITs intentionally narrowed the scope of arbitration and restricted the availability of use of ad hoc arbitration in the International Centre for Settlement of Investment Disputes (ICSID), unless disputes were related to compensation over expropriation and nationalisation (Heymann 2008: 515).

China's BITs have evolved significantly in the past decade, offering more balance between investor and recipient protections, including a more fully fledged dispute-settlement provision. 'While it has not yet converged on U.S. "high-standard" BIT practice, it has come closer' (Gantz 2014: 28). Recent BITs signed with developed countries, such as Canada in 2012, represent remarkable progress in the way China addresses national treatment, most-favoured nation (MFN) treatment and dispute settlement, though there have been some reservations. The enlarged scope of these BITs indicates a clear shift for China in its negotiating stance, based on its role changing from being merely a recipient to being also a major outbound investor. The ongoing BIT negotiations with the United States will, when completed, reflect China's most advanced such regulations.

The negotiations for BITs or for investment chapters within FTAs will be among the priorities of Chinese trade negotiations in the future, especially under the umbrella of the 'one road and one belt' strategy. Cautious agreement on reciprocal national treatment, MFN and dispute-settlement mechanisms in host countries will benefit Chinese investors in the long run by offering accessible, stable and predictable investment environments. This will also help to ensure a successful transition from the tradition of government-led overseas investment to private outward investment while adhering to the relevant international rules.

Last, China's change in its stance in BIT negotiations leaves room for it to join high-level FTAs. Building a predictable and stable, investment-friendly environment will be in China's and China's investors' favour. Despite many contentious issues in the high-level trade rules, the shared concern over protections for investors could create common ground for China and other developed countries to work together. The consensus on investment issues will pave the way for China to join the negotiations for high-level international trade rules.

Services

According to WTO statistics, China's services exports reached $205 billion in 2013. With a steady annual rate of increase of nearly 8 per cent, Chinese exports in services cover 4.4 per cent of total world services exports. China's imports of services in the same year were $329 billion, reflecting a higher share—some 7.52 per cent—of total world imports. China's services imports also increased more sharply, at an annual rate of 18 per cent (WTO 2014).

Transportation and travel explain most of the increase in services trade. More importantly, value-added services are contributing increasingly to GDP—up to 46 per cent in 2013 from 32 per cent in 1992 (World Bank 2015). The expansion of GVCs integrates not only Chinese component manufacturers into the global economy, but also the service providers of these production lines. As a huge market that holds much promise for China's middle class, there is great potential for a boom in trade in services, both domestically and globally. This is particularly true in the global context given that China's advantage in providing cheap labour is diminishing. Indeed, China faces a great opportunity to expand its services into the region and the world.

In that context, China will also embark on negotiating service agreements with its trading partners. Its activeness in participating in the TISA, as mentioned above, is part of this story. The emphasis in negotiations for services is first on opening market access in the transportation and travel sectors; the Chinese Government faces few difficulties to open domestically. Liberalisation of the financial and telecommunications sectors is expected to gradually increase in the pace and prioritisation of domestic reforms. This liberalisation of services trade also could provide China with a new engine for its economic growth.

New sensitive issues

Some new sensitive issues—such as SOEs, the environment and labour—pose challenges for China in twenty-first-century trade negotiations. As outlined above, these issues are important impediments to China joining high-level trade negotiations such as those of the TPP. Handled badly, they can also be impediments to genuinely free trade. Environment was once an area in which

Chinese standards once diverged from most developed countries, but today Chinese standards in many areas exceed those of some countries, including Australia, which are expected to be members of the TPP. If the TPP is concluded, the pressure for China to tackle labour standards in particular will increase. China's commitment to addressing these issues, however, is also subject to progress in Chinese domestic reforms in each relevant sector. If the TPP cannot be concluded in the near future, this will buy China time to proceed at its own pace on domestic reforms in related issues.

It is noted, however, that Chinese negotiators will pay more attention to the regulation of these new issues in such high-level trade negotiations. Due to the sensitivity of these issues, the TPP, even were it to be concluded, might not be able to set binding rules for members. China could address these rules as non-binding, or seek a transitional period in which to adapt to relevant rules, in order to minimise its exposure to any negative consequences. Despite the sensitivity and complexity of these issues, China might consider adjusting by putting emphasis on domestic reform and negotiation strategies.

Conclusion: To work towards converging on a trade deal

The international trading system is at a crossroad, thanks to deadlock in the multilateral Doha Round of WTO negotiations and the parallel emergence of a few mega-regional trade negotiation platforms. The mega-regionals, which have attracted a lot of attention, could turn out to be a stumbling block for genuinely global free trade, or could pave the way to reaching a multilateral deal within the WTO's frameworks. It is important that they pave the way, and that major participants in regional preferential trading areas keep this at the front of their minds. Divisions among trading blocks, as reflected in the shape of these mega-regional negotiations, pose uncertainty for the international trading system and suggest there could be delays in adapting to these trading dynamics. Though geopolitical concerns could justify such divisions, large traders need to work together to converge on a trade deal towards the goal of evolving the new trade rules that are needed for twenty-first-century prosperity and economic security. Through this process, China will play an active role and seek to expand its influence to match its economic power. Any attempt to exclude China is unwise and would be unsuccessful, as the story of the Asian Infrastructure Investment Bank proves.

China seeks to work with its large trading partners, such as the United States and the European Union, towards taking responsibility for collectively upgrading international trade rules. The internal reform of the Chinese economy and its changing role in the global economy provide common ground for China, a large developing country, and developed countries to work on their divergence and to agree to a new set of rules. As an important and indispensible player in the Pacific Rim as well as the world, China is expected to take on a more active role in the evolution of a twenty-first-century trading system.

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