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**From Political Alliance in China's Conception to
Comprehensive Partnership in Building: the
Relations between China and the European
Community/European Union**

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Summary

The analysis of evolution of the relations between China and the EC/EU from the mid-1970s to China's accession to the WTO demonstrates that bilateral relations have undergone a special development. The bilateral relationship was begun with China's conception of making political alliance with a 'unified Europe', shifted to the pursuit of actual economic benefits, and further develops to the building of a comprehensive partnership. Despite the importance of external constraints, the fundamental factors causing this development were the changing domestic constraints in deepening interdependence. This development, in different periods and in different domestic contexts, had different significances for each of the parties. But the pursuit of economic benefits has always been the primary goal for both of them.

The needs to attain new domestic goals in the transition period brought about a new European preference in China's external relations. But developments in China have both provided opportunities for and posed challenges to the EU. Economic interests define the EU's policy adjustments and policy-scope broadening, both as response to domestic demands and as reactions to China's policy practices in a deepening interdependence. The sole option to promote and protect European interests in China is to encourage China's further integration into the world economy. The establishment of a WTO rule-based bilateral economic relationship and new comprehensive partnership framework can ensure long-term mutual interests and promote cooperation on some important international issues of shared interests.

Zusammenfassung

Die Analyse der sich entfaltenden Beziehungen zwischen China und der EG/EU seit Mitte der 70er Jahre bis zu Chinas Beitritt zur WTO (Welthandelsorganisation) zeigt, dass die bilateralen Beziehungen eine spezifische Entwicklung durchgemacht haben. Die bilaterale Beziehung begann, als China das Konzept entwarf, eine politische Allianz mit einem vereinten Europa einzugehen, sich dann änderte mit dem Ziel nach ökonomischen Nutzen und sich dann weiter entwickelte zum Aufbau einer umfassenden Partnerschaft. Trotz der Bedeutung der externen Beschränkungen, waren die fundamentalen Faktoren, die diese Entwicklung verursachten die sich verändernden einheimischen Zwänge in der sich intensivierenden Interdependenz. Diese Entwicklung in verschiedenen Perioden und in verschiedenen häuslichen Zusammenhängen hatte unterschiedliche Bedeutungen für jeden der beiden Partner. Aber das Streben nach ökonomischem Nutzen war immer das bedeutendste Ziel für beide von ihnen.

Die Notwendigkeit, in der Übergangsphase neue häusliche Ziele zu erreichen, führte zu einer Begünstigung der Europäer in Chinas Außenbeziehungen. Aber die Entwicklungen in China haben sowohl günstige Gelegenheiten als auch Herausforderungen für die EU geschaffen. Wirtschaftliche Interessen bestimmen die EU-Richtlinien und deren Ausweitung. Beides als Antwort auf einheimische Nachfragen und Reaktionen auf Chinas politische Praxis in der sich intensivieren gegenseitigen Abhängigkeit. Die einzige Option, die europäischen Interessen in China zu fördern und zu schützen, besteht darin, China mehr in den Welthandel zu integrieren. Der Aufbau einer gemeinsamen wirtschaftlichen Beziehung basierend auf den Regeln der WTO und im Rahmen einer umfassenden Partnerschaft kann die langfristigen gegenseitigen Interessen garantieren, und die Kooperation in einigen wichtigen internationalen Angelegenheiten von gemeinsamem Interesse fördern.

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Finally, this dissertation is dedicated to the memory of my parents.

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I. Introduction

This dissertation is an empirical study describing and analysing the evolution of the relations between the People's Republic of China (PRC) and the European Community/European Union (EC/EU) from the mid-1970s to China's accession to the WTO. It has two fundamental purposes. First, it aims at supporting the following thesis: In China's external relations there are no 'overall interests and objectives'. The interests in and objectives of China's policies towards other countries as well as the EC/EU are always defined in terms of its concrete external policy goals at different periods and in different external and domestic contexts. While the relations with the EC/EU have different perceived and actual implications in China's external relations due to complicated external and internal factors, the pursuit of maximum economic benefits has been the constant principal objective. Despite the fact that external constraints in different periods have always been factors behind the setting of policy goals to various extents, the elements within the state have increasingly become main determinant in the setting of external policy goals and policy implementation. The relations between China and the EC/EU are subject to China's external policy goals and contribute importantly to the attainment of China's domestic development objectives. This thesis is contrary to that maintained by Harish Kapur in his pioneering study of the relations between China and the EEC.¹

The pursuit of maximum economic benefits has always been the constant and principal goal of the policies of the EC/EU towards China. The EU's policies primarily aim at promoting and protecting European economic interests, for bilateral exchanges directly and increasingly influence the interests of EU sub-systemic actors, such as transnational companies and European sectoral associations. Changing Chinese contexts and its policy practices have compelled the EC/EU, while seeking to maintain policy continuity, to continually adjust its policies and broaden policy scopes in order to facilitate attaining the goals of maximising economic benefits. European policy practice indicates that the place China holds in the EU's external relations has also undergone changes in accordance with China's altered relative

¹ Kapur concluded: (...), the EEC had become a major economic centre (...) For the Chinese, who had erroneously supposed that this evolution was taking place in the early 1960s, though it was unmistakable in the 1970s, the new autonomous centre – if encouraged – might serve overall Chinese interests and objectives. (Harish Kapur 1985, p. 24) So far his viewpoint has not been questioned and challenged by the literature. One recently published dissertation sought to reveal Chinese misperception of European integration in the 1980s and the 1990s by analysing of the perception of the Chinese 'influential elite' concerning Western Europe. (Stefan Friedrich (2000), *China und die Europäische Union : Europa's weltpolitische Rolle aus chinesischer Sicht*)

position in the EU's external relations. This change was mainly caused by China's efficient export-promotion and foreign-investment policies. The European approach shifted from various preferential trade measures to promoting China's further integration into the world economy subject to accelerating its smooth transition and maintaining high economic growth. The second, and even more important, task is to provide a systematic study of the development of the relations between China and the EC/EU from the mid-1970s to China's accession to the WTO in 2002. The scholarly contribution this study hopes to make to the literature on the relations between the EC/EU and China will be in terms of the following. First, it concentrates on the policy areas within the actual policy competence of the two parties and provides a systematic description and analysis of policy changes in the main issue areas in the bilateral relations. Second, it emphasizes the decisive role of China's international policy goals in guiding its policies towards the EC/EU. Third, it demonstrates that for each of the two parties new domestic factors in the process of transition have significantly influenced policy adjustments, policy scope broadening and policy practice. Fourth, it seeks to reveal an interaction on the part of policy practice by the two parties in order to facilitate understanding how the bilateral relations have developed. In short, it seeks to provide a new approach to this theme within a comprehensive analytic framework by combining a description of policy practice as revealing the policy interactions between the two parties, analysis of the decision-making structure/process in different domestic contexts of the two sides, and isolating the principal factors within the state or/and domestic factors causing policy changes in different periods. So far no existing study has attained this goal.² Thus this study seeks to fill the gap between the importance of the bilateral relations and the current insufficiency of studies dealing with this theme.

The key factor supporting my thesis is that it draws a wealth of convincing material. The material must be conducive to the following goals: to explain why China resorted to an unexpected policy practice towards Western Europe as well as European integration in the 1970s and why the EC's importance in China's external relations changed in a new Chinese context created by the launch of the Open Policy; to demonstrate how China sought to maximise benefits in different domestic contexts by effecting adjustments in external economic policy and to reveal the factors that led to such policy adjustments; to describe

² Harish Kapur, *China and the European Economic Community: the New Connection*, Martinus Nijhoff, 1985; Putnam Mundy Ebinger, *The Politics of Potential: the Relations of the People's Republic of China and the European Community and Its Member-States France and Great Britain, 1969-1979*, (Tufts University, 1988, unpublished dissertation); Xiao Zhi Yue, *The EC and China*, Butterworths, 1993; and Richard L. Grant (ed.), *The European Union and China, a European Strategy for the Twenty-First Century*, The Royal Institute of International Affairs, 1995; Stefan Friedrich, *China und die Europäische Union: Europas weltpolitische Rolle aus chinesischer Sicht*, Institut für Asienkunde, 2000.

different Chinese policy practices towards the EC/EU in different Chinese domestic contexts; and to reveal how the EC/EU adjusted its policies towards China in different European and Chinese contexts. The policy interactions between the two parties shifted to building a comprehensive and WTO rule-based framework of bilateral relations in order to facilitate cooperation and to ensure actual long-term interests. To attain these goals, this empirical study relies mainly on first-hand material. Concerning the period from the 1950s to the 1970s, the primary source is the Chinese official documents and memoirs of Chinese diplomats published in the latter part of the 1980s and in the 1990s. Most of these materials have not been used by current studies of the relations between China and Western Europe. Some new and different interpretations will be given to such material as other students of this topic have used, e.g. certain articles in the principal Chinese newspapers and journals in the 1960s. Laws, regulations, statistics and documents published by Chinese authorities in the 1980s and 1990s are the principal material drawn on here to analyse how the evolution of the framework of China's external economic institutions has evolved. These documents demonstrate how China pursued maximum economic benefits by various efficient policies, both liberal and mercantilist. Concerning the policies of the EC/EU towards China, this analysis relies mainly on official documents published by the EC/EU. In addition to the principal documents directly relating to the issue of bilateral relations, the Green and White Papers of the EC/EU issued by the Commission in the 1990s concerning various EU policy areas directly and indirectly related to exchanges with China have not been neglected, for they help to reveal the causes behind the EU's policy practices evolving in the case of China.

The principal goal of this empirical study is to reveal how the bilateral relations have been developed, beginning with mutual misunderstanding between the parties but evolving into a comprehensive partnership in building. This will require description and analysis of the policy practices of the two parties and demonstration of how they interacted in different periods. This can be attained only by selecting the key factors in different periods, internal and external. However, while not discounting the importance of external factors, the author argues that internal factors have always been crucial, despite the fact that in some specific external contexts their importance seemed less obvious than that of external factors. Thus, the emphasis of analysis is laid on society as well as the state, on many different types of actors and not just on national governments. Their relative importance differs in different policy areas and in different internal and external contexts. Meanwhile, the importance of external contexts in some specific periods is also emphasised. This will be mainly demonstrated by the selection of independent variables. The factors within the state in the case of China and

domestic factors in the case of the EC/EU are the main independent variables explaining the policy behaviour. They will be further identified according to the questions each part of this dissertation seeks to answer.

The decision-making structure/process acts as intervening variable. Taking account of the fact that some features in China's political system varied in the Mao period and the post-Mao period as well as the fact that this dissertation must deal separately with two different issue areas concerning 'high politics' in the Mao period and actual economic exchanges in the post-Mao period, this study provides two different decision-making models concerning China: the predominance of individuals in the Mao period for the setting of policy goals or guidelines and developing policy networks, whereas in the post-Mao period the state institutions play the central role in external economic policy making and implementation. Concerning the EC/EU, this study seeks to provide a primary analysis of institutional arrangements concerning the major policy areas falling within its competence in the case of China.

In order to test my thesis that the bilateral relations had different actual significations for each of the parties in different periods and within different external and domestic contexts, this study must provide both a description and an analysis with regard to changes in policy goals and in policy practice by each of the parties. The policies of the EC/EU towards China, despite its relatively definitive policy goals and constant policy instruments, underwent obvious changes in the 1980s and the 1990s, as indicated by policy adjustments and policy scope broadening. Such policy changes served both as reaction towards China's policy practice and response to internal demands. However, the changes in China's policy goals and policy instruments as adopted to maximise benefits and facilitate overcoming various adverse socio-economic issues demonstrate that the main dynamics of changes came from China in the transition period. Accordingly, the evolution of bilateral relations is divided into three periods: the Mao period, the post-Mao period and the 1990s.

This study is divided into three parts additional to the introduction and general conclusion. Such an arrangement aims at providing a clear description and analysis of policy developments for each of the two sides, while seeking to reveal the interactions between them. The first part (chapter 2) is a simplified survey of China's relations with the Western European countries as well as with the EC in the Mao period, the idea being to support with convincing material the thesis that China's relations with Western Europe and the EC/EU actually meant different things in different external and domestic contexts. The following independent variables are identified to explain China's policy behaviour in this period: the likely influence of external constraints, the roles of the principal Chinese leaders in the

decision-making process, the ideological bias, China's international strategies, factional conflicts and the principal Chinese leader's interpretation of European integration.

The other two parts provide an analysis of changes in the actual policies of each of the two parties, which are mainly pitched at pursuing the maximum benefits in the bilateral exchanges in different domestic contexts. The second part, consisting of two chapters (3 and 4), describes and analyses China's external economic policy goals and its policy practices towards the EC/EU within the changing external economic institutional framework in the post-Mao period and in the 1990s. Chapter 3 provides an analysis of the evolution of China's external economic institutions after the launch of the market-oriented economic reforms and the Open Policy. It serves both as a Chinese setting for the analysis of China's policy practices towards the EC/EU and as a Chinese background for the analysis of the EC/EU's policy practices towards China. Such policy practices are both reactions to China's external economic policies and responses to the changes in China in the deepening interdependence. Chapter 4 concentrates on the analysis of China's policies towards the EC/EU in this domestic context, namely how China pursued actual benefits in the case of its relations with the EC/EU by increasingly linking its policies towards the EC/EU to the developments within China in the transition period. Domestic socio-economic factors, such as sector interests, regional interests, interests of state-owned enterprises and other emerging societal pressures in the transition period, all of which have become major constraints on China's external economic policies and on the policies towards the EC/EU, are selected as independent variables.

The third part (chapter 5) provides a description of the evolution of the EU's policy practice towards China. In addition to describing and analysing its concrete policy adjustments and policy scope broadening, it also seeks to reveal factors causing such changes in different periods. Such policy practices, both liberal and protectionist, in different Chinese and European contexts, principally aims at maximising economic benefits, meeting demands of various EU systemic and subsystemic actors, and facilitating the building of a WTO rule-based bilateral framework of economic relations. The interests of the following systemic and sub-systemic actors are the main independent variables, e.g. the EU institutional interests mainly relating to the Commission, the transnational companies, sectors lacking international competitiveness, and non-business interest groups.

II. Western Europe in China's Foreign Relations from the 1950s to the Early 1980s: Secondary Enemy, Potential Ally or Economic Partner?

1 The relationship between the PRC and Western European countries in the 1950s, a shift from deliberate aloofness to confrontation

1.1 Establishment of the special Sino-Soviet relationship and formulation of the foreign policy principles in the early period of the PRC

As a consequence of European commercial expansionism, the early encounter between China and Western European countries in the mid-19th century was confrontational. It was dominated at the outset by Western European power politics. Consequently, through a series of unequal treaties concluded between the Chinese governments (mainly the Manchurian Qing regime 1644-1911) and the European powers in the period from the mid-19th to the early 20th century, China was forced to make increasing concessions and to grant Western powers various commercial and political privileges. The combined external and internal pressure facilitated the breakdown of the Manchurian Qing regime.

This situation in the relations between China and the imperialist countries – invasions and allocation of influence spheres between powers continued till the outbreak of the Second World War. In this period, two movements developed one after another in China, Nationalist and Communist. The former emerged as a reaction to the Western dominance in bilateral relations; and the latter was initiated and motivated by a small group of radical Chinese intellectuals with the help of Moscow in the early 1920s. Most of the intellectual Chinese Communists in this period had undergone an ideological shift from Nationalism to Communism. However, even as Communists, learning from the unfortunate past experience in China's relations with the imperialist powers after the mid-19th century, they still retained strong nationalist ambitions of pursuing external security based on material capacity through 'catching-up' with the advanced Western powers, maintaining national sovereignty and territorial integrity, and transforming the weak China into an influential world power conforming to its deeply-rooted brilliant civilisation, enormous size and population. In addition, they are also pragmatists, less restricted by Marxist-Leninist orthodoxy. While trying to seek theoretical support for their practices in the Chinese context, which is different

from that of Europe, they rely more on formulation of their own theories according to the realities in China to legitimise their practices.

The formation of two confrontational blocs after the Second World War compelled Chinese leaders, whether Nationalist or Communist, to pursue a bloc-oriented foreign strategy in order to guarantee external security and ensure support from either of the two blocs for the reconstruction of this war-torn country after the eight-year anti-Japanese war. The foundation of the Chinese Communist regime in October 1949 upon the defeat of the pro-West Chinese Nationalist Kuomintang in the three-year civil war determined China's Communist bloc orientation. As Mao argued, in the context of two-bloc confrontation there was no alternative of taking a 'third road' – the pursuit of neutrality between the two confrontational blocs as in the case of the Yugoslavians.³ The main arguments were to obtain international recognition in order to legitimise the new regime and foreign economic and technological aid for domestic reconstruction.

The Chinese bloc-oriented international strategy in the early 1950s with the principal goal of establishing a special relationship with the Soviet Union in order to facilitate the consolidation of the newly founded communist regime and obtain support for economic reconstruction implied, at least for the time being, the ignoring of the importance of the 'intermediate zone between the Soviet Union and the United States', in which Western Europe was included.⁴ In 1949 the Chinese Communist delegation to Moscow informed Stalin of the two principles of the new Chinese regime in dealing with the relations with the capitalist countries: to struggle with all imperialist countries but seek to benefit from the contradictions between them and to follow the Kremlin on all important international issues. Stalin further proposed that China should not seek to establish diplomatic relations with the Western countries before it became powerful.⁵ Consequently, this led to the decision that the establishment of diplomatic relations with Western countries would not be considered 'even in a rather long period', but that economic exchanges with them should be continued.⁶

³ *Mao Zedong Xuanji (Selected Works of Mao Zedong)* Vol. 4, p. 1362. Two assumptions were critical for this decision. The Chinese Communist leadership assumed that the new Chinese regime would not be recognised by the countries of the West upon or soon after its foundation, and that China could obtain economic and technological aid for economic recovery only from the Soviet Union and other European Communist countries.

⁴ Early in the mid-1940s Mao formulated the idea of an 'intermediate zone' existing between the United States and the Soviet Union. The significance of this idea was that to compete with the United States in the intermediate zone was the best way to weaken it and to defend the socialist force (the Soviet Union). Whether the US enabled to exert control on or encountered opposition from its allies in this zone determined whether US ambition and actions would be constrained or not, and to what extent be constrained. His argument revealed the idea of weakening the US by winning its allies, undoubtedly including Western European countries, through differentiated policy practices. *Mao Zedong Xuanji (Selected Works of Mao Zedong)*, Vol. 4, p. 1193.

⁵ Shi Zhe, *Shi Zhe Huiyilu, Zai juren shenbian (Memoir of Shi Zhe)*, p. 402

⁶ *Mao Zedong Xuanji (Selected Works of Mao Zedong)*, Vol. 4, p. 1325.

In this period, the Chinese Communist leadership completely supported the two-camp theory and its practice.⁷ The importance of this theory was that it rationalised, supplemented by the Cominform as the instrument, Moscow's control of other communist parties and subjection of the national states to the bloc interests.⁸ However, whether the Chinese Communists had won Soviet trust before Chinese direct involvement in the Korean War was questionable, due to the lack of mutual understanding and the Soviets concern that the Chinese Communists would follow the Yugoslavians sooner or later.

The bloc identity and the deliberate maintenance of aloofness from the Western-bloc countries were clearly revealed in the three principles guiding Chinese external relations after the new regime's foundation: *yibian dao* (leaning to one side – establishing and maintaining special relationships with the Soviet Union and the Eastern bloc countries), *lingqi luzao* (starting a new kitchen — diplomatic relations established by the previous Nationalist government would not be recognised and inherited by the new Chinese government without negotiation and all international treaties and agreements entered by the previous government would not be automatically assumed but would be re-examined and in some cases abrogated), and *dasao ganjing fangzi zai qingke* (cleaning up the house before inviting guests — postponing the establishment of diplomatic relations with the Western countries before the new regime was confident of eliminating the Western economic privileges as well as political and cultural influences).⁹

The Sino-Soviet Treaty of Friendship, Alliance and Mutual Assistance of 1950 officially declared the special relationship between these two Communist countries. It specified the duty of mutual assistance in the case of aggression by a third country, the duties not to participate in any alliance or coalition against the other, and the obligation to consult with each other on all important international issues concerning common interests.¹⁰ Additional agreements ensured Soviet economic and technological aid to China. In the framework of this special relationship, according to the allocation of international tasks between Beijing and

⁷ For instance, its firm support for all Soviet efforts in establishing and consolidating the control of the Eastern bloc in this period, such as the expulsion of Yugoslavia from the Cominform and Soviet suppressions of any attempts in Eastern European countries to disengage from its control, could be regarded as the effort of the Chinese Communists to demonstrate their credibility.

⁹ This theory demanded the strengthening of mutual consultation and voluntary co-ordination of action between individual communist parties to wage an uncompromising struggle in all aspects to confront the imperialist camp. See 'The report of Zhdanov on the international situation to the Cominform, September 22, 1947' in Myron Ruth (ed.), *The International Situation and Soviet Foreign Policy*, 1970, pp. 124-139.

⁹ *Zhou Enlai Waijiao Wenxuan (Selected Articles of Zhou Enlai on Foreign Relations)*, pp. 48-50.

¹⁰ Peter Calvocoressi, *Survey of International Affairs, 1949-1950*, Oxford University Press, 1953, London, p. 340.

Moscow, China took the responsibility for supporting the Communist movements in Asia in order that the Soviet Union could concentrate its attention and resources on Europe.¹¹

1.2 The transition from deliberate aloofness from the Western bloc to military confrontation with it

Although Beijing strictly maintained its position of deliberate aloofness from America's European allies, bloc-oriented foreign principles were not equal to foreign policies wholly determined by bloc interests. Beijing sought to retain limited initiatives and policy flexibility towards the countries outside the Eastern bloc and continue low level economic exchanges with the American allies. One outcome of this consideration was the decision by the new Chinese government that Hong Kong's status as a British colony would not be unilaterally changed.¹²

European countries (not including the Eastern bloc countries) were placed into two categories: non-American-ally countries and American allies (Western European countries). For those falling in the first category, it positively and actively responded to their proposal for establishing diplomatic relations, with the precondition that negotiations were needed, thereby confirming the new regime's international status as the sole legal representative of the whole Chinese people. Beijing established diplomatic relations with Sweden, Switzerland, Finland and Denmark in 1950. The establishment of diplomatic relations with these countries undoubtedly did not violate the mutual understanding between Beijing and Moscow in dealing with Chinese external relations.

However, Beijing's ambiguous position on the issue of establishing diplomatic relations with the countries falling in the second category (in Mao's words, all of them had a notorious history of invading China 'from far away' in the 19th and early 20th century) might frustrate its effort to establish and consolidate the special relationship with Moscow, if such an ambiguous position was linked to the pervasive Western confidence in potential rupture between the Chinese and the Soviet Communists. In this respect, Beijing did not show any vagueness and hesitation. It was demonstrated by the guiding line in treating the Western European diplomats remaining in China and in responding to the British proposal to begin the negotiations for establishing a diplomatic relationship.

All diplomatic missions from Western countries still remained in Nanjing, the capital of the defeated Kuomintang regime, upon its occupation by the Communist army. It indicated the

¹¹ *Shi Zhe Huiyilu (Memoir of Shi Zhe)*, p. 412.

¹² Qi Pengfei, in *Zhonggong dangshi yanjiu (Studies of the History of the CCP)*, No. 1, 1997. pp. 55-61.

intention of the West to look for the chance to establish some contacts with the new Chinese government in order to 'have a foot in the door'. The British government, according to its tradition of recognising, but not approving of, governments which exercise effective control over their territories, and from the demand to continue Hong Kong's colony status as well as to better protect its economic interests in China, recognised the new Chinese government in January 1950, although the British decision was criticised by Washington as 'premature'.

The Western diplomats, according to instructions from Beijing, could only be treated as normal foreign citizens residing in China.¹³ Such a decision meant that their diplomatic immunities would not be automatically acknowledged and their activities and communications were restricted. Thereafter, all Western diplomatic missions, with the exception of the British, left China. As for British *de jure* recognition of the new Chinese government without approval of the regime, it was criticised by Beijing as 'an indication of British antagonism towards China'.¹⁴ Negotiations for establishing diplomatic relationship were deliberately postponed.

Beijing's direct military involvement in Korea as well as active support for the Vietnamese Communists in Indochina was the principal cause for the transition of the relations between the new Chinese government and the Western countries from deliberate aloofness to open confrontation. The factors leading to such an active involvement in regional conflicts bordering China were complex. They included: fulfilling the responsibility assigned to Beijing by Moscow to support the Asian Communists, enhancing China's prestige in the Communist camp through the decisiveness of Chinese Communists, helping other Asian Communists gain power in the 'Chinese way'—to gain power from below, and perhaps most important, creating buffer zones in order to obtain an external security environment for domestic economic reconstruction. China's direct involvement in Korea facilitated consolidating the special Sino-Soviet relationship, which led to the ensuring of Soviet economic and technological aid.¹⁵

Compared to the attainment of the above goals, the importance of Western European countries in China's external relations in such a context was regarded as marginal. This was indicated by the fact that the Chinese leadership was clearly conscious of the consequence of

¹³ Zhou Enlai, 'women de waijiao fangzhen he renwu (Our Diplomatic Principles and Tasks)', in *Zhou Enlai Waijiao Wenxuan (Selected Articles of Zhou Enlai on Foreign Relations)*, p. 85.

¹⁴ *People's Daily*, January 12, 1950.

¹⁵ About the causes leading to Chinese involvement in the Korean War, see Allen Whiting, *China crosses Yalu: the Decision to Enter the Korean War* (Stanford: Stanford University Press, 1960), pp. 2-13; see also Hao Yufan and Zhai Zhihai, 'China's Decision to Enter the Korean War: History Revisited', in *China Quarterly*, No. 121, 1990, pp. 99-108. About Chinese involvement in Indochina, see Chen Jian, 'China and the First Indo-China War, 1950-54', in *China Quarterly*, No. 133, 1993, pp. 85-92; and Lu Ning, *The Dynamics of Foreign Policy Decision-making in China*, 1997, pp. 79 - 83.

the decision of Chinese involvement in the conflict between the French colonialists and the Vietnamese Communists in Indochina: French refusal to recognise the new Chinese government and long-term confrontation.¹⁶ However, in fulfilling the duty of supporting the Vietnamese Communists with large amounts of material aid, training of troops and campaign planning by military and political advisory groups, the Chinese adopted ‘active engagement but not direct involvement’ in the Indochina conflicts. Undoubtedly, the lack of sufficient domestic resources to open two fronts simultaneously and the concern that such a direct Chinese involvement in Indochina might also invite American immediate direct involvement in this region were the principal factors leading to Chinese carefulness. But it also implied that Beijing had no intention of unduly enraging Paris and sought to make, through concrete policy measures, an implicit distinction between the United States and its Western European allies.

1.3 Chinese efforts to repair its relations with Western European countries in the mid-1950s

1.3.1 International and domestic contexts after the Korean War

A clear definition of the role of Western European countries in China’s external relations and the design of a new policy strategy was made after the Korean War to suit the new external environments and domestic demands. The Sino-Soviet special relationship had been consolidated and China’s decisive role in Korea had enhanced its prestige in the Communist bloc, but this also led to a long-term and all-sided Western containment. The death of Stalin in 1953 meant a decrease in Beijing’s dependence on Moscow, for the Communist camp had lost a predominant dictator. The fragile new group leading the Soviet Union after Stalin’s death sought to reduce the tensions between the two blocs and gave some autonomy to the fraternal Communist parties in order to minimise adverse foreign impacts on Soviet domestic politics. A continual Chinese confrontation towards the West would no longer be in Moscow’s interests in this context. Its insistence on Beijing’s participation in the Geneva Conference of 1954 indicated that it was willing to help Beijing find chances to pursue an improvement of the relations with the Western governments through high-level direct contacts in appropriate international forums.

¹⁶ Hoang Van Hoan, *Changhai yishu* (A Drop in the Bucket), pp. 255-256.

Beijing concluded that some new developments in the relations between the United States and its allies after the Korean War had appeared, namely the Western European countries were no longer willing to closely follow Washington;¹⁷ and China was desirous of applying the new principles to its relations with them, as Zhou Enlai clearly stated that peaceful coexistence and economic exchange became China's main policies towards Western Europe.¹⁸

Domestically, the first five-year plan had been set out since 1952. China now needed to concentrate its resources on economic development. Peaceful approaches instead of military confrontation became more appropriate in pursuing a favourable external environment. In this domestic context, the primary objective of both the special Sino-Soviet relationship and the beginning of the new diplomacy towards non-communist countries was to facilitate domestic economic reconstruction, namely to create a peaceful external environment for attaining this goal by improving relations with the non-communist countries, the neighbouring countries in particular, and to obtain technological and economic aid from the Soviet Union.

Mainly in order to facilitate domestic economic construction and the beginning of a more active diplomacy with the non-socialist countries, the Chinese central administrative institutions underwent restructuring in 1954. The State Council was formally organised, replacing the former Central Government, and came to function as the highest central administrative organisation both in domestic and foreign affairs. Zhou Enlai was the premier of the State Council and the foreign minister. Three so-called 'non-governmental' organisations were established under the direct leadership of the State Council, to conduct the trade and the 'people-to-people diplomacy' (*renmin waijiao*) with the countries without diplomatic relations.¹⁹ Thus, under Zhou's leadership, a new institution for the formulation and implementation of policies towards capitalist countries was formed. Supporting by this new institution, Zhou also obtained more autonomy in conducting Chinese diplomacy.

As dependence on the Soviets in foreign affairs decreased, Beijing acquired more self-confidence, indicated by the formulation of five principles for peaceful coexistence as universally applicable principles guiding the conduct of Chinese external relations (mutual respect for each other's territorial integrity, non-aggression, non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence). The formulation of the Five Principles could be regarded as a partial adjustment of the former bloc-oriented foreign

¹⁷ Zhou Enlai, *Zhou Enlai Waijiao Wenxuan*, pp. 58-62.

¹⁸ Zhou Enlai, 'tuijin zhongying guanxi, zhengqu heping hezuo (Promoting Sino-British Relations and Pursuing Peaceful Co-operation)', *Zhou Enlai Waijiao Wenxuan (Selected Articles of Zhou Enlai on Foreign Relations)*, p. 81.

¹⁹ These three organisations are the Chinese Association for Promoting International Trade (*Zhongguo Guoji Maoyi Cujin Hui*), the Chinese Association of Foreign Friendship (*Zhongguo Duiwai Youhao Xiehui*), and Chinese Diplomatic Academy (*Zhongguo Waijiao Xuehui*).

policy principles. To decrease the Western sanctions against China and create a favourable external environment by improving relationships with the non-socialist countries in general and the neighbouring countries in Asia in particular became the main goals in Chinese external relations.

1.3.2 Chinese diplomacy in the Geneva conference of 1954

The Geneva Conference of 1954 provided the sole chance to begin direct contacts between the Chinese highest government delegates and those of the Western Countries in the 1950s. China's principal objective was to stop the continuation and extension of the conflict in Indochina, and thus to exclude the possibility of American direct involvement and avoid continual confrontation with the West in this region. To realise regional neutralisation through international supervision was an option. The approach to attain this goal was 'to fully utilise the contradictions between the United States and its allies through active Chinese diplomacy'.²⁰ The Chinese delegation, led by Zhou Enlai, taking the chance of participating in this conference, made the first effort to improve China's relations with the Western European countries. Beijing also sent a trade delegation to Geneva both to seek for the possibility of enlarging trade with these countries and to back up the diplomatic effort. Seizing the opportunity of direct contact with the British delegation, a diplomatic relationship between China and Britain at the level of charge d'affaires was established. However, Beijing failed to make any breakthrough in its relations with France, even though the Chinese delegation made an important contribution to the successful arrangements in Indochina by persuading the Vietnamese Communist delegation to make compromises on some key controversial issues. After this conference, the Chinese leadership concluded that over a certain period there would be no significant changes in the relations between the United States and its European allies.²¹ This conclusion seemingly implied a revision of the former optimistic expectation of making some breakthrough in the relations with the Western European countries. The contacts between China and the Western European countries thereafter were maintained mainly through the so-called 'non-governmental channels', namely the 'people-to-people diplomacy' and trade.

²⁰ Han Nianlong, *Memoir of Han Nianlong (Han Nianlong Huiyilu)*, p. 64.

²¹ Zhou Enlai, *Zhou Enlai Waijiao Wenxuan*, p. 81.

1.4 China's attitude towards and analysis of European integration in the 1950s

During a rather long period in the 1950s, the Chinese leadership seemed to pay little attention to European integration, formally marked by the establishment of the European Coal and Steel Community in 1951. It had to focus its attention on the domestic work in consolidating the Communist regime and economic reconstruction. Concerning its foreign relations, the Eastern bloc and the neighbouring countries were the principal targets. For the Chinese, Europe was too distant and European integration was a matter for the Europeans.

In addition, two additional factors restricted the Chinese leadership in appreciating this new development. First, Lenin's opposition to European integration constituted the theoretical impediment for Chinese understanding of this development.²² However, Beijing's analysis of this development in the 1960s indicated that it applied Lenin's analytical model of uneven development between capitalist countries, but did not completely accept Lenin's definition of the anti-socialist nature of European integration. It completely abandoned Lenin's orthodox conclusion in the 1970s.

Second, Chinese preoccupation with absolute state sovereignty and independence constituted another impediment to understanding regional integration. Mao defined Chinese society in the first half of the 20th century as 'semi-feudal and semi-colonial'. One principal task of the Communist revolution was to change this state of affairs. For Mao and many of his colleagues, to defend the hard-won state sovereignty and independence meant minimising Chinese dependence on the external world. It would be best if the modernisation could be realised by way of self-help. Regional integration, viewed from this perspective, would inevitably lead to a restriction on state sovereignty and would paralyse the efforts to establish an independent national economy for China. With this preoccupation, the Chinese leadership even gave economic integration in the socialist camp the cold shoulder. In 1954, it refused the Soviet plan to involve China in the economic co-ordination in the socialist camp through Soviet economic aid.²³

Beijing noted in 1957 the foundation of the Common Market. The *People's Daily* reprinted the full text of the statement of the Soviet Foreign Ministry but gave no further commentary.

²² Lenin argued that a United States of Europe, under capitalism, was either impossible or reactionary from the standpoint of the economic conditions of imperialism; but that *temporary* agreements were possible between capitalists and between states. In this sense, a United States of Europe was possible as an agreement between European capitalists. He concluded that the purpose of 'the United States of Europe' was to jointly suppress socialism in Europe and jointly protect colonial booty against Japan and America. V. Lenin, 'On Slogan of the United States of Europe, (Über die Lösung der Vereinigten Staaten von Europa)'. The German text can be found in *Lenins Werke*, Berlin, 1960, vol. 21, pp. 342-346.

²³ Shi Zhe, *Shi Zhe Huiyilu (Memoir of Shi Zhe)*, p. 580.

It appeared to indicate that Beijing accepted Moscow's position towards this development, which held that the establishment of the Common Market was reactionary and anti-socialist in particular. This development indicated the deepening split in Europe as well as the intensifying contradictions among the member states of this organisation. In addition Moscow advocated a 'co-operation on the basis of Europe in its entirety'.²⁴

Beijing's position was partly modified one year later. It highlighted that European integration was an indication of intensifying contradictions within the Western bloc, which had led to an imbalance of force and to regroupings. This development was a consequence of the confrontation between the two blocs. But such a modification did not mean the formation of Beijing's own position towards European integration, for Moscow also regarded the Common Market as an indication of intensifying contradiction within the Western bloc.

Nevertheless, the situation in China in 1958 seemingly provided a new explanation for Beijing's unanticipated interests in this development in Europe. Having purged large numbers of intellectuals in 1957 with the primary goal of eliminating any contrary opinions from them, and having begun the 'Great Leap Forward' – a Chinese experiment involving mobilisation of the population but not relying on experts and technological progress to pursue rapid industrialisation, Mao needed a domestic consensus to support his experiment of this kind in order to facilitate mobilising the masses. To attain this goal, he had to ensure the cadres and masses believe that this experiment was conducted in a favourable external environment, in which the Western bloc was declining, mainly because of conflicts between its states. Thus an analysis to affirm this judgement by demonstrating the increasing internal conflicts and the tendency of this bloc to split was inevitable. From this perspective, the Chinese analysis of European integration perhaps only served as a part of propaganda campaign in this period, but not a revelation of its real understanding of the Western bloc.

Defined as 'an international cartel organised by monopoly capitals of six West European countries in order to monopolise the West European market, to reduce internal competition and to strengthen capabilities to compete with the countries outside the Common Market', the Common Market was the consequence of capitalist development in the second period — a 'monopoly international economic organisation'. Based on an analysis of the relationships between the Common Market and its two principal trade partners (the EFTA and the USA), European integration was interpreted to be a French effort to form a Paris-Bonn axis in order

²⁴ The Chinese text of the Soviet statement can be found in *Xinhua Yuebao (New China Monthly)*, March 1957, p. 173.

to prevent Britain from interfering in European continental affairs.²⁵ This development indicated that “contradictions between imperialist countries were further intensifying, and that the ‘free world’ was becoming more scattered and divided”.²⁶ Taking into account the fact that all Common Market members were also members of NATO, Beijing repeated the Soviet argument that this economic organisation was to co-operate with that military coalition, and was therefore anti-socialist, but it stressed that the goal of the Common Market was ‘to resist American economic expansion in Europe’.²⁷

2 Policy making structure and process concerning policies towards Western European countries in the Mao period

2.1 A survey of the evolution of decision-making structure and process in the period from the mid-1950s to the mid-1970s

The remarkable feature of the hierarchical Chinese decision-making structure in the period of Mao Zedong (1949-76) was that it was highly personalised.²⁸ But more important, Mao’s status in the decision-making structure shifted from dominating to predominating, partly due to his successful purging of any of his challengers and partly due to his efforts to dismantle the regulated policy-making structure and process, which were institutionalised following the Soviet model in the early 1950s.

In the hierarchical decision-making structure, in terms of the Party constitution, the ultimate political authority rested in the standing committee of the Politburo, which was, before the Cultural Revolution, composed of seven members, but Mao and Zhou were the ultimate decision makers concerning Chinese foreign relations.²⁹ The importance of other organisations in policy making, such as the central committee and the Politburo as well as its standing committee, varied at times due principally to Mao’s effort to maintain his decisive role in all important decision making and to easily build a coalition supporting him on important issues through breaking the restrictions of the institutionalised decision-making

²⁵ ‘yichang huxiang yaoba jingzhengzhe yansi de douzheng (A Struggle between the Competitors to Drown the Other Reciprocally)’, *People’s Daily*, December 8, 1958.

²⁶ *Ibid.*

²⁷ Yang Guang, in the *People’s Daily*, December 7, 1958.

²⁸ Barnett, *The Making of Foreign Policy in China, Structure and Process*, 1985, p. 16.

²⁹ Among the other five members, three of them (Zhu De, Lin Biao and Chen Yun) did not play active roles concerning Chinese foreign policies. For instance, Zhu De was of old age, Lin Biao and Chen Yun were separately assigned the responsibilities of army and economic planning. Two of them (Liu Shaoqi and Deng Xiaoping) were responsible for the general and daily work of the party.

process.³⁰ The active performance of the Secretariat of the central committee, which dealt with the daily work of the Party and functioned as a linkage between the Party central committee and the state central administration (the Secretary General Deng Xiaoping was both a member of the standing committee of the Politburo and vice premier of the State Council), contributed to the institutionalisation of the decision-making process in the period from 1956 to the first half of the 1960s, but this important organisation was disbanded in the period from 1966 to the end of the 1970s.

In 1958 eight 'small leading groups' were organised within the Party central committee to communicate, make proposals and supervise the work of various systems (*Xitong*) such as foreign affairs, industry, agriculture, and so forth. Each system was supervised by a politburo member. Through this institutional arrangement Mao as well as other principal Party leaders could exercise close supervision over the operations of the central state administrative organisations. The arrangement also implied exerting some restrictions on Zhou's power. The Central Foreign Affairs Small Leading Group (CFASLG), led by the foreign minister Chen Yi, (1958-66), were consisted of some other leaders in the Party and government organisations handling Chinese foreign affairs, including the director of the party international liaison department, the vice foreign minister, the director of the overseas Chinese affairs committee, the minister of foreign trade and the head of the trade union. Its functions included reporting to the central committee about the current work in foreign affairs, making proposals for guiding principles and working plans.³¹ The foreign minister, both as the head of the foreign affairs office organised in the State Council and as the head of the CFASLG, was the principal co-ordinator between the central Party organisations and the foreign affairs organisations in the state administrative system. However, the CFASLG appeared unable to play an active and important role, indicated by the fact that one of its most significant proposals in the early 1960s was totally refused and angrily criticised by Mao.³²

The launching of the Cultural Revolution had a complicated impact on Chinese foreign policy making and implementation. Many of the leaders who might have had the chance to participate in the decision making or functioned as advisors were purged and the institutionalised decision-making process was broken. The consequence was that the

³⁰ One example was to restructure the decision-making structure and process by replacing the assembly of the central committee and the Politburo with the 'Central Committee Working Meetings' (*zhongyang gongzuo huiyi*), whose agenda of topics was determined by and whose participants were selected by Mao, including many of the leaders at the local level with less information on the ideas of Mao and other central leaders. These local leaders tended to support Mao.

³¹ *Jianguo Yilai Mao Zedong Wengao (The Manuscripts of Mao Zedong after the Foundation of the PRC)*, vol. 7, pp. 268-269, & vol. 8, p. 38.

³² Also see 3. 1. pp. 25-26

relationship between Mao and the administrative organisations transformed to a command-obey one, namely that there was neither bureaucratic frustration nor bureaucratic initiatives. Mao's personal instructions in every aspect could be immediately put into policy implementation.

The Cultural Revolution was itself Mao's undertaking to purge his perceived opponents not by legal proceedings according to the Party constitution but by motivating the masses. To attain this objective he paid no attention to the consequences of the radical activities of the mobs. In 1967 even Zhou had difficulties in dealing with troubles in China's foreign relations caused by the radical leftists. One obvious consequence of the developing radical leftist tendency was that the five principles for peaceful co-existence were replaced by 'revolutionary diplomacy' and revolution exporting. However, compared with the policy domains concerning domestic affairs, the adverse impact on China's external relations caused by the radical leftist tendency was not so lasting and strong. None of the radical leftist factions (the Lin Biao group and the 'Gang of Four') sought to engage deeply in China's foreign affairs, both out of concern about challenging Mao's authority and due to a lack of expertise. In addition, as the head of the central administrative system, Zhou's personal role in minimising the adverse impact of the Cultural Revolution on Chinese external relations was never marginal.

2.2 Power sharing and function assignment between Mao and Zhou in the decision-making structure

Mao's two principal roles in the Chinese Communist Party, both as absolutely highest party leader and as unquestionable theoretical authority, were associated with and supported each other. As the theoretical authority he formulated his theories to legitimise his strategies, to justify policies in various external and domestic situational contexts; and perhaps more important, the authoritative theories, helping explain the adjustments of the foreign policy principles and policies in varied external environments, facilitated obtaining support and achieving a consensus between the central and the local levels.

In the ultimate decision units such as the standing committee of the Politburo, the Politburo or the central committee working meetings (zhongyang gongzuo huiyi), the power-sharing and function assignment between Mao and Zhou were the prerequisite condition to maintain a lasting coalition between them. As highest Party leader in the decision-making structure Mao ultimately defined situations, designed strategies, and imposed his ideas, even those not

widely shared, on his colleagues. Their habitual obedience to Mao both in terms of Party discipline and the concern for their own fate, was an important factor ensuring Mao's predominance in important decision making. Zhou was the principal leader concerning detailed policy formulation and implementation. For most of the time after the foundation of the PRC Zhou managed to maintain his autonomy in dealing with the relations with non-Communist states, the so-called relations on the basis of the five principles for peaceful co-existence, but his autonomy was restricted in some specific situations and in some issue areas.³³

Sometimes Mao also gave personal instructions on important policy formulation and was involved in the implementation of policies of the greatest importance in China's foreign relations, such as the relations with the Soviet Union in the 1950s, France in the mid-1960s and the United States in the early 1970s, in order to facilitate adjustment of positions, to demonstrate China's stressing of this new development (such as the Sino-French relationship in the 1960s) or to legitimise China's initiatives (such as the rapprochement between China and the United States in the early 1970s)

Mao's predominance in decision making did not mean that he could make decisions on most important issues without consultation with his colleagues and achieving consensus, in particular relating to the definition of situations and strategy planning. In addition to the decision on Chinese involvement in the Korean War, two cases in the 1950s and the 1960s illustrated that there were some discussions concerning decisions of highest importance within a small group. Mao determined both the agenda of topics and the list of the participants. However, the rareness of such meetings indicated by the published documents appeared to demonstrate the high concentration of decision-making power on Mao and Zhou, namely that such a meeting was convened only in a compelling situation. One discussion took place in 1959, when the institutionalised decision-making process was still in place, concerning the potential impact on China's external environment due to the détente between Moscow and Washington.³⁴ It likely functioned both as the ultimate strategy-designing unit and as a forum for exchanging views, providing advice, building a consensus and ensuring co-ordination among the leaders of various systems. Another case demonstrated that Mao needed advisory

³³ For example, in a short period in the Cultural Revolution he was unable to lead the operations of the foreign ministry, and according to the assignment of work concerning the relations with other Communist countries as well as concerning the support for the national independence and Communist movements, more Party, government and army organisations were involved in policy formulation and implementation through concrete measures.

³⁴ *Jianguo Yilai Mao Zedong Wengao (The Manuscript of Mao Zedong after the Foundation of the PRC)*, vol. 8, p. 564 and p. 597. The attendees included Mao, the principal leaders of the party, the government, as well as organisations of foreign affairs, army and propaganda.

support from the political elite for his idea concerning the definition of situations and appropriate strategies. In the specific situation of the Cultural Revolution and after the border clashes between Chinese and Soviet troops in 1969, an advisory group composed of four marshals was convened in order to make a careful assessment of the external environment and put forth proposals to cope with it.³⁵

As the head of the central administration, Zhou's solid and extensive foundation in the Chinese political elite and his almost irreplaceable key role in detailed policy formulation and implementation were likely the most important factors facilitating the maintenance of the long-term coalition between him and Mao. In addition, Zhou's mediating tactics in achieving consensus among individuals with different views within the central leadership also strengthened his status.

As head of the hierarchical central administrative system and the secondary system of foreign affairs, Zhou had always been one of the principal leaders in the central decision-making circle. He was not only involved in all important decision-making concerning China's external relations, but also had a significant role in interpreting the principles and guidelines and making proposals. After defining the situations and setting the goal and bottom line in policy implementation, Zhou had relatively full autonomy in diplomatic operations to attain the goals.³⁶ The pragmatic conducting of China's foreign policies revealed his sustained effort to minimise the adverse impacts from domestic leftist radicalism on China's foreign relations. He was much better informed than other Chinese leaders in international affairs and seemed to have more personal influence on conducting China's policy operations towards capitalist countries. Most of the key Chinese diplomats in these countries and the functional leaders of the ministry of foreign affairs had been his important assistants and close colleagues.³⁷ He managed the three most important information collecting and processing organisations—Chinese embassies overseas, functional departments of the foreign ministry and the New China News Agency. Therefore he was able to exert a more direct personal role on information gathering and supplying, and thereby to influence the definition of the situations. In addition, he organised an advisory group within the system of the State Council composed of experts in international politics, international law and international economy. With the help

³⁵ Xiong Xianghui, 'dakai zhongmei guanxide qianzou (The Prelude for Opening Sino-American Relations)' in *Lishi de Zhujiao (Footnotes for History)*, pp. 173-174

³⁶ For instance, in the early 1960s he was fully empowered to conduct the negotiations with the French mission on the establishment of diplomatic relation between China and France. He personally managed the entire negotiations. See Li Qingquan 'xuexi Zhou zongli de tanpan yishu he waijiao fengge' in Waijiaobu (ed.) *Xin Zhongguo Waijiao Fengyun*, pp. 158-167.

³⁷ For example, the Chinese charges d'affaires in London in the 1950s and 1960s Huan Xiang and Xiong Xianghui, both of whom were experts in international affairs and his principal assistants.

of this group, he was able to make more appropriate proposals in policy formulation and implementation. His expertise facilitated increasing his autonomy in policy implementation. Nevertheless, in the Cultural Revolution, together with the advisory group, this information collection and processing system was disbanded. Despite the fact that most Chinese embassies abroad started their daily work in the early 1970s, the staff members had to concentrate their attention on domestic political changes but not developments abroad. In addition, the advisory organisations in the State Council system could not function as usual because many of its experts had to leave Beijing to receive re-education in the so-called 'May-Seventh Cadre School' (Wuqi Ganxiao). Consequently, the New China News Agency became the sole principal institution for information supplying. This may have led to the consequence that the principal leaders had not got enough and well-processed information when they had to make important decisions.

One case seemingly demonstrated how little room was left for Zhou in defining the situation in the period of the Cultural Revolution. A new assessment in one article written by the foreign ministry in 1973 argued that the two superpowers were in 'collusion' in dominating the world and their collusion was even greater after they had concluded the SALT I and the ABM treaty in 1972. This view was criticised by Mao for its 'revisionist inclination'. Zhou had no option but to shoulder the responsibility for this 'faulty assessment' and the foreign minister lost his position.³⁸ Mao's anger probably stemmed from concern that the new assessment would lead to the revision of his West-oriented international strategy of building a united front to cope with Moscow, which was based on the assumption of a continual confrontation between the two superpowers, for one must pose the question whether this strategy was valid and appropriate if the relationship between the two superpowers transited from confrontation to collusion.

This case demonstrated the extent and the consequence of extreme concentration of decision-making power in Mao's hands, namely that with regard to history-making decisions and setting of guide-lines and policy strategic goals, none of other leaders had the courage to put forward different or contrary opinions. Concerning China's policies towards Western Europe in the 1970s, it contributed to answering the question as to why Mao's interpretation of European integration, no matter how distant from the reality of this development, could be transformed into a consistent Chinese policy behaviour towards the EC, an absolute support for European integration, linking this development to the imagined Western European role in containing Soviet hegemonism and further to other important international issues in the 1970s

³⁸ Mao Zedong, *JianguoYilai Mao Zedong Wengao (Manuscripts of Mao Zedong after the Foundation of the PRC)*, Vol. 7, pp. 356-357, footnote. Also see Lu Ning, pp. 136-137.

without questioning whether the EC had such a competence or not and observing the difficulties in and current situation of European integration.³⁹ This perplexing phenomenon might reveal an attempt to legitimise the absolute support for European integration determined by Mao both by maintaining the validity of Mao's definition of European integration and by attributing various positive EC significations for some new international developments in this period. It was a specific phenomenon in the Cultural Revolution and did not mean that such a support for the EC served Chinese 'overall interests and objectives'.⁴⁰

3 Chinese policies towards Western European countries in the 1960s and the 1970s

3.1 The Chinese perception of Western Europe in the late 1950s and in the 1960s

Mao was convinced that the Western bloc was full of uncompromising contradictions and that a splitting within the Western bloc was only a matter of time.⁴¹ Such a conviction relied on his model for analysing the international developments, 'great turbulence, sharp division, and extensive regroupings' (da dongdang, da fenhua, da gaizu). His international strategy, which aimed at finding as many allies as possible and making alliances even with the secondary enemies in order to facilitate opposing the principal foe, was based on this conviction. He did not change this analytical model till the 1970s.

Lenin's idea of viewing the Western bloc as a temporary alliance with intensifying internal contradictions caused by the shifts of relative power status between its members provided an orthodox theoretical support for Mao's pragmatic philosophy for dealing with the countries in the Western bloc. But as Holmes points out, Mao tended to treat the ideas of Marx, Engels, Lenin and Stalin as methods and political theories, but his own ideas were essentially pragmatic and related specifically to the Chinese situation.⁴² The core concept stemmed from the traditional Chinese practice of 'playing one barbarian off against another' (yi yi zhi yi) and 'making friends with distant enemies in order to facilitate attacking the neighbouring foe' (yuan jiao jin gong).

³⁹ Concerning Chinese perception of the significations of European integration in the 1970s, see 3.4 pp. 34-37, and 3.6. pp. 39-41.

⁴⁰ Kapur concluded that 'For the Chinese, who had erroneously supposed that this evolution was taking place in the early 1960s though it was unmistakable in the 1970s, the new autonomous centre – if encouraged – might serve overall Chinese interests and objectives'. Cf. Kapur (1986), p. 24. He attributed this perplexing phenomenon to that the Chinese leadership had a rather 'simplistic vision of the West'. Cf. *Ibid.*, p. 30.

⁴¹ Mao Zedong, *Jianguo Yilai Mao Zedong Wengao (Manuscripts of Mao Zedong after the Foundation of the PRC)*, Vol. 7, p. 581, and p. 599.

⁴² Leslie Holmes, *Politics in the Communist World*, p. 16.

Mao stressed that revolutionary practice was ‘to make use of contradictions, win over the many, oppose the few, and crush our enemies one by one.’⁴³ In order to fully exploit the contradictions, one must find the ‘particularity of contradiction’, distinguish the principal contradiction from secondary, and take into account ‘contradictions within the enemy camp’ for the purpose of making necessary policy adjustments. Distinguishing the principal contradiction from the secondary was of particular importance in working out correct strategies and policies.

One report written by the Chinese charge d’affaires in London in 1958 was highly appreciated by Mao. For this reason, this report could be regarded as revealing of Mao’s ideas on Western Europe in this period. According to this report, Western Europe was full of various contradictions, which were demonstrated in the relations between European countries and by the conflicts between American-British association and some continental countries through forging association.⁴⁴ Based on his conviction that the ultimate split of the Western bloc was only a problem of time, Mao stressed that profiting by utilising these contradictions between the Western-bloc countries was ‘an important matter concerning the principle of our external policies’.⁴⁵

3.2 China’s foreign policy practices in the case of France in the 1960s

In the early 1960s the rupture between China and the Soviet Union was made public. The Soviet withdrawal of its economic and technological assistance in this period greatly obstructed China’s ambitious planning for rapid industrialisation and made the special Sino-Soviet relationship purposeless. Economic hardships in the early 1960s, mainly due to the failure of the Great Leap Forward, intensified the conflicts within the Party leadership over Mao’s leading ability in economic construction.

⁴³ Mao Zedong, ‘lun zhengce (On Policy)’, *Mao Zedong Xuanji (Selected Works of Mao Zedong)*, Vol. 2, p. 289.

⁴⁴ Its core theme was that the Western bloc was no longer a monolithic one. It highlighted the intensifying contradictions within the Western bloc in political and economic aspects through comprehensive analysis of the relations between Britain and its principal allies, namely the United States, France and West Germany. It argued that under the form of ‘interdependence’ the contradictions between Britain and the United States were developing, each seeking to pursue its own interests by sacrificing those of the other. This tendency would continue and their contradictions would become aggravating and more complex in the coming year. The contradictions between Britain and the continental European countries were also developing both in political and economic aspects. One of the reasons leading to the intensification of contradictions between Britain and other Western countries was the breaking of the balance of force between Western European countries owing to the resurgence of West Germany. The failure in negotiations on the creation of the free trade zone in Western Europe was an indication of the change of the balance of force between Britain and the continental European countries and the decline of British dominance in this region. The balance of force now was favourable for France and Germany. See *Jianguo yilai Mao Zedong wengao (Manuscripts of Mao Zedong after the Foundation of the PRC)*, Vol. 7, pp. 582-583, footnote.

⁴⁵ Mao Zedong, *Mao Zedong Xuanji (Selected Works of Mao Zedong)*, vol. 5, p. 342.

Mao's predominant status came to meet challenge within the Party in this context. As the ultimate decision maker, he had to bear responsibility for the failure of his domestic policies. Facing aggravated China's international isolation, increasing domestic challenges and in particular the economic crisis, Mao took a sophisticated attitude towards China's external relations. On the one hand, he had to insist on his ideological radicalism in order to maintain his status within the Party, and refused the proposal by some members of the CFASLG, which suggested that in order to facilitate solving domestic economic hardships, China should seek to improve its external environment by reducing confrontation both with the Soviet Union and with the West through a decreased involvement in the national independence movements and Communist armed struggles in other countries. On the other hand, he could not ignore China's international isolation and the serious consequences from the Soviet withdrawal of its economic and technological aid. Any success in Chinese foreign relations in this context would not only alleviate China's international isolation and economic crisis but also facilitate regaining Mao's dominant status in the Party. His theory of two intermediate zones revealed the attempt to integrate his radicalism and pragmatism into one theoretical framework, in order to justify China's foreign policy operations in this period. The formulation of this theory (in the mid-1960s) after the beginning of the policy operation (in the period between the end of the 1950s and the early 1960s) was to provide a theoretical support for the international strategy in this period. Similarly, the formulation of the Third-World theory in the mid-1970s, three years later than the Western-oriented policy strategy had begun to be applied, aimed at attainment of the same goals. These two cases indicate Mao's pragmatism in dealing with strategies, theories and policies, namely that his international strategies dictated what policies were to be adopted and what theories he needed to formulate in order to legitimise the policies in attaining the goals set by the strategies.

By setting up two categories of Chinese external relations that differed in nature (the solidarity with 'Marxist-Leninists and revolutionary people' and 'diplomatic relationships on the five principles of peaceful coexistence'), he set China's strategy in this period: increasingly active involvement in the national independence and Communist movements in the 'first intermediate zone', and pragmatic pursuit of improvement of relations with the countries in the 'second intermediate zone' as well as a maximising of economic profits by strengthening trade with the Western countries.⁴⁶ Both radical and pragmatic policy practices

⁴⁶ He argued that the state-to-state relationship and the relations between the peoples were of different nature. The Chinese could only be in solidarity with 'Marxist-Leninists and revolutionary people'. The relationship with capitalist states was confined to the realm of diplomatic relationships on the five principles of peaceful coexistence, 'but it is a completely different matter from the solidarity with the people of other countries.' See *Mao Zedong zhuzuo xuandu (Selected Readings of the Works of Mao Zedong)*, vol. 2, p. 834.

in pursuing the international strategy could be legitimised and justified by the theory of the 'two intermediate zones'.

Zhou was the principal leader directly involved in China's active diplomacy towards the Western European countries in this period. China's objectives were pragmatic based on the assessments of the varied dependences of each country on the USA and their positions on the issue of Taiwan. Towards most of these countries it had only limited objectives.

France, which came to challenge American dominance under de Gaulle's leadership, became the principal target of China's Western European diplomacy. After Paris offered Algeria independence, the most difficult issue impeding the development of relations between Beijing and Paris was that of Taiwan, for both Beijing and Taipei sought to declare their international legality by excluding or limiting the other's international contacts.

The negotiations for establishing diplomatic relation with France were completely under Zhou's management after the bottom-line had been set. While fully demonstrating pragmatism, Beijing sought to maintain its principle on the issue of Taiwan through another approach. In fact, it accepted the French programme of establishing diplomatic relations without preconditions. Both governments separately issued a statement simply declaring the establishment of diplomatic relation between them without mentioning the issue of Taiwan. Paris avoided the perplexity of moral condemnation and of excessively enraging Washington by openly declaring the abandonment of Taiwan. The Chinese government published a unilateral statement, claiming that its decision to establish the diplomatic relationship with France was based on the mutual understanding that the government of the PRC, as the sole legal government representing the whole Chinese people, conducted the negotiations and concluded this agreement with the French government.⁴⁷

3.3 Chinese analysis of European integration in the 1960s

Mainly as a consequence of the debates with Moscow, Beijing needed to formulate its own positions on a series of important international issues, including European integration. Undoubtedly, the antithesis between Beijing and Moscow significantly radicalised Beijing's views on a series of important international issues in order to diametrically oppose Moscow's position, even though the radicalised views were not contradictory to Mao's analytical model of international developments in this period. In this sense, it was questionable whether such radical views genuinely reflected Beijing's assessment of the international developments, or

⁴⁷ Xie Li, 'zhongfa jianjiao tanpan leimu' in Hanzhang (ed.): *Zhongnanhai Waijiao Zhenwen lu*, pp. 119-126.

whether they only served the purpose of claiming that Beijing's position was opposite to that of Moscow.

The key issue in the bitter debate between Beijing and Moscow on some important international issues in the early 1960s was which strategy the Communist bloc should adopt in order to cope with the Western bloc – offensive confrontation or defensive peaceful coexistence. The principal divergence between Beijing and Moscow on the choice of strategy related to the following key problem: via which approach, at what and whose cost to pursue the peaceful coexistence. More concretely, whether such a pursuit of peaceful coexistence between the two superpowers would be at China's expense when Beijing had perceived its external environment had been deteriorating since the end of the 1950s, indicated by the border conflict with India and the insufficient support from the Communist camp for its confrontation with the rivals. Moscow's withdrawal of its aid was the direct factor leading to making the divergence public, but the foreign pressure in the early 1960s was helpful to regain solidarity of the Party in this difficult period after the failure of the Great Leap Forward. To find and analyse the internal contradictions within the Western bloc, in particular that between the Western European countries and the United States, not only related to the key issue of ascertaining whether the Western bloc was so powerful that the Communist bloc had to pursue détente with it, but also supported China's advocating of an offensive international strategy.

Chinese analysis argued that although the confrontation between socialism and imperialism constituted the 'fundamental' contradiction in general, the 'focus' of the contradictions in the current world had nevertheless shifted to the developing struggles of the Asian, African and Latin American peoples against US imperialism and to the conflicts between the United States and its allies within the Western bloc, which had been greatly weakened by these new developments. The 'focus contradictions' in the current world created the context in which the Communist camp should focus its resources to promote development of this positive trend and adopt an offensive international strategy.⁴⁸

In this context, European integration unexpectedly came to gain importance in Chinese analysis of the developments concerning the Western bloc. But to a large extent, Beijing's new interest in European integration was inspired by de Gaulle's ambitious international policies to challenge American dominance and the Fouchet Plan in particular, a design of a European confederation of states with common foreign and defence policies as well as co-operation on cultural, educational and scientific matters.

⁴⁸ 'On the Difference between Comrade Togliatti and Us', in *Xinhua Yuebao (New China Monthly)*, No. 1, 1963, p. 15

Concerning the significations of European integration, the divergence between Beijing and Moscow focused on whether the Western bloc was weakened or strengthened by this development. Regarding European integration as the consequence of the changing balance of forces within the Western bloc, Beijing intentionally opposed the views shared between the Soviets and Italian Communists on this development.

The position of the Italian Communist Party consisted of two components: on the one hand, European integration constituted a part of East-West confrontation, in the sense that European integration was combined with the armaments and war preparation of the NATO; on the other hand it promoted the enlargement of the market and economic development in Western Europe. Promoting international economic cooperation, and the economic cooperation in Europe in particular, therefore came to be one of the principal tasks of the Italian Communists.⁴⁹ Moscow followed the advice of the Italian Communists, and accepted that the Common Market promoted investment, modernisation, and external trade, as well as wage increases.⁵⁰ In short, European integration alleviated the contradictions both between states and between classes in Western Europe and improved its situation. Such a shift of Moscow's position towards European integration served, in Chinese interpretation, to support its 'revisionist' international line of seeking peaceful coexistence with the imperialist camp.

Beijing argued that European integration clearly demonstrated 'a new type of intensifying contradictions within the Western bloc — the competition between individual capitalist countries developing to the rivalry between associations of nations'. The capitalist world grouped into three competitive associations of nations (the Common Market, the EFTA and the Alliance for Progress) was described as a 'product of an acute contradiction among the imperialist countries.' These groupings were characterised with the Leninist phrase 'as agreements and alliances between robbers' where a 'genuine long term interest to bind them together is lacking'. Contradictions between imperialist countries were not reconciled.⁵¹ This new development revealed a significant change in the balance of forces within the imperialist camp — the position of the United States and Britain was weakened, but that of the Western European countries, the six states of the Common Market in particular, was relatively strengthened.⁵²

⁴⁹ 'More on the Difference between Comrade Togliatti and Us', in *Xinhua Yuebao (New China Monthly)*, No. 3, 1963, p. 20.

⁵⁰ About Moscow's position, see John Pinder, *the European Community and Eastern Europe*, p. 8.

⁵¹ Fan Chengxiang, 'Diguo zhuyi maodun xianjieduan de fazhan wenti' (On the Question of the Development of Imperialist Contradictions in the Present Period), *Red Flag*, No. 5, 1963, p. 5.

⁵² *Ibid*, p. 1.

Defined as ‘the association of nations developed on the basis of the state monopoly capital’, the Common Market had ‘increasing exclusiveness’, and was planning to organise the ‘European Political Union’. This association of nations, with a very well-organised supranational institution, had clear economic and political goals — to unite Europe ‘economically, politically and even in military and foreign affairs.’ ‘France and West Germany have formed an axis and on this basis are planning to organise a Western European ‘political Union’. This development was very unfavourable for other countries outside this group, the United States and Britain in particular.⁵³

The consequence of organising this exclusive economic association of nations was that ‘the US press has openly taken its Western European allies to task for their rebellion.’ The Common Market, ‘in various economic significations’, had constituted a force ‘great enough to contend with the United States and Britain’. ‘The Western European countries claimed complete equality with the United States on the formulation of the West’s global policy and in the settlement of the most important economic and political issues as well as problems of military strategy. Their efforts to get free from American political and military control and to gain a status conforming to their economic strength had ‘greatly shaken American leadership in the capitalist world’.⁵⁴

However, despite the efforts of the six member states of the Common Market to get free from American economic control, this goal could not be attained in a short time. For ‘in an expectable rather long period, the United States will continue to be the imperialist country with the most powerful economy among the Western countries’, and ‘it continues to have significant influence on the internal and foreign affairs of these countries’. In addition, there existed many economic interest conflicts between the six member states of the Common Market, which could be exploited by the United States. Currently, its focus was ‘to isolate and attack France in order to compel De Gaulle to yield’.⁵⁵

Beijing argued that such an association of imperialist nations had a reactionary and aggressive nature and an objective directed against the socialist countries, as a consequence of the irreconcilable socialist-imperialist confrontation, but it ‘was not specially organised to oppose socialist countries’. Moreover, in the current period, ‘the more immediate and real contradiction that the Common Market faces is that of competing with the United States and Britain in a daily shrinking capitalist world and of gaining a status equal to these two countries within the imperialist camp. The Common Market leaders are actually engaged in a

⁵³ *Ibid*, p. 4.

⁵⁴ Fan Chengxiang, ‘On the Question of the Development of Imperialist Contradictions in the Present Period’, *Red Flag*, No. 5, 1963, p. 2.

⁵⁵ *Ibid*, pp. 2-3.

struggle against US control and seek to squeeze out the political and economic dominance of the United States and Britain in Europe, although it is under the banners of fighting against communism and creating a 'Europe for the Europeans'.⁵⁶

What was the general signification of European integration for the whole capitalist world, positive or negative? In terms of Lenin's orthodox analysis of imperialism, Beijing asserted that the regrouping within the Western bloc represented a 'significant symptom of ever-deepening general crisis of capitalism'. The establishment of the Common Market did not indicate a strengthening of the tendency towards unity between capitalist countries. Quite the contrary, it was a demonstration of the 'falling apart of the imperialist camp'. This was not only demonstrated by the intensifying contradictions between the Common Market and the United States as well as Britain, but also by the relations between the member states of this organisation, which were of 'both mutual collusion and fundamental conflicts'. The escalation of internal contradictions would continue, and the falling apart would inevitably occur when the crises came.⁵⁷

Beijing acknowledged that integration 'temporarily and marginally' promoted economic growth. However, contrary to the Italian Communists' argument that European integration both promoted economic growth and improved the living standard of the working class, Beijing argued that the state-monopoly integration was only the 'life-saving injection for the capitalist system'. It could not overcome fundamental contradictions in capitalism, prevent economic crisis or alleviate class antagonism, pre-empt the competition for neo-colonial markets, and even eliminate the possibility of military conflicts.⁵⁸ One of the principal objectives of economic integration such as the Common Market was 'to re-divide the inner European Market and fight for the international market outside Europe, but not to solve the contradiction between the productive forces and the relations of production'. For this reason, it was not in conformity with the demands of current scientific and technological progress and was not the creature of the objective tendency of economic globalisation.⁵⁹ The consequence of economic integration would be the inevitable strengthening of the exploitation of the working class. It would create favourable conditions for uniting all forces in the extensive common struggle opposing monopoly capitals.⁶⁰

Beijing's position seemed to be contradictory. On the one hand it asserted that European integration had weakened the Western bloc and posed a challenge to American dominance in

⁵⁶ *Ibid*, pp. 7-8.

⁵⁷ *Ibid*, pp. 5-6.

⁵⁸ *Ibid*, pp. 11-12.

⁵⁹ *Ibid*, p.7.

⁶⁰ *Ibid*, pp. 13-14.

and control over the Western bloc; on the other hand, it had to acknowledge that the Western European countries had to follow the United States during a rather long period. It appeared to indicate a highlighting of Chinese evaluation of the positive significations of European integration by maintaining Lenin's orthodox analysis of imperialism. But it implied such an idea, that the Western bloc would be further weakened by the increasing internal contradictions. The pursuit of détente with the United States rather than adoption of an offensive strategy would be helpful to strengthen American control over its European allies and further isolate France. In Beijing's perception, Paris was pursuing a European role in world politics with the principal goal of challenging American dominance, and European integration around the Paris-Bonn axis was one part of this effort. More important, the analysis of European integration revealed the central constant concept of Beijing about Western Europe, that it was becoming an increasingly autonomous entity with the main objective of forming a new force in world politics. This was a positive development with potential long-term implications with regard to the relations between continental European countries and non-continental Western countries. Moreover, Beijing clearly concluded that the Soviets and the Italian Communists overestimated the positive significations of European integration for alleviation of the contradictions within Western Europe, such as conflicts between the Common-Market states and contradictions between two major antagonistic classes in these countries. Thus, even though both Beijing and Moscow gave a relatively positive evaluation of European integration, they obviously did so from different perspectives and with different objectives in mind. Beijing's analysis supported its claim of adopting an offensive international strategy by highlighting the importance of European integration in weakening the Western bloc.

3.4 Chinese conception of Western Europe in the 1970s

Beijing's new understanding of the international environment in the early 1970s concentrated on the consequences of the changed balance of power between the two superpowers: the expansion of Moscow's global influence supported by its rapidly developing military strength, the renewed American isolationism and the decrease in its overseas involvement by way of recognising the *status quo* in Europe and by encouraging its European allies to improve relations with the Soviet Union. Mao asserted that the post Second World War peace would

not be maintained much longer, and there was only one choice – revolution or war.⁶¹ It appeared to reveal Mao's judgement that the balance of power had been broken.

In light of Mao's views of the early 1970s, even though the relationship between China and the Soviet Union had deteriorated from ideological divergence to confrontation with border clashes, Moscow's international strategy still focused on Europe. The border conflict between the Chinese and the Soviet troops was only the practice of Soviet plotting of 'making a feint to the east and attacking in the west'. As a continent with a cluster of many separate, small and weak countries, it had neither the capacity nor the courage to withstand pressure from the superpowers. Consequently, they sought to transfer the focus of Soviet expansionist ambitions from Europe to other regions. The pursuit of détente in Europe obviously demonstrated these endeavours and was caused by the weakness of the European countries. Only a powerful Europe, by unifying these small, separate and weak countries, could reverse this trend.⁶² Mao seemed to conclude that the Sino-Soviet confrontation would endure for a rather long period. While criticising the Soviet-Western détente, supporting European integration, which was European unification in Chinese perception, was the sole approach to increasing European self-confidence and reversing the trend of 'pursuing appeasement' in Europe.

Mao's view offered the key explanation of China's expectation of and absolute support for European integration, more European than the Europeans. First, European integration was an effort to form a new force through unification of the individual and small European countries with the principal goal of contending with the superpowers. Second, the current principal objective was to ensure external security, namely to cope with Soviet expansionism. Third, it was a positive development and in any sense was worthy of gaining absolute Chinese support. However, after having gained more information and a deeper understanding of this development, Zhou, by the mid-1970s, seemed to have formulated his own ideas on relations between China and the EC, a relationship of South-North nature rather than for containing hegemonism.⁶³ As revealed in the next section, the Chinese press in this period sought to reflect these two views by linking European integration with European security and by highlighting the importance of strengthening the relations between the EC and the developing countries.⁶⁴

Mao's concern that détente in Europe between the two blocs might have an adverse impact on China's external security originated from deeply-rooted distrust of Western powers through

⁶¹ Mao Zedong, *JianguoYilai Mao Zedong Wengao (Manuscripts of Mao Zedong after the Foundation of the PRC)*, vol. 13, p. 32, footnote.

⁶² Wang Shu, 'con jizhe dao dashi (From Journalist to Ambassador),' in Wang Shu *et al*, pp. 22-24, 35-38.

⁶³ Also see 3. 6. pp. 39-41.

⁶⁴ Also see 3. 6. pp. 39-41.

historical analogy: the détente in the 1970s was the renewal of the appeasement of the 1930s.⁶⁵ One commentary in the *People's Daily* of 1977 asserted that the Western objective in détente with the Soviets was to 'divert the disaster water (the Soviet expansionism) to the East (China)'; and the West was carrying out a policy of 'suicide' by exporting capital and manufactured goods to the Soviets with the consequence that the Soviets could transfer more resources to the military.⁶⁶

In defining the Chinese external situation in the early 1970s and formulating the new Chinese international strategy, Mao seemingly accepted the opinion put forward by the group composed of four Chinese marshals in 1969. This opinion maintained that the situation in Europe was the key factor determining whether or when a war between two superpowers might begin and China could postpone the outbreak of the war through active diplomacy and by motivating various international factors, particularly by bringing about rapprochement with America.⁶⁷

In the special situation of the Cultural Revolution, this opinion had special importance. The new international strategy and the diplomatic operations according to this opinion in fact prevent the radical military group expanding its power into China's foreign relations, restricted the role of the army in China's politics, and facilitated the control of China's diplomacy under the moderate faction headed by Zhou in the first half of the 1970s. Perhaps it was more important for the Sino-European relations that this opinion linked Europe directly with China's external security.

According to the new international strategy formulated in the early 1970s, Beijing was going to establish a broad international united front, involving all Western states and developing countries, including the United States (Yixian jia liangbian, 'one line supplemented by two

⁶⁵ For instance, early in 1966, one commentary in the *People's Daily* had concluded that the Soviet-American détente would deteriorate China's external environment. (*People's Daily*, February 1, 1966). The German-Soviet Treaty of 1970 was criticized as 'a big fraud to shield under the label of peace the aggressive face of Soviet social imperialism and German militarism', and it constituted a part of the global Munich scheme between the Soviet revisionist and the US imperialist. The objective of this treaty was to cheat the European people. 'Commentary on the Soviet-West German Treaty', *People's Daily*, September 13, 1970.

⁶⁶ Ren Guping, 'Munihei xieding he dangdai de suiying sichao (The Treaty of Munich and the Appeasement in Contemporary Period)', *People's Daily*, December 26, 1977.

⁶⁷ This idea held that a war between the superpowers, even though inevitable, was not imminent and could be postponed, provided China could make full use of various international factors through active and flexible diplomacy. The most likely place for such a war was still Europe, for it was the focus of the superpowers' contention and confrontation. The main approach to achieving the goal of postponing a new world war was to unite the West. The key factor was the improvement of relations with the United States. Xiong Xianghui, 'dakai zhongmei guanxide qianzhou (Prelude for Opening Sino-American Relations)' in *Lishide Zhujiao (Footnotes for the History)*, pp. 173-174.

sides') to cope with Soviet hegemony.⁶⁸ The United States and the Second-World states would play the principal role, together with China, in containing the Soviet expansionism. Compared to the advanced Western countries, the Third-World countries were reduced to playing only a supplementary role in China's new international strategy. This design was an attempt to regain the perceived broken balance of power, by uniting the West to equalise the Soviets. A united and strong Western Europe, as an indispensable part of the planned united front to contain Soviet expansionism, was a decisive factor determining whether this strategy would be successful or not.

Mao's theory of the 'Three Worlds', formally formulated in the mid-1970s, could be regarded as justifying China's new West-oriented international strategy and policy practices in this period; or more convincingly, as providing a necessary explanation for this strategy and policy operation which had begun in the early 1970s. It singled out the Soviet Union as the principal enemy and regarded the United States, being less 'ferocious' and having a shared interest in constraining the Soviets, as the potential ally; and advocated co-operation between the Second- and the Third-World countries to pursue the common interests of opposing Soviet hegemonism.⁶⁹

3.5 Western Europe in China's policy operation in pursuing its international strategy in the 1970s

In putting the West-oriented international strategy into policy operation, two factors led to a European preference. Internationally, the United States, as hegemony, was still China's target of criticism. As the self-entitled speaker of the Third World, it was certainly a dilemma for China to openly stand together with one of the hegemonies, despite Beijing's calculation that the improvement of relations with the United States constituted the vital factor to constraining

⁶⁸ Xiao Chen, 'Deng Xiaoping waijiao sixiang yanjiu (A Study of the Thought of Deng Xiaoping on Foreign Relations)', in *Zhonggong dangshi yanjiu (The Studies of the History of the Chinese Communist Party)*, No. 3, 1996, p. 72.

⁶⁹ According to this theory, there existed 'three both combined and contradictory aspects – the 'three worlds'. The character of the First World – the United States and the Soviet Union, was 'hegemonism', and the potential origin of the new world war. However, the Soviet hegemony was more dangerous and more deceiving, for it was under the cover of 'socialism'. The Second World, which was constituted by all advanced countries in the two blocs except for the Soviet Union and the United States, had the common character that they were all under 'the oppression, control or bullying' of the First World, and that they all had the will to get free from this control and maintain their independence and sovereignty. All developing countries belonged to the Third World, regardless of their political, economic and social systems. They had the common objective of maintaining their independence, developing their national economy and changing the existing international economic order. In the hegemonism-dominated world, their common task was to oppose the superpowers and in particular, to oppose the 'Social Imperialism' (the Soviet Union).

Soviet expansionism. In addition, the disputes with the United States, such as that on the Taiwan issue, impeded the development of bilateral relations. Consequently, the two countries had not established an official diplomatic relationship by 1978.

However, there was no such dilemma in treating the Second-World countries as allies, particularly with the EC member states, some of which had traditional cultural, economic and political links with most of the Third-World countries. Chinese perception of the importance of European integration in ensuring China's external security and the consequently absolute support for this process further reinforced the European preference. Western Europe was the key component of the designed international united front, but also the weakest one needed to be reinforced. To strengthen the relations with the European countries was the most effective approach to reverse the tendency of 'appeasement in Europe' and promote the conceiving of 'unified Europe'.

Domestically, the factional conflicts within the Chinese leadership reached their highest point in this period, revealed by the debate extending over a range of policy dimensions both internal and external. The radical leftist faction asserted that the effort made by the moderate faction to increase technological imports from Western industrial countries was contrary to the principle of self-reliance. But such technological imports were regarded by the moderate faction as the key factor for attaining the goals of both accelerating economic growth and technological upgrading. China's traditional policy practice in external economic relations was that trade was subject to political objectives and served as a principal policy instrument. For the moderate faction, trade with Western Europe in this context constituted one part of the policy operation for the Western-oriented policy strategy. The highlighting of the importance of Western European countries was helpful to attain the objective of strengthening economic exchanges with them. In fact, in practising Mao's Western-oriented policy strategy, the moderate faction sought more to attain domestic goals than international goals.

The Western European preference in practising Mao's Western-oriented strategy in the 1970s could be demonstrated by the following statistics: China invited, in the period 1973-75, the foreign ministers of seven EC states and four EC heads of state to visit China;⁷⁰ The establishment of diplomatic relations with all EC member states except for Ireland by the mid-1970s facilitated the Western European preference. In this context, despite its limited physical capacities, China could make use of the high-level contacts to exert its influences on issues of its concern. In terms of published Chinese documents, Chinese emphasis

⁷⁰ Kapur (1985), p. 28.

concentrated on two themes: reminding the Europeans of the dangers of Soviet expansionism and expressing China's absolute support for European 'solidarity'⁷¹.

3.6 Chinese image of European integration in the 1970s

As mentioned above, renewed Chinese interest in European integration in the early 1970s originated from its urgent demand of ensuring external security: a 'strong Europe' through 'unification' to reinforce its capabilities in confronting Soviet expansionism might contribute to impeding 'the disaster water being led from west to the east', thus alleviating China's external security pressure from the Soviets after the border conflicts between China and the Soviet Union in 1969. Later it evolved to linking more extensive international issues, for example, support for the formation of a multipolar international system and promotion of North-South dialogue. This aspect gained a more significant importance after the status of the PRC had been enhanced to the permanent member of the UN Security Council. China's expectation of its international role was accordingly boosted, through co-operation with some international actors, such as the EC, to play a more important part in extensive international issues.

In a meeting with a Chinese correspondent of the New China News Agency (NCNA) in 1972, whose argument that the Soviet strategic focus was still in Europe was highly appreciated by Mao, Chinese Premier Zhou Enlai expressed his eagerness to obtain more information about the Paris summit. He criticised the ignorance of Chinese correspondents of the importance of this development and instructed them to focus their attention on informing the process of European integration, which he described as 'not popular but a very important development'. Zhou's words appeared to reveal that the Chinese leadership did not obtain enough new information on European integration when Mao made his judgement.

In this meeting Mao linked the process of European integration directly to Chinese external security, namely that Europe could overcome its weakness in confronting Soviet expansionism by unification of the small and separate European countries.⁷²

The Chinese Premier's 'Euro-passion' was a by-product of the 'solemn declaration' of the communiqué of the Paris summit of October 1972: 'the member states of the Community, the driving force of European construction, affirm their intention, before the end of the present

⁷¹ See the addresses by Chinese leaders in welcoming the European statesmen published in the *People's Daily*, for example, May 26, 1974; April 21, 1975; November 1, 1975; January 20, 1978.

⁷² See 3. 4. pp. 34-37.

decade, to transform the whole complex of their relations into a European Union'.⁷³ This goal was planned to be attained by the end of the 1970s.

Zhou's instruction took immediate effect. In January 1973 the Commission's press bureau was visited by a Chinese correspondent to obtain documentation on the Community,⁷⁴ and the Chinese press began to focus its attention on the developments on this continent. In the *People's Daily*, there were 63 entries about Western Europe in 1972, but in 1975 the number increased to 297.⁷⁵ Most of them dealt with two themes: European security and European integration. More concretely, the significance of the ambiguous 'European Union' was interpreted from the perspective of European security; and in most of the articles concerning European integration, 'Western Europe', 'the European Community', 'European integration' 'European solidarity' and 'European unification' were synonyms and were often used alternatively in the same text. It revealed that Mao's idea of Western Europe dominated China's interpretation of 'transform(ing) the whole complex of their relations (the relations between the EC member states) into a European Union', namely the building of an alliance of European countries, political, economic and military.

Chinese attention focused on the following themes: the goals of this development, the relationship between the European Community and the Third World, the relationship between Western Europe and America, solidarity among the EEC member states, their common goals and their co-ordination in foreign policies.

Now that Soviet expansionism, which constituted the principal threat to China's external security, had replaced the hegemonism of the United States and had become the principal foe, and the sole approach to confront it was the international united front which included the Americans, the relations between the European countries and the United States were of key importance. Beijing abandoned or at least revised its principal view of the 1960s, that European integration was both a demonstration of intensifying contradictions within the Western bloc and a Western European effort to confront Washington. Despite the highlighting of the importance of European integration in contending with hegemonism, in fact Beijing hoped that the integrating Western Europe and the United States could further co-operate to contain the most dangerous common foe – the Soviet Union. Britain had been viewed as an American 'Trojan Horse' in Europe, but its entry into the EEC was now acclaimed as 'an important development which would facilitate the struggle of the Western European people

⁷³ Commission, 1972, General Report, point 5 (16).

⁷⁴ Kapur, (1985), p. 29.

⁷⁵ Kapur, (1985), p. 50, Table 4:2.

against hegemonism.⁷⁶ A comprehensive report issued by the NCNA in 1974 highlighted the tendency in improvement of the relationships between the USA and Western Europe, which had deteriorated due to disputes on bilateral trade and their divergence on Middle East issues. The principal factor for this positive development in US-European relations, according to this report, was that both sides became aware of the importance of the solidarity between them in confronting Soviet expansionism; in particular Western European leaders had been aware that European integration needed active American engagements.⁷⁷

Chinese commentaries stressed that strengthening the relationship between the European Community and the Third World might be of potential significance in creating a new international economic order, but it was again linked to the issue of coping with the superpowers and the Soviet Union in particular. One commentary of the NCNA on the Lomé Convention of 1975 stated: 'in the context of increasing competition for hegemony between the Soviet Union and the USA, in order to contend with the two superpowers through converging actions, the tendency to increase contacts between the Second and the Third World is strengthening.' The rapidly developing co-operation between the two worlds was due to the 'solidarity and combat' of the Third-World countries. According to this commentary, the importance of this development was to frustrate the Soviet plotting of seeking world hegemony. Thus, the conclusion of the Lomé Convention was 'a heavy blow' to the superpowers and the Soviet Union in particular.⁷⁸

The Chinese had abandoned Lenin's theory of uneven developments between capitalist countries, which led to a relatively pessimistic assessment of the process of European integration in the 1960s. They became now more confident that the decisiveness of the EEC member states in promoting the integration and co-ordination among them could overcome the conflicts of interest between the member states and the Community. The compromise between Britain and the EEC on renegotiating the terms of British entrance into this organisation, Britain's decision to remain in the EEC through a successful referendum, and Tinndmans' proposal to strengthen co-operation and co-ordination among the EEC member states so as to further the integration, were applauded as a new phase of European integration. These developments revealed that the European countries were aware that furthering economic and political integration and strengthening co-operation were the more important

⁷⁶ Deng Xiaoping's speech in the banquet to welcome British ex-prime minister Edward Heath. *People's Daily*, 26. May, 1974.

⁷⁷ *People's Daily*, July 15, 1974.

⁷⁸ 'luomei xieding shuoming le shenme? (What does Lomé Convention demonstrate?)' *People's Daily*, March 4, 1975.

condition for maintaining independence in the context that ‘the two superpowers are contending for Europe, and particularly the Soviet Union is taking an offensive stance.’⁷⁹

The articles analysing Moscow’s objectives to form an all-European economic co-operation implied Beijing’s opposition not only to this proposal but also to the increase in economic exchanges between the EEC member states and the Soviet Union. Beijing argued that these contacts would impede European integration and decrease America’s role in Europe; and that they would increase Western European dependence on the Soviet Union and accordingly the Soviet economic influence in this region. More seriously, the technology transfer and financing from Western Europe would not only alleviate Moscow’s economic difficulties and upgrade its technologies, but also strengthen its capability to seek hegemony.⁸⁰

In summary, despite the fact that the reports and commentaries on European integration in the Chinese press were not written by Chinese leaders, they revealed details of the Chinese conception of European integration. By linking this development to each important issue of Chinese concern both in North-South and in East-West relations, and particularly to opposing the Soviet hegemony, the EEC became an ideal political ally. European integration had at last found a whole-hearted Communist supporter.

Such a continuing attribution of new positive significations to this development seemed to be necessary in the specific domestic context in the 1970s. Mao’s judgement of the importance of European integration brought about the important status of Western Europe in China’s external relations. Even though his judgement was far from the European reality, supporting European integration constituted one part of the Western-oriented strategy.

The EEC, in this context, gained an unusually important status in China’s external relations. In his visit to China in 1975 with the goal of exploring the establishment of an official Sino-EEC relationship in order to open the bilateral trade agreement negotiations, the Commissioner of foreign trade, Christopher Soames, was met by all important Chinese government leaders responsible for foreign affairs and had the chance to speak with the severely ill Chinese Premier Zhou in hospital on extensive international issues, mainly concerning the North-South issues.⁸¹ This seemingly indicated that with the decrease in China’s external security concerns and after the first oil crisis, Zhou came to focus his attention on international political economic issues. From this perspective he seemed to form some new understanding of China’s relations with the EEC. This seems to be supported by

⁷⁹ ‘xi’ou lianhe ziqiang de qushi zai fazhan (The Tendency of Uniting and Self-strengthening in West Europe is Developing)’, *People’s Daily*, April 4, 1976.

⁸⁰ Zheng Weimin, ‘suxiu guchui de quan’ou jingji hezuo’ shi shenme huose (What Bubbish is the All European Economic Cooperation Advocated by the Soviet Revisionist?)’, *People’s Daily*, March 15, 1975.

⁸¹ Bull. 5. 1975, p. 13.

the fact that before the beginning of the negotiation for a bilateral trade agreement, China strongly demanded to be differentiated from the Soviet Union and other Eastern European countries, namely that China should be treated as a developing country in the external relations of the EEC.⁸²

4 The implication of China in the EC's external relations: economic partner rather than political ally

The importance of China for Europe had always been ignored by most European countries, with the exception of France, taking account of China's geographic location and limited economic and military capacities. Unlike the Chinese, who were striving to find various positive and significant importance of the EEC in current international developments by linking the process of European integration and the EEC's activities in its external relations to Mao's judgement, the EEC had clear objectives both current and long-term within its competence when it initiated the process to develop relations with China.

The EC Commission obtained the mandate to negotiate trade agreements with state trading countries on behalf of the EEC member states after 1975. It indicated a new step in presenting a European role in the world, an important development both in the EEC institutional evolution and for its external relations. The EEC presented in 1974 a proposal to the state-trading countries to begin negotiations on a list of subjects including import quotas, agricultural imports, most-favoured-nation treatment, safeguard mechanisms, and problems of payment and trade finance. It insisted that the negotiations would be conducted with the individual Eastern European countries but not with the CMEA. This position conveyed the EEC's refusal both to recognise the CMEA as an equal partner and to legitimise Soviet control of Eastern European countries through this organisation. Such a rejection of the CMEA as an equal partner also indicated the determination of the Commission to avoid the reduction of its competence, for the CMEA lacked formal competence for trade policy.⁸³ The EC's proposal was refused by the member states of the CMEA. Moscow insisted that any such negotiations would be conducted between the two organisations.

To establish an official relationship with China undoubtedly was also of profound political importance in the EEC institutional evolution, namely a Commission mandate to negotiate trade agreements with third countries presented a common European line to non-Community countries. Facing the natural tendency among member states to turn inwards in a time of

⁸² Kapur (1985), p. 34.

⁸³ John Pinder, *the European Community and Eastern Europe*, p. 13.

recession owing to the oil crises of 1973-74, the Europeans turned back to intergovernmental mechanisms to overcome the difficulties, indicated by the creation of the European Council in 1974, to serve first and foremost as an arena in which international and global questions could be raised. Thus, the establishment of the official relationship with China was an achievement of the Community. Furthermore, the establishment of relations with China and successful negotiation of the bilateral trade agreement were particularly important for the Commission in its effort to maintain its competence in the EC's external relations and strengthen its status compared to that of the Council.

China's status in the EEC's external relations in the context of the refusal of the EC's initiative by the Eastern Bloc states and the desire to strengthen the EC's external role was accordingly enhanced. The success of the EEC in establishing official relations with China was acclaimed as 'probably the most far-reaching event to take place in the field of the Community's external relations',⁸⁴ and 'a development of prime importance in world politics,'⁸⁵ that would lead to a fuller understanding on the part of China of the Community's positive attitudes towards the developing world.⁸⁶

In contrast to China, the principal goal of the EEC in establishing official relations with China was primarily to expand the trade between the EEC and China, which was by then the EEC's main external competence. The EEC Commission had, in 1973, made the judgement that China would become one of the EEC's most important economic partners. In the report of the European Parliament Committee on External Economic Relations, China was described as 'the world's most populous country, whose human and natural resources are immeasurable and which will play an increasing role in the last quarter of the century.'⁸⁷ The Chinese market was estimated to have the capacity to absorb US\$ 25 to 35 billion worth of goods from other countries.⁸⁸ The economic crisis in the mid-1970s further compelled the European industries to seek new overseas markets and raw material suppliers. The potential of the Chinese market size was demonstrated by the contrast that a nation with a population of 800 million accounted for about 1% of EEC exports in the 1970s.

Apart from the above mentioned optimistic assessment of China's potential as a large market, the chance to win a favourable position in the competition with Japan and the United States for a larger piece of the Chinese market was another factor motivating the EEC to take the

⁸⁴ Debates of the European Parliament, sitting of Wednesday, 18 June 1975, in Kapur (1985), Appendixes, Document 3, p. 122.

⁸⁵ *Ibid.*, p. 130.

⁸⁶ *Ibid.*, p. 126.

⁸⁷ Kapur (1985), p. 32.

⁸⁸ *Ibid.*, p. 32.

initiative in establishing official relations with China. The bilateral trade between China and nine EEC member states increased from 348 million EUA in 1970 to 722 million EUA in 1974.⁸⁹ Ninety percent of the EEC's export to China was constituted by chemical products, transport equipment and finished products of light and heavy industries. The composition of the EEC's exports to China was significant to EEC industries and particularly important to German industries, which accounted for about half of the EEC's export to China. But the EEC's favourable status in China's foreign economic relations came to meet the increasing challenge from Japan and the United States.

Even though it could not parallel the EEC in technological export to China in the 1970s, Japan had some incomparable advantages in expanding its economic exchanges with China: its favourable geographic location and its willingness to import raw materials, fuels such as coal and oil in particular. These factors were very important in the 1970s, at that time when China still maintained the principle, though not in absolute terms, of maintaining trade balance, and was reluctant to receive any foreign credit. Primary products composed a large proportion of its exports, and its labour-intensive manufactures, such as textile products, were subject to strict quantitative restrictions. Thus, the increase in the export of raw materials and fuels was then thought to be the sole approach to rapidly generate foreign exchanges.

America constituted another challenge to the EC in the Chinese market. Trade between China and the United States accounted for US\$ 4.7 million in 1971, in 1973 it increased to US\$ 752.6 million and in 1974 it further increased to US\$ 921.2 million.⁹⁰ Though agricultural products constituted the main part of American export to China, the American administration's initiatives to relax the export controls and the increase in Chinese purchase of American machinery (including Boeing aircraft, M.W. Kellogg fertiliser plants, and oil production and exploration equipment) came to pose a challenge to the EC's dominant importance in this respect.

For both the governments of the countries in Western Europe and their peoples, it was a general conviction in the 1970s, through recognition of the status quo, to maintain stability and to bring about 'change through contact' and through institutional arrangements to 'positively affect' the relations between the two confronting blocs. Military security and a policy of détente were not contradictory but complementary, and institutionalised contacts with Eastern European countries should have been helpful towards achieving pluralist democracy and market economy throughout Europe. Thus, for the Europeans, if the Soviet factor played some role in motivating them to develop relations with China, it meant the

⁸⁹ Kapur (1985), p.42.

⁹⁰ Harry Harding (1992), *A Fragile Relationship: the United States and China since 1972*, p. 364.

contacts with China must contribute to the improvement of the relations between the two blocs. As Christopher Soames stressed in Beijing, the EEC was ready to increase its trading and economic links with the Eastern European countries and thus contribute to diminishing Europe's divisions.⁹¹

5 New foreign policy principle and new national interest preference

As early as 1978, the new Chinese leadership under Deng Xiaoping, as it set out the programme of economic institutional reforms and began to formulate the Open Policy to replace the domestic and foreign economic policies of the Mao era, came to consider abandoning the West-oriented international strategy.⁹² This appeared to indicate the new leadership was clearly aware that in the special domestic situation after the Cultural Revolution, which was characterised by prevailing poverty and ideological apathy, the attempt to legitimise the new leadership could only rely on the improvement of population's welfare as well as rapid economic growth, but not on ideological orthodoxy. To attain this goal China would have to adjust its foreign policies in order to facilitate transferring limited resources from military to civilian sectors. Thus domestic but not external constraints became the principal factors leading to the formulation of a new foreign policy principle.

However, the domestic political situation in the latter part of the 1970s, when some Maoists still occupied key positions in the central leadership, seemed to exclude the possibility of changing domestic and foreign policies simultaneously. For the moderate faction led by Deng, the appropriate choice was resolving the urgent socio-economic issues by immediately abandoning Mao's radical-leftist domestic policies but postponing the change of foreign policy strategy till this faction had consolidated its dominance in the central leadership. Such a choice aimed at both reducing the resistance from the Maoist leaders and facilitating winning extensive domestic support. In this domestic context, China's commentaries on European integration, even in the late 1970s, still maintained the general and fundamental validity of Mao's judgement and highlighted the implications of this development in opposing the Soviet hegemony.

The new Chinese leadership had a different perception of the international environment regarding the extent of the external threat. Two factors, namely the awareness of the overestimation of the foreign threat and the adverse consequences of the effort in pursuing an

⁹¹ Speech by Sir Christopher Soames in Beijing, 8 May 1975, in Kapur (1985), Appendixes, Document 1, pp. 115-116.

⁹² Yang Chengxu, 'duli zizhu heping waijiao zhengce de fengshuo chengguo (The Substantial Successes of Peaceful Independent Foreign Policies)', in *Xinhua Yuebao (New China Monthly)*, No. 11, 1999, p. 50.

alliance with Washington, supported formulation of the new foreign policy principle. It found the bottom line of the Soviet-Vietnamese alliance through the limited border war with the Vietnamese troops in early 1979. Beijing took initiatives in improving relations with Moscow, while posing three preconditions. The first consultation for improving the bilateral relations between China and the Soviet Union, on the level of vice foreign minister, began in October 1982. This meant that normalisation of Sino-Soviet relations was underway.⁹³ Despite Chinese insistence on three preconditions for the normalisation of bilateral relations, Beijing did not insist on solving these three issues at once but hoped that Moscow would make some response, particularly to press Vietnam to withdraw its troops from Cambodia.⁹⁴ These three preconditions should be regarded as a tactic to obtain dominance in the process of normalisation rather than to impede it. In addition, such a deliberately controlled and managed process of improving the Sino-Soviet relations with preconditions would not have an adverse impact on China's relations with the West.

Beijing increasingly felt the constraints from the West-oriented foreign strategy and its damage on China's profile in the Third-World countries because of the pursuit of an alliance with one of the superpowers. Beijing was suspicious of Washington's plan that China would pursue the principal goal of opposing the Soviets by courting the West at any cost, including some arrangements of 'two Chinas', or 'one China, one Taiwan'. China did not chime in with American President Reagan's new confrontation with the Soviet Union of the 1980s. In addition, his anti-Communist rhetoric was not pleasing to the ear of Chinese Communist leaders. China stressed more South-South co-operation and South-North dialogue in building a new international economic order.

Mao's assertion of the inevitability of the world war was replaced by Deng's judgement that 'peace and (economic) development were two principal themes in the current world'. In the mid-1980s Deng clearly argued that if a world war did not break out within this century, it would no longer break out.⁹⁵

The new foreign policy principle of 'making decisions independently and holding the initiative in China's own hands' (*duli zizhu de waijiao zhengce*) formally posed in 1982 implied replacing Mao's Western-oriented international strategy with Deng's avoiding of alliance and decreasing in external involvements. This was a more pragmatic approach to

⁹³ Qian Qichen, 'Jieshu guoqu, kaiji weilai (Close the Past, Open the Future)', in *Xinhua Yuebao (New China Monthly)*, No. 3. 1998. pp. 33-36.

⁹⁴ To reduce Soviet troops in the border region, particularly to withdraw Soviet troops from Mongolia, to withdraw Soviet troops from Afghanistan, and withdraw Vietnamese troops from Cambodia. *People's Daily*, April 17, 1985.

⁹⁵ *People's Daily*, April 18, 1985.

decrease China's external engagements, as a result of a re-estimation of the external environment, the concern about urgent domestic demands and the awareness of the consequences of inappropriate active external involvements in the period from the 1950s to the 1970s. In short, China could not continue the active external commitments as it had done in the past. According to Deng's words, similar active external involvements would be postponed until after China becomes more powerful, and China's current primary task is to focus on developing its physical capacities.⁹⁶ Accordingly, China's foreign policy objectives were set to promoting common economic prosperity by developing friendly co-operation with all countries regardless of social system and maintaining world peace. China's foreign policies became more closely linked to domestic demands.

One of the editorials of *Hong Qi* (the Red Flag) even explicitly proposed to separate external economic exchanges from external political relationships in order to maximise economic benefit.⁹⁷ Its argument implied that pursuing technological upgrading and profiting from foreign economic exchanges, rather than pursuit of foreign security, became the main goal of China's foreign relations. Foreign economic exchanges in this context effectively became 'the second pillar' in China's external relations, not necessarily being subject to political demands or serving political goals.

Accordingly, the signification of European integration and the EC also underwent changes in Chinese external relations as indicated by a commentary on the London summit of 1981. It stated in a cool tone that European integration was a 'protracted and slow process' because of conflicts of interest between the member states. The European Community was defined as an 'economic association with the tariff-union as the main part'.⁹⁸ Such a pessimistic tone, sharply in contrast to that of the 1970s, seemed to imply that the importance of the 'political European factor' in Chinese external relations, defined as the counterweight to the two superpowers, had greatly decreased, at least for the time being; and the Chinese at last understood that the EC was merely an economic power.

The status of the EC in China's external relations accordingly shifted to that of an economic counterweight to Japan and the United States. In Beijing's exploration of the new sphere of

⁹⁶ *Deng Xiaoping Wenxuan (Selected Works of Deng Xiaoping)*, vol. 2, pp. 111-112.

⁹⁷ It argued, 'many states are in bitter political confrontation between each other, but they manage to maintain economic exchanges, for they have the demands of economic interests,' and in the interactions between economic and political factors, the economic one is eventually decisive, and behind the political relations between nations there is a 'great economic interest'. For China, the foreign economic relations are of strategic importance, and to develop Chinese national industries and accelerate the economic development can be realized only with the help of foreign capital and advanced technologies. 'On the Problems of Our Foreign Economic Relations' (lun duiwai jingji guanxi wenti), *Red Flag*, No. 8, 1982. pp. 1-8.

⁹⁸ Xu Qingmei, 'ouzhou gongtongti lundun shounao huiyi, (The London Summit of the EEC)', *People's Daily*, December 1, 1981.

'economic diplomacy', Western Europe's status was enhanced. China sought to increase its trade with the EC. By giving a third of the China pie to each of its principal trade partners (Western Europe, Japan and the United States), it sought to decrease its dependence on any particular source of trade, and to counteract Taiwan's economic diplomacy in Europe and further political co-operation with Western Europe.⁹⁹ Chinese premier Zhao Zhiyang definitively placed the Sino-EC relationship within the framework of North-South co-operation.¹⁰⁰ It is worth noting that in his meeting with the president of the Commission, Gaston Thorn, Deng did not mention the foreign policies of a unified Europe, but stressed the importance of independent foreign policies by individual European states for maintaining world peace.¹⁰¹ It appears that by the early 1980s the Chinese leadership had abandoned the 'wishful thinking' of European integration.

6 Conclusion

In the period from the 1950s to the 1970s, the goal of decreasing the adverse impact of changes in its relations with the two superpowers, with special reference to the Sino-Soviet relations, had always been central to China's foreign strategy. Its general policy strategy towards Western Europe was subject to this imperative. The status of Western Europe in China's external relations shifted from that of secondary enemy in the 1950s to political ally in the 1970s. Accordingly, Chinese views on European integration shifted from. It regarded this development as a demonstration of the internal contradictions within the Western bloc in the 1960s, but imaged the EEC to become a political ally in the 1970s. This shift indicated that changes in Sino-Soviet relations in this period were the key external factor in interpreting China's different analysis of the same development in Europe.

There existed a close linkage between the evolution of Chinese perceptions of European integration and the shift of China's international strategies. That the importance of the EEC in China's international strategies shifted from meeting the demand of reducing international isolation to coping with Soviet expansionism revealed that in different situations European integration had different significations in China's external relations. But the core of the Chinese conception of European integration was that it was creating an autonomous

⁹⁹ George Yang, 'Mechanisms of Foreign Policy-Making and Implementation in the Ministry of Foreign Affairs', in Carol Lee Hamrin and Suisheng Zhao (eds.), p. 98.

¹⁰⁰ Speech of Zhao Ziyang to the Royal Institute on International Relations in Brussels, in Kapur (1986), Appendixes, Document 31, pp. 333-338.

¹⁰¹ *People's Daily*, December 6, 1983.

independent political and economic entity. Chinese international strategy provided an analytic framework for its interpretation of European integration in the 1970s.

However, the high politicisation of the policy operated in China's relations with the EC in the 1970s was, to a large extent, the result of domestic developments in this period, namely Chinese misperception of European integration was transformed into actual policy practice in this context. The EEC was regarded as an emerging autonomous entity and therefore European integration, in particular following the formulation of the concept of the 'European Union' in the early 1970s. The EEC, perceived as the unified entity of Western Europe, gained strategic importance in China's strategy for coping with the deteriorating external environment in the 1970s. In short, European integration provided the ideal solution to China's dilemma in dealing with this difficult task, a form of wishful thinking aiming at alleviating external pressures with the help of a unified strong Western Europe.

Chinese misperception of European integration demonstrated in two aspects, an overestimation of the pace of this process coupled with an underestimation of the inherent difficulties. Consequently, this led to an unrealistic expectation towards the EEC as the representative entity of the 'unified Europe', without taking account of its main external competence. In this context, the EEC gained significant importance in Chinese external strategies with the principal objective of coping with the Soviet expansionism and ensuring external security.

Despite the fact that China's policy goals seemed to be determined by the relations between China and the two superpowers, domestic factors were crucial in the transformation from policy goals to actual policy practice. The concentration of the decision-making power in Mao's hands in the specific Chinese domestic context of the 1970s was the key factor leading to the transformation of Mao's misunderstanding into policy operation without meeting any domestic dissonance. Policy operation could only be vested in Mao's judgement in the specific domestic context of the time. In turn, the Chinese perception of European integration, a misperception of the reality, contributed to supporting the policies operated towards the EC. Such a change in China's domestic politics was the principal factor leading to a perplexing phenomenon, namely that the exchange with the EC was focused on the domains of low politics, i.e. trade between China and the EC, while the importance of the relations with the EC was linked to the high politics, i.e. the issues concerning China's external security.

However, the pursuit of high-political goals and economic benefits were two mutually complementary objectives, even though in some specific situations the pursuit of high-political goals was at the cost of economic benefits. In conducting its policies towards

Western European countries, the pursuit of economic benefits by China became the primary actual goal.

From the above analysis it can be concluded that the highly politicised operation of the relations with the EC was a special case in Chinese external relations in the specific settings of the time, both external and domestic. For this reason, it is questionable whether this case can be used to support the argument that ‘in the final analysis political factors not only outweigh economic considerations, but actually tend to influence them’, and (...) ‘her (China’s) foreign policy is nevertheless basically determined by political objectives’.¹⁰²

Mao’s misperception of European integration provided the primary dynamics for the establishment of the bilateral official relationship between China and the EC. Deng’s pragmatism was more in conformity with shared interests and the basic nature of the bilateral relations. Such pragmatism facilitated policy adjustments and operations. As the importance of the ‘European factor in China’s external security’ came to disappear in the 1980s, the ‘European factor in China’s domestic economic developments’ replaced it and provided new dynamics for developing the bilateral relations.

¹⁰² Cf. Kapur (1985), p. XIV.

III. Evolution of Chinese External Economic Policies: from Mercantilism towards Liberalisation

1 The launching of economic reforms and Open Policy: domestic and external settings

As analysed in the former chapter, legitimising the new post-Mao leadership under Deng was the primary goal in launching the economic reform in the end of 1978.¹⁰³ The reforms began in two dimensions directly linked to urgent domestic demands: the agricultural sector and China's external economic administration. The reform of the system of landholdings aimed at motivating the farmers' initiatives in order to provide more agricultural products thereby to meet the popular expectation of a rapid raising of the living standard. The demand to rapidly generate foreign exchanges in order to reduce the trade deficit, which accumulated to about 4.3 billion dollars in the period from 1978 to 1980,¹⁰⁴ mainly due to the launching of the ambitious industrialisation programme,¹⁰⁵ facilitated commencement of the reform in the central-monopoly foreign trade system. In order to restore the foreign trade balance, China had to cancel and postpone the import of some complete plants mostly from Japan and Western Europe in 1978 and 1979.

The failure of that ambitious industrialisation programme demonstrated that China's centrally monopolised foreign trade system as well as the export mainly composing of low value-added primary products was not competent to provide enough foreign earnings for technological imports.¹⁰⁶ The increase in the export of agricultural and other light-industrial products would inevitably be contradictory to attaining the goal of obtaining popular political support for the new leadership through enhancing the living standard, leave aside the quantitative restrictions imposed by the trade partners on some major Chinese exported items. The pressure of rapid foreign exchange generation and the gradualist introduction of market mechanism facilitated the reform of the Chinese centralised foreign trade institutions, mainly through administrative decentralisation.

¹⁰³ See also chapter II, 5. pp. 46-49.

¹⁰⁴ Calculated by the author according to *Zhongguo Duiwai Jingji Maoyi Nianjian (Yearbook of Chinese external economy and trade)*, 1986.

¹⁰⁵ According to this ambitious economic development plan, the targets of 60 million tons of steel output and about 400 million tons of grain should be attained by 1985. It proposed an ambitious list of constructions, including 120 big industrial and infrastructural establishments, among which were ten ferrous metallurgical and nine nonferrous metallurgical plants, eight coal-mining bases, ten new crude oil and natural gas extracting establishments, thirty large power plants, six new railway lines, and five modern seaports. *People's Daily*, 7 March 1978.

¹⁰⁶ About the composition of Chinese exports to the EC in this period, see Kapur (1986), p. 65, Table 3.4.

There existed some differences among the Chinese leaders in the issues concerning the extent to which market mechanisms should be made use of and the pace at which the Open Policy should be pursued, indicated by the formulation of various guiding ideas to define the primary goal of the market-oriented economic reforms in the period from the 1970s to the 1990s, such as ‘the centrally planned economy complemented by market mechanisms’ (jihua jingji weizhu, shichang tiaojie weifu), ‘socialist commodity economy’ (shehui zhuyi shangpin jingji), and ‘socialist market economy’ (shehui zhuyi shichang jingji). The shift of these guiding ideas from ‘planned economy’ to ‘market economy’ only means the increasing extent of making use of market mechanisms. The central leaders were in consensus on the point, as Deng clearly highlighted, the reform ‘will not be permitted to be run counter to our socialist system.’¹⁰⁷ Undoubtedly, his words can have different interpretations in different domestic settings, but its core is to maintain political stability by maintaining the dominant leadership of the CCP. The ideological constraints gradually decreased, indicated by the continuation of the Open Policy. Undoubtedly, the benefits from the extending external economic exchanges and the increasing transnational linkages were effective factors promoting the market-oriented economic reforms and the Open Policy.

Deng’s phrase ‘feeling the stones while crossing the river’ (muozhe shitou guohe) in the new domestic context implies that the target of the economic reform and the Open Policy is fixed: pursuing economic growth through market-oriented economic reforms; but the process of reform must be gradualist and any measures cautious. In short, Chinese involvement in globalisation must be controlled in order to facilitate attaining the principal domestic goals — pursuing economic growth but maintaining political and societal stability. Such a gradualist strategy through partial integration in the world economy seeks to maximise benefits.

The new Chinese leadership under Deng was also conscious of the gap between China and the advanced countries. The rapid economic growth mainly depended on new technologies.¹⁰⁸ A long-term and sustained development could only be achieved by participating in the global division of labour and from the influx of capital, technology and managerial know-how, as the recent experiences of the New Industrial Countries (NICs) in Asia had demonstrated. The industrial structure adjustment in the advanced industrial countries after two oil crises meant capital and technology transfer abroad and a search for new market and raw materials suppliers. This new international development provided China with the precious chance of

¹⁰⁷ Deng Xiaoping, ‘shixing kaifang zhengce, xuexi shijie xianjin kexue jishu (Adopting Open Policy and Learning Advanced Science and Technologies of Other Countries)’ in *Deng Xiaoping Wenxuan (Selected Works of Deng Xiaoping)*, vol. 2, p. 133.

¹⁰⁸ See also chapter II, 3. 5. pp. 37-39.

accelerating its economic growth and upgrading its technology with the same (or similar) mercantilist approaches as those adopted by the NICs.

The mercantilist model for development adopted by the NICs means an active and even dominant state role in promoting industrialisation. The state gives high priority to promoting exports first through labour-intensive and later through technology-intensive products, canalises imports to facilitate industrialisation, attracts selected foreign investments to promote marketing and technology upgrading, and on this basis builds up some key industries composed of large enterprises with international competence. Amsden's analysis of the industrialisation of South Korea stresses the state's part through intervening and disciplining (performance-based incentive) in order to stimulate economic activity and realise economies of scale.¹⁰⁹

At the launch of its mercantilist export-promotion policies, China had advantageous conditions, both internal and external, compared to most other developing countries. Its agricultural output can meet the demand of the population growth and foreign earnings mainly contribute to technological but not corn imports. Its comprehensive industrial system, in spite of the bias to defence-related and heavy industrial sectors, facilitates improving the export composition by increasing some manufactured exports, in particular capital- and technology-intensive items, and replacing imports by domestic products. Its sustained economic growth, combined with the potentiality of China's market size as well as political and social stability, provided optimistic (or over-optimistic) prospects for foreign investors. As the forerunner in transforming the centrally-planned to a market economic system, it won extensive support from the West and relatively better trade terms; and it could obtain generous financing from the World Bank and IMF throughout the greater part of the 1980s. In addition, a large part of the foreign investments in China by the end of the 1980s came from the overseas Chinese, mainly for export processing.¹¹⁰ The overseas investments accelerated foreign earning generation decreased Chinese dependence on the loans from international financial institutions and foreign governments as well as commercial banks, promoted Chinese learning of marketing, quality control and managerial know-how, and effectively alleviated the pressure of unemployment in the transition period. Hong Kong played the key role in providing marketing information and as the principal source of overseas investment.

However, the most important factor is the maintenance of the active role of a 'strong state'. The leadership has enough autonomy and capacity in pursuing its development policy strategy – the export-promotion strategy and the Open Policy, and is able to extract resources from

¹⁰⁹ Alice Amsden, *Asia's Next Giant, South Korea and Late Industrialisation*, pp. 14-17.

¹¹⁰ By the end of the 1990s, such investments still accounted to 70 percent of total foreign investments in China.

society and distribute them selectively in accordance with the programme. Undoubtedly, during the two-decade process of economic reforms the role of the strong state has been gradually eroded, but this process has by no means fundamentally changed the domestic context in which the party-government entity functions as the dominant policy-making and policy-implementation unit. The lack of differentiation between state and society facilitates policy implementation.

Two factors are decisive for the evolution of China's external economic institutions: fulfilling the requirements of the WTO in the negotiation process for accession to this organisation and responding to increasing domestic socio-economic issues in these two decades. The former sets the target but the latter determines the speed. In the process of accession to the WTO, some measures have been adopted to fulfil WTO requirements, and the process has increasingly indicated its influences in adjusting Chinese external economic policies. However, rather than WTO requirements, The changing domestic socio-economic factors in China provide a more convincing explanation for the institutional evolution, indicated by the policy emphasis shifting from pursuit of export promotion to the attainment of more extensive domestic goals, such as alleviating unemployment, narrowing regional disparities, restructuring state-owned enterprises, etc. For the Chinese leadership the problem is in what time and to what extent China can fulfil what requirements of the WTO, namely how far to fulfil the WTO requirements was determined by the needs to minimise the adverse impact in the process of accession in different specific domestic settings.

2 The building of a governing coalition and policy networks, a general survey

2.1 The general tendency of external economic policy making

The decision-making structure and process of external economic policies have been undergoing significant changes in the transition from a centrally-planned economy towards the 'socialist market economy'. The key issue is while changing the incompetent central-monopoly foreign economic institutions, how to build a new governing coalition supporting the development goals in the market-oriented economic transition and new policy networks in sectoral policies, in order to continue the role of the 'strong state' in policy formulation and implementation.

Under the label of 'formulating policies on a scientific basis' (kexue jichu shang de juece), professionalism is promoted in decision making to meet the demand of dealing with more

complicated external economic issues. In building the policy networks concerning foreign economic exchanges, the importance of the party organisations in detailed sectoral policy making is decreased, and various administrative organisations are granted relatively clear assignment of responsibilities and power in policy formulation. All this poses demand for establishing a better educated, younger and more technocratic leadership in each administrative level and more extensive incorporation of experts into the policy networks. It is also a transition of the principal decision-making role in most economic policy dimensions from the revolutionary peasants to the better-informed city bureaucrats and, further, to well-educated experts. The prevailing pragmatism indicated by Deng's often quoted phrase, 'It does not matter whether the cat is white or black, as long as it catches mice,' namely that any approaches can be adopted if they can facilitate attaining the goals, accelerated this transition. Experts of young generations play increasingly important parts both in detailed policy making and in re-shaping Chinese external economic institutions in the market-oriented economic reforms and the Open Policy. Less restricted by ideological orthodoxy, they normally are supporters of the Open Policy and advocators of integrating Chinese economy in the global market. International organisations, such as the system of the World Bank, also provide personnel training.¹¹¹

The building of a new governing coalition is in fact the effort to obtain support for the new policies from the central to the local level and strengthen co-ordination and co-operations between them in the market-oriented economic reform. Because the decentralisation of foreign trade administration, the market-oriented reforms and the Open Policy are carried out simultaneously, some government departments, regions, sectors, enterprises and individuals become losers, while others become winners; and the interest preferences of each level are influenced by and changed in this process. For the practices of the former command economy have gradually been changed, namely a redistribution of economic and political power between them, there is a need for redefinition of the relationship between central and local governments, and between central administrative organisations and enterprises. This redistribution influenced policy contents and preferences.

While at the beginning the market-oriented economic reforms and the Open Policy focused on reducing the adverse institutional influences from the former centrally-planned economic institutions, the external economic policies gradually become combined with regional and sectoral interests as well as redistributive policies. The adjustments of the orientations of

¹¹¹ Margaret M. Pearson, 'China's Integration into the International Trade and Investment Regime', in Economy and Oksenberg (eds.), *China Joins the World Process and Prospects*, pp. 161-205.

regional and sectoral policies and continual adjustments of redistributive policies in the changing domestic settings aim at obtaining extensive local support for the new policies.

In the centrally-planned period, most of the interests and demands of various sectors were represented by the organisations within the central administrative system, such as various central commissions and central sectoral ministries managing industries, commerce, foreign trade, finance, telecoms and banking. In the new domestic context of removing the former commanding economic institutions, all of them face the necessity of regrouping and reorganisation in order to facilitate communicating their interest demands through appropriate channels and via governmental organisations in order to influence policy formulation. The variety of the influence of their interest demands on the formulation of China's external economic policies relates to their degree of organisation and their links to the central governmental organisations. Their interest demands are various, depending on whether the Open Policy has made or will make positive or negative impacts on their interests. In addition, the decentralisation of economic administration, the export-promotion policies and the formation of a foreign-investment regime increasingly influence the interests of various governmental organisations, sectors, local governments, and enterprises. New actors influencing external economic policy formulation and implementation are brought about in this process. The competence of local governments concerning foreign economic exchanges has been increased.

The state-monopoly sectors, such as telecoms, financial services, and some defence-related industries normally demand strong state protection. Generally, these sectors have still kept their good organisation formed in the period of centrally-planned economy and managed to maintain their direct links to the central government. Some organisations representing the interests of these sectors, such as the ministry of telecommunications and the banking system, are still components of the central governmental system. For these sectors, the best means to ensure their interests is to minimise competition from foreign investors through the maintenance of the state monopoly. Naturally such a demand is always legitimised by the argument of ensuring state economic security through state monopoly or protection of the so-called 'infant industries'. Concerning the industrial sectors, the situation is complex. Some manufacturing sectors – if the enterprises have built international competitiveness, rely on import of materials and component parts to keep production operations, or pursue technological progress through technological imports – demand the removing or reducing of tariff/non-tariff barriers and more liberalisation of the investment regime. These enterprises generally have close transnational linkages. Some large enterprises do not oppose furthering

the Open Policy or reducing tariff/non-tariff barriers but demand the ensuring of state support and more preferential policies in order to strengthen their international competitiveness. These enterprises normally belong to the 'pillar industries', play crucial role in reducing unemployment and maintain close ties to the State Economic and Trade Commission as well as local administrative organisations. In the past two decades, many small enterprises have been disorganised by the market mechanism and state policies. The surviving enterprises of this kind usually maintain their operation relying on their behaviours in the domestic or international markets but not preferential policies. So far the external economic policies have not been the key factors influencing their survival. As for the agricultural sector, its interests so far have not been substantially influenced by the Open Policy. Without any organisation to represent their interest demands, the farmers' interests can only be considered by the central government from the concern of maintaining societal stability and reducing regional disparities. The perceived adverse impacts on this sector due to the reduction of quantitative restrictions on the imports of some main agricultural products after China's accession to the WTO perhaps compel the central leadership to pay more attention to Chinese farmers. In the negotiations for China's accession to the WTO with its principal economic partners, one of the most disputable issues was to what extent to open the markets of the agricultural products, telecoms and financial services for foreign imports and investments.

Thus the appropriate approach to enlarge the coalition supporting the Open Policy is to encourage local governments and more enterprises to benefit from direct participation in the external economic exchanges on the one hand, on the other the state seeks to provide support for some important enterprises through preferential policies. The removing of some sectoral ministries and adjustments of foreign trade and investment policies generally have positive influences on the interests of local governments and enterprises. The evolution of China's external economic policies seemed to indicate the linear relationship between the enlargement of the governing coalition and the continual liberalisation of foreign trade and the investment regime.

Concerning policy formulation and implementation in the administrative system, the effort contains two aspects. At the central administrative level the efforts focused on reducing the frustrations to the market-oriented reforms and strengthening the co-operation and co-ordination in policy formulation and implementation. The approaches in this respect included the removal of most of the former central administrative organisations representing the interests of domestic industrial sectors, the incorporation of their interests into the newly-organised central government organisation, and the broadening of the competence of the

remaining organisations. The former fragmented central management by different industrial ministries has now been transformed into one central government organisation, the State Economic and Trade Commission (SETC). Many sector ministries have been disorganised and various central administrative organisations managing domestic economy have been incorporated into this organisation. Such a transformation undoubtedly reinforces the 'guiding role' of the central government in the governing coalition. At the local level, the central leadership sought both to strengthen the control on the provincial party leaders and to extend the administrative competence of local governments in dealing with local foreign economic exchanges. A positive phenomenon is that both coastal provinces concentrated with foreign investments and inland-regions concentrated with state-owned enterprises demand furthering the Open Policy in order to alleviate unemployment, to obtain capital, technology transfer, etc. Decentralisation of administration, as a measure to motivate incentives and win support for the new policies through reallocation of decision-making power and interests (including fiscal allocation) leads to an increase in the autonomy of the localities. The provincial governments are rapidly gaining more responsibilities for civilian expenditure by the government, investment and project approval. They also have the ability to blend official central policy to a wide variety of different applications through local laws and regulations.¹¹² One consequence of the decentralisation is that the local governments have sought to promote local interests through various local laws and regulations both for protecting local markets and enterprises and for competing with each other to attract foreign investments. Consequently, the central administrative power has been eroded and foreign investors are perplexed by various local preferential policies in attracting foreign investments, but they are also difficult in meeting various local interest demands. In such a domestic situation, it is questionable whether the central administration has enough capacities to maintain unified national external economic policies, in particular relating to policy implementation. In this context, external pressures become a key factor in reformulating unified external economic policies. Making use of the pressure to comply with the WTO rules, the central government organisations came to seek to unify Chinese laws, regulations and rules, both at the central and at the local level.¹¹³ In the meantime, the government is also strengthening the contacts with large foreign-investment enterprises to facilitate their operations. For instance, Siemens, owing to its early entry into

¹¹² For instance, according to statistics, the provincial people's congresses have made out more than eight thousand local laws and regulations concerning local external economic relations. NCNA, March 4, 2001.

¹¹³ For instance, the central government has withdrawn some of the preferential policies in trade and foreign investment granted to the coastal provincial governments, and came to implement national unified domestic tax and foreign trade duty policies in the late 1990s.

China with extensive investments in various industrial sectors and provinces, is setting up a co-ordination committee with the central governmental departments.¹¹⁴

Different policies (such as history-making decisions, guidelines and principles, important policies, sector policies, etc.) are made in different decision-making structures and processes, in which different actors are involved and different organisations play different roles. Important decisions are still made by the ultimate decision-making unit, namely the Politburo and its standing committee as well as the standing assembly of the State Council. Some of the most important laws concerning external economic relations and the agreements concluded with foreign governments must be approved by the National People's Congress as well as its standing committee. In history-making decisions a strong individual role is institutionalised.¹¹⁵ Deng's personal role in several important decisions reveals one of the enduring problems of the Chinese political structure: the incapacity to institutionalise policy-making and the consequent need to invoke the name of the 'supreme leader' to legitimise policy choice.¹¹⁶

In the post-Deng period, two features can be seen in important decision making. First, the strong individual role in the important decision making was still retained, indicated by the fact that the Premier of the State Council personally participated in the negotiations with the American delegations on Chinese accession to the WTO in order to break the deadlock.¹¹⁷ Naturally, such an individual role can become possible only after the bottom line has been determined by the Politburo or approved by the head of the Party. Second, in the post-Deng period, the current Premier of the State Council must meet the increasingly hypercritical examination of his annual government report by the National People's Congress at its annual assembly. This examination process directly relates to his prestige and strengthening or weakening the Premier's status within the central leadership. Consequently, the central administrative organisations are compelled to initiate communications with other principal institutions beforehand, such as the Standing Committee of the National People's Congress, in order to formulate more appropriate policies and plans.

¹¹⁴ Wang Zhile, 'shijie zhuming kuaguo gongsi zai zhongguo touzi de diaoyan baogao (A Research Reportage about the Investments from World-famous Transnational Companies in China)', in *Zhong Wai Guanli Daobao*, 1997, 3-4.

¹¹⁵ This was indicated by the fact that all important decisions required Deng's endorsement before his formal retirement. His speech in his 'Southern Tour' of 1992 launched a campaign for 'further and bolder reform'. It led to formulating the concept of 'socialist market economy,' which gives blanket ideological authorisation for any form of economic management that appears to work, and the decision of 'exchanging domestic market access for acquisition of foreign technologies'.

¹¹⁶ Tony Saich in Robert Benewick *et al* (eds.), *China in the 1990s*, p. 50.

¹¹⁷ Long Yongtu xitan zhongguo jiaru WTO jingguo (A detailed account by Long Yongtu of the process of China's accession to the WTO) <http://www.zaobao.com/special/wto>

Most foreign economic policy formulation and implementation are made in networks more transparent, fragmented but more technical. Professional knowledge, a good advisory network and in-time feeding back of policy implementation outcomes are necessary conditions for accountable policy formulation and adjustments. Professional knowledge and educational achievement are preconditions for selecting and enhancing the young officials who are involved in foreign relations, in addition to the knowledge of foreign languages and international affairs. Some of them have been educated at foreign high schools. In the current leading group of the Ministry of Foreign Trade and Economic Co-operation (MOFTEC), the minister and all vice ministers are promoted from low level to minister level within the foreign trade system and have received an education in foreign trade or foreign affairs at university level.¹¹⁸ Such an arrangement strengthens their role in policy formulation and implementation relying on their expertise and familiarity with the operation of this ministry. Early in the 1980s, some experts on foreign affairs from throughout Beijing's foreign affairs community began being invited to attend the meeting on China's foreign relations depending on the meeting's agenda.¹¹⁹ However, it is questionable to assume that the experts generally have an important influence on policy formulation. The parts that research institutes and experts play in policy making are different according to a variety of issues, institutional or non-institutional links between them and the decision-making units, and their capacity in information collection, processing and supplying.¹²⁰ Normally, relying on their professional knowledge, they play a much more important role in the policy domains of 'low politics' than those of 'high politics'. The research institutes affiliated to government organisations, such as the Development Research Centre of the State Council, the Ministry of Foreign Trade and Economic Co-operation (MOFTEC), the State Development Planning Commission (SDPC, the former state planning commission) and the State Economy and Trade Commission (SETC), play an important role in sector policy formulation. In addition, the experts in these institutes have easily access to first-hand information, and they have the obligation to make proposals in policy formulation. Some research institutes have been enlarged in order to conduct studies on more extensive themes in various issue areas.¹²¹

¹¹⁸ For instance, China's principal deputy in foreign trade negotiations and current vice minister of the MOFTEC, Long Yongtu studied at the London School of Politics and Economics and had had extensive working experience in international organisations before becoming the principal deputy in the negotiation of China's participation in the GATT/WTO.

¹¹⁹ Barnett, pp. 44-45.

¹²⁰ On the functions of various Chinese institutes concerning world politics, see Lu Ning, pp. 130-135.

¹²¹ For instance, the foreign trade ministry had a small research institute since the 1950s, and on this basis the International Trade and Economic Cooperation Research Institute was organised in 1997 and belongs to the MOFTEC. It has currently about 600 researchers and staff members. Its main tasks now are to provide information about China's principal trade partners, including trade circumstances and policies, to make

The process of formulating long-term specific planning programmes for the development of thirteen principal industries, such as automobiles, chemicals, mechanical engineering, etc., reveals the new approach of maintaining the active role of a strong state by transforming its role from 'central commanding' to 'central macro-guidance'.¹²² Such programmes contain the analysis of the situation of each industry, the setting of the development objectives, the announcement of central government's intentions, and the guiding of allocation of resources. That all principal organisations within the State Council system (such as the organisations concerning domestic industries, foreign trade, finance, planning, taxing, technologies and quality controlling) participated, under the leadership of the SETC, in the formulation of these programmes indicates the intention to strengthen the co-ordination and co-operation at the central government level to ensure the attaining of the goals set in these programmes. Normally each of these organisations also prepares its own detailed plans to implement these programmes, and local government organisations accordingly prepare similar programmes for each province. Through hierarchical and horizontal co-operations and co-ordinations among various actors in this network, the efficiency in policy formulation and implementation is ensured.

2.2 The functions of central administrative organisations concerning China's external economic relations

In the system of the State Council, the ministerial structure has thus been affected by the reforms aimed at strengthening co-operation and co-ordination among government organisations and reducing frustrations in policy making and implementation. Most of the government organisations established in the period of the centrally-planned economy had been removed by the end of the 1990s.¹²³

investigations and provide analysis reports concerning Chinese foreign trade and foreign investment policy implementation.

¹²² First, the SETC informs the local organisations concerning its general ideas about the development of these industries and demands the central administrative organisations and local economic and trade commissions formulate their own plans for restructuring industries. Within the SETC a planning department (guihua si) has been organised, composed of experts of planning in the various industries. Second, on the basis of the plans of local and various industrial administrations, the final national programmes are formulated after extensive consultations between central and local organisations, and pursuit of proposals from think tanks and enterprises. Third, after the final formulation of these national programmes, the central and local organisations concerned accordingly formulate their own programmes to implement the objectives put forward in the national programmes.

¹²³ For instance, the State Council reform program in 1998, launched by current Chinese premier Zhu Rongji, planned to reduce half of its staff. The number of the organisations in the State Council had been reduced from 40 to 29 by the end of the 1990s.

The standing assembly of the State Council, which is currently composed of the premier, four vice premiers and five State Councillors (guowu weiyuan), is the ultimate decision unit in the central administrative system. Most of them are also members of the Politburo. It can be regarded as an 'economic cabinet', for most of the members are responsible for various aspects of the Chinese economy. The five State Councillors include the former foreign minister and minister of foreign trade. They are both Politburo members and members of the Small Leading Group in Foreign Affairs of the Central Committee. Through these institutional arrangements the central party leadership, the central government and functional administrative organisations are incorporated into one collective policy-making unit.

The SDPC, the SETC and the MOFTEC are separately responsible for three principal aspects of Chinese economic operations: planning, domestic economic policy formulation and implementation, and foreign economic policy formulation and execution. Each of these three central government organisations retains its branch at the provincial level both to ensure the policy implementation at the level of local governments and to reflect the local demands to the central administrative organisations.¹²⁴

The MOFTEC plays the principal role in formulation and implementation of Chinese external commercial policies, and as the principal government organisation representing China in negotiation with foreign governments concerning economic exchanges. But it also retains the power to control the import of some commodities. In accordance with the WTO requirement to decrease administrative intervention in economic operations, its importance might decrease following China's accession to the WTO, and its principal functions may transform to formulating a new Chinese external economic law system and supervising the execution of the laws.¹²⁵

Under the leadership of the MOFTEC, six national chambers of commerce have been organised on the basis of the former state trading companies in order to indirectly manage China's principal export commodities: textiles; metals, minerals and chemicals; machinery and electric/electronic products; light industrial products and handicraft articles; medical products; foodstuffs and animal by-products. As the main intermediating linkages between the MOFTEC and the foreign trade entities, enrolling many principal Chinese enterprises

¹²⁴ In the period of transition, some practices of the centrally-planned economic system are still retained and some mixed policy areas arise, their responsibilities often being blurred and changed between various government organisations. Two cases indicate the strengthening co-ordination among them: the catalogue for the guidance of foreign investment industries is jointly issued by the State Development Planning Commission, the State Economic and Trade Commission and the MOFTEC. In the important import and export planning and plan adjustments, the State Economic and Trade Commission and the State Development Planning Commission have a fixed relationship of co-operation and consultation with each other.

¹²⁵ For details of the MOFTEC, see <http://www.moftec.gov.cn>

involved in foreign trade as their members, the chambers of commerce aim at attaining better co-ordinations among the export entities in enforcing the foreign trade policies and function as the formal communication channel between the MOFTEC and export entities. The chambers of commerce have two principal functions: disciplining the exporters' behaviour in terms of the chamber rules in order to decrease the competition between exporters of the same products and feeding back the demands of the exporters to the MOFTEC for formulating appropriate policies. In addition, the experts of the chambers with their expertise in trade also play an advisory role in detailed policy and regulation shaping through institutional arrangements and help the MOFTEC in negotiations with China's trade partners. They also provide information to the chamber members and represent Chinese companies in anti-dumping proceedings abroad.

The SDPC manages to retain its role in 'strategic planning', and its importance in economic development planning (including trade planning of important commodities) and policy formulation has been strengthened due to the launching of the inland development programme. For instance, it plays the decisive role in determining how to make use of foreign investments and loans for important infrastructure projects (e.g. agricultural and environmental projects). Concerning foreign trade, it functions as goal-keeper by retaining the power to approve the importing of some major products categorised either as general or special commodities.¹²⁶

The SETC, organised in the mid-1990s and currently containing nine sectoral associations and ten sectoral administrative organisations, has extensive responsibilities overlapping both trade and industries, but its main responsibilities relate to domestic industries and commerce. It is the centre of industry policy making and implementation, supervises the programmes of industry restructuring, import of advanced technologies and technology upgrading, coordinating the manufacturing of important equipment by domestic enterprises. It guides foreign investments in industrial and commercial sectors, formulates policies of and guiding categories for foreign investments, as well as takes the measures combining the restructuring of state-owned enterprises and attracting of foreign investments. The organisation of this new government organisation indicates the effort of the central administration to retain management of large state-owned enterprises after most of the central industrial ministries have been removed in the process of industry restructuring. Thus via nine sectoral associations the SETC is establishing a hierarchical network with the large state-owned

¹²⁶ For details of the SDPC, see <http://www.sdpc.gov.cn>

enterprises, through which to overcome institutional fragmentation and inter-sectoral cleavages.¹²⁷

The fact that these three principal State Council institutions, although each has its individual assignments, are all involved in foreign economic policy formulations reveals the remaining influences of the centrally-planned economic institutions. But foreign trade and foreign investment have been blended together and it is impossible to deliberately separate domestic economic activities from foreign economic exchanges since the launching of the Open Policy. Thus such arrangements can also be regarded as one to facilitate the transition, namely a transient effort to strengthen horizontal co-ordination and co-operation in policy formulation and implementation among the three principal central government organisations relating to planning, foreign trade and domestic industries. Each of these three central governmental organisations has established its own hierarchical communication networks from the central to the local level. The policy making processes and up-down policy implementation encompass complex planning procedures at all levels of authority.

In summary, in the process of market-oriented economic reforms, the approaches of the state to managing external economic exchanges have been greatly changed, but the strong state role has not been fundamentally weakened. State is not differentiated from society and both are highly centralised. Continuing the dominant roles of the party/administrative agencies, building and structuring the policy networks are the principal approach to maintaining the role of a strong state. The policy networks tend to be very integrated and single-minded, with compulsory membership, ordered linkages with central policy units and overlapping memberships. The

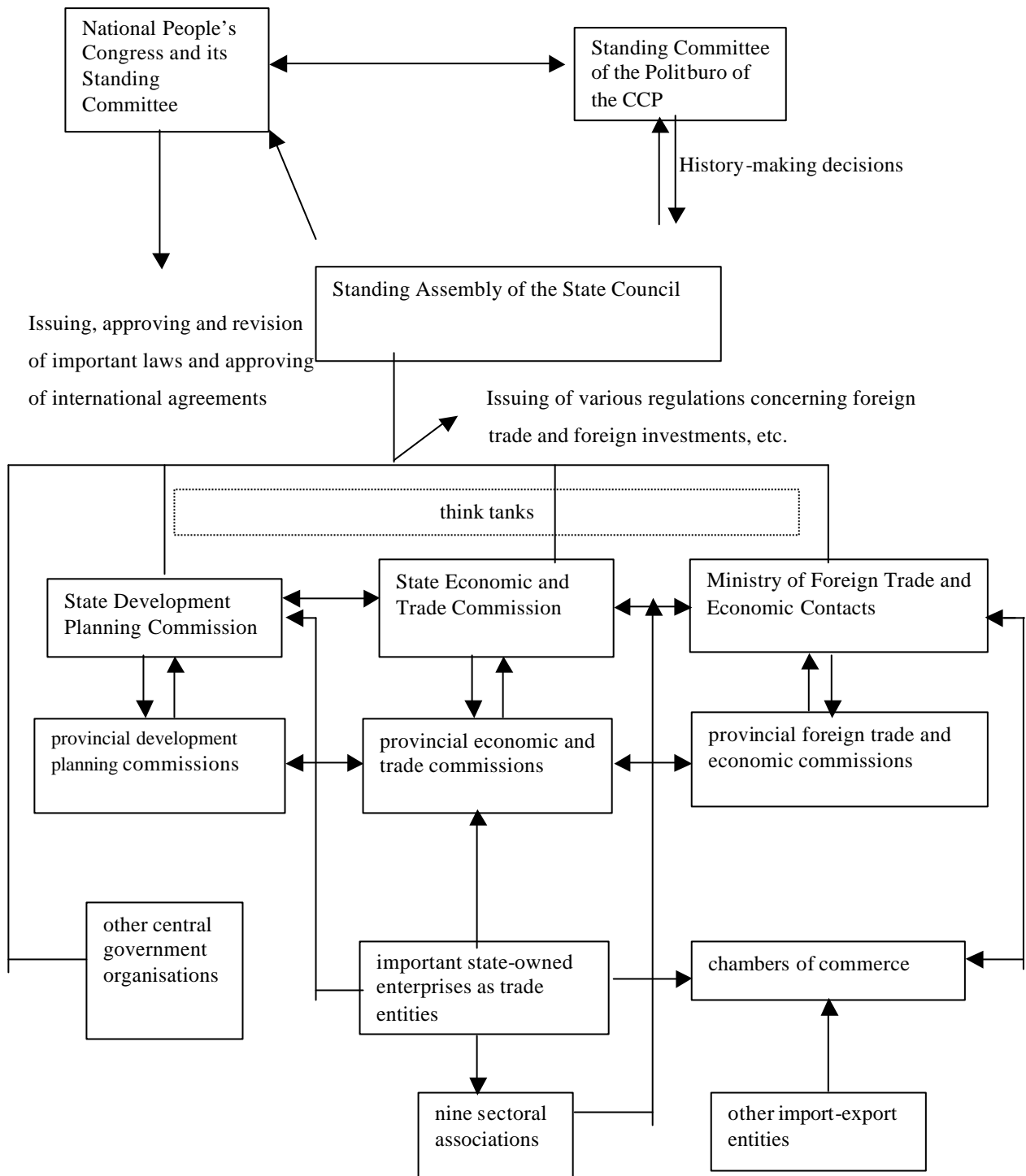
structured networks of foreign economic policies facilitate promoting exports and disciplining import through co-ordinated public and private actors. Through such a combination of hierarchic authority over society and horizontal consultation and bargaining between the central administrative organisations, the state continues its high-degree autonomy vis-à-vis emerging sectoral and regional interests. By incorporating various central government organisations, chambers of commerce as intermediary organisations, large enterprises and enterprise groups, and think-tanks into this policy network, co-ordination and co-operation in policy formulation and implementation are facilitated. (See Figure A)

Obviously, such a framework of arrangements is not in conformance with the WTO requirements to reduce state interventions. According to this framework, domestic and external markets are still separately managed by two central administrative organisations.

¹²⁷ For details of the SETC, see <http://www.setc.gov.cn>

After China's accession to the WTO, domestic market is integrated into the world market. Therefore, these two central administrative organisations will be merged or disorganised, but the central planning organisation may be strengthened in order to smooth some important policy formulation concerning regional development, industrial restructuring and some large state projects aiming at reducing regional disparities.

Figure A: External economic policy making and implementation network



2.3 Principal Chinese actors in the state system involved in the relations with the EC/EU

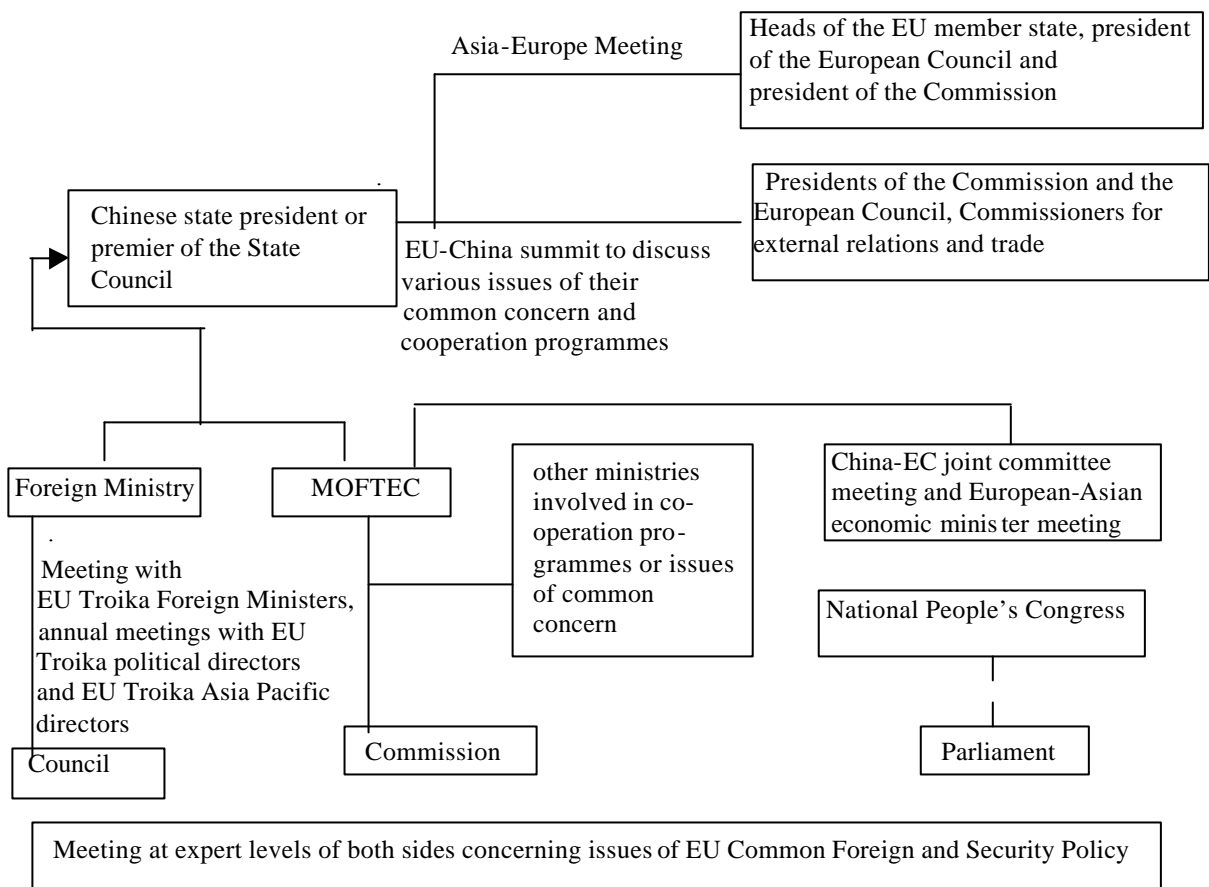
The competence of the EC/EU in its external relations and principal issues concerning different third countries or regions determines what governmental organisations of a third country, such as China, are involved in relations with the EC/EU. After the shift of the EC to the EU and the formal formation of the 'Second Pillar' in the EU's external relations, the EU seek to strengthen the high-level European-Asian dialogues. However, the conduct of the bilateral relations is still mainly limited within the 'Community competence'. (See Figure B)

The MOFTEC is still the principal government organisation in dealing with China's relations with the EC/EU, but its role is declining due to the strengthening of higher bilateral contacts. Since 1984 the Ministry of Foreign Affairs has also established the institutional political consultations with the Council of Ministers of the EC/EU. The National People's Congress had friendly contacts with the European Parliament in the 1980s, but such contacts appeared to exist no more in the 1990s due to China's anger at the fact that the European Parliament was actively involved in interfering in Chinese internal affairs such as the human rights, Taiwan and Tibet issues. With the formation of the 'Second Pillar' of the EU's external relations in the 1990s, the Sino-EU political dialogues have been institutionalised, demonstrated by the establishment of the framework of a structured political dialogue on issues of common concern in 1994. The Sino-EU summit after 1998 functions as a forum to communicate new developments in each side, exchange views on some important international issues and discuss some important issues in their common concern. The Euro-Asian Meeting provides another forum for the leaders of both sides to discuss extensive topics relating not only to bilateral relations but also to important international issues. The tendency is that not only the principal state leaders, but also more Chinese government organisations to various degrees have been involved in the relations with the EU to different degrees.¹²⁸ For instance, at the Sino-EU meeting of 2001, the themes relate to EU eastern enlargement, the illegal immigrants from China, regional security, etc. Thus, the annual meeting between leaders of two sides has become an increasingly important mechanism in the bilateral relations, and the themes discussed have been beyond economic exchanges. However, similar to the situation of the EU's external relations with a strong 'First pillar' but a weak 'Second pillar', the limited extension of this policy dimension does not change the fact that economic exchanges still constitute the principal part of the bilateral relations. Undoubtedly, the EU's economic policies, as the most efficient external policy instrument, have increasingly been

¹²⁸ For instance, the Ministry of Defence and Ministry of Public Security were involved in the dialogue on non-proliferation and the issue of illegal Chinese emigrants.

politicised. But many EU engagements of the Second-Pillar policy domains have been incorporated in the development co-operation policy domain through various programmes and technical assistance. Thus the MOFTEC, both as the principal Chinese representative and negotiator in external economic relations and as the principal Chinese partner of the Commission in carrying out the programmes, in fact continues its role as the principal Chinese government organisation dealing with the relations with the EU.

Figure B Current contacts between China and EU institutions



3 The evolution of foreign trade policy framework

3.1 A survey of the central-command foreign trade management

Before the launching of the economic reform at the end of the 1970s, China's foreign trade, described as 'an extreme example of import substitution',¹²⁹ was put under rigid state control from the trade plan to foreign currency. Such an institution was in conformity with the principal objective of the centrally-planned economic system, by concentrating resources as much as possible to attain the government's primary goals, normally to give priority to heavy and defence-related industries, and through strict control of foreign trade, imports in particular, to maintain the trade balance and ensure the import of materials and equipment for the priority projects.¹³⁰

This state-monopolised and centrally-controlled foreign trade system facilitated concentration of resources on industrialisation in the early period, but the cutting-off of contacts between the manufacturers and the world market, as well as the monopolisation of foreign trade by a few state companies, led to the consequence that the manufacturers had no autonomy concerning their production and profit and could not motivate their initiatives.

3.2 Measures to motivate initiatives for export promotion

Decentralisation of the rights of export has been by far the principal approach to promoting export growth. But it has always been complemented by other policy instruments, such as partly changing the foreign exchange management system and retaining open or implicit state subsidies for exports. These measures aim at motivating the initiatives of various export entities (such entities including foreign-investment enterprises, foreign trade companies, domestic manufacturing enterprises with foreign trade right, and other various economic organisations granted the rights of foreign trade). The centrally-planned system evolved in the 1980s to a mixture of mandatory planning, guidance planning and market forces. The

¹²⁹ Nicholas R. Lardy (1992), *Foreign Trade and Economic Reform in China, 1978-1990*, p. 16.

¹³⁰ The State Planning Commission made the foreign trade plans and supervised the plan implementation. The Foreign Trade Ministry supplied the necessary information for the plan formulation and as the single - government organisation implemented the plans through its foreign trade companies (11 foreign trade companies in 1973 organised according to trade commodity categories). The trade contract negotiations, as well as conclusion and implementation of the contracts, were completely conducted by these companies. The foreign trade enterprises and companies produced, exported and imported commodities strictly in terms of the plans. The state monopoly of foreign currencies through the single state professional bank and the overvalued exchange rate between RMB yuan and foreign exchanges deliberately separated the domestic and the foreign price system.

mandatory planning was legally binding obligation. The government sought to help the foreign trade companies to implement it by means of state credit. The list of products in the mandatory planning had constantly been shortened. In the latter part of the 1990s, while retaining the guidance planning, a foreign trade contract system was developed, in which periodic targets were set for trade entities for value of exports, foreign exchange earnings, and foreign exchange remissions to the state foreign exchange authorities.

The decentralisation of administration concerning the rights of export and simplifying of the approval procedure brought more and more enterprises into the world market. At the end of the 1990s any enterprises could export their products after registering with the proper authorities but not waiting for approval. Well over 200,000 enterprises have the rights of foreign trade.¹³¹ An agency system has been set up to help some enterprises to export their products to the world market. In the meantime, the practice of annual examination of the export performances of enterprises has been introduced, and preferential policies in tax exemption and in loans from state banks linked to export performances and technological upgrading.

The shift from an overvalued to an undervalued exchange rate is obviously favourable for export promotion. The artificially highly valued exchange rate of the RMB was reduced after a period of the dual-track exchange rate system (*shuangchong huilü*), a uniform market-determined exchange rate system was formed in 1994, and in 1996 current account convertibility was achieved. The foreign exchange retention and quota system, adopted after the mid-1980s as an export-promotion instrument, was abolished as early as 1994. Domestic enterprises must surrender their foreign exchange earnings to the banks. If they need foreign exchange, it can be purchased at banks, but such a purchase is under the control of the state foreign currency management bureau (*guojia waihui guanliju*).

Foreign-investment enterprises can retain their foreign exchange earnings but are required to maintain exchange balance. The obligation to use foreign exchange for all foreign transactions in fact forces foreign companies to earn hard currency through export of their products, borrowing abroad, or selling of Chinese goods abroad. The obligation for foreign companies to obtain foreign exchange through the 'swap centres' was abolished in the latter part of the 1990s with the development of a national market in foreign exchange through the banking system.

Another effective means to promote exports is various export subsidies provided both by central and local administrations. Throughout almost the whole period of the 1980s, the

¹³¹ NCNA. March 14, 2001, <http://www.chinesenewsnet.com>

localities profited both from exportation and from the subsidies. In order to increase their revenue, local governments set foreign earning targets for the local foreign trade companies. Numerous rapidly organised local foreign trade companies competed with each other deliberately through raising purchasing prices in order to get more products from the domestic market while reducing the selling prices of the commodities in order to increase their competitiveness on the world market. The consequence was that from 1984 to 1989 there existed a continual external trade deficit.¹³² The striking increase in anti-dumping against Chinese exports to its principal trade partners (also including the EC) in this period was partly a consequence of this confusion. The subsidies increased together with the export growth and progressively became a burden in the latter part of the 1980s.

The central government's revenue decreased in this period mainly due to the worsening performances of more state-owned enterprises, and continuing to support exports with general direct subsidies was either difficult or unnecessary. In this situation, some measures came to be taken to enforce the central control over Chinese foreign trade in order to end the confusion, such as breaking up some trade companies and reinforcing the administrative import management, to replace direct export subsidies with various tax exemptions. While abandoning the practice of generally granting subsidies for exports, the government sought to selectively finance the exports of other high value-added manufactures.

In the early 1990s the government phased out the open subsidies for exports but retained the practice of contracts between the government and enterprises in export amount, foreign exchange earnings, and foreign exchange remission. Some enterprise groups incorporating production and trade have been organised and the state seeks to adopt indirect financial measures other than open subsidies, such as organising the state-run export bank, and providing export credit and funding, to promote exports. During this period, both the increase of foreign earnings and profits from foreign trade were emphasised, and various preferential policies were adopted to accelerate improvement of export composition.

The duty exemptions and tax reductions for supplied and imported (purchased) materials and equipment for export processing significantly reduced the cost of manufacturing exports. Exports associated with this arrangement accounted in the early 1990s for about 64 percent of China's manufacturing exports.¹³³

Various policies to attract export-oriented foreign investments facilitate the favourable trade balance and the building up of foreign reserve in the 1990s. The launching of China's accession to the GATT/WTO requires the government to phase out any state subsidies for

¹³² See statistics in Table 3.1.

¹³³ World Bank, *China: Foreign Trade Reform, a World Bank Country Study*, p. 60.

manufacturing exports according to the rules of this organisation. Thus, the policy emphasis on export-promotion further shifts to improving export composition via increasing the export of high value-added manufactures.

3.3 Reducing administrative control on exports and principal measures to improve export composition

Licensing and quotas are two important foreign trade policy instruments, but their function has undergone a shift from controlling both exports and imports to controlling imports but encouraging exports. Normally, licensing and quotas are linked together, particularly concerning the control of the exports of sensitive and semi-sensitive products, such as textile products. The government has sought to make use of export licensing both to maintain trade order and to motivate the initiatives of the enterprises. First, early in the mid-1980s the categories of the export goods licences are clearly classified in term of central and local control.¹³⁴ Second, export licensing and quota granting are no longer monopolised by certain enterprises but linked to export performances by the introduction of the practice of bidding through competition after 1994.¹³⁵

The principle in allocating export quotas is a bias towards important enterprises with good export performances. The success of this practice is demonstrated by the fact that the share of Chinese fulfilment of the export quotas for textile products has long been 100 percent, contrast as opposed to 80 percent in the case of most other countries.¹³⁶ In the meantime the government is gradually relaxing the licensing control, and the list of licensed exported goods is gradually becoming shorter. In 2000, it included quotas for thirty-two products, among which were 21 textile products and 11 other products.¹³⁷

In order to accelerate the improvement of export composition by increasing the capital- and technology-intensive products, since the 1980s enterprises and technology research institutes have been encouraged to co-operate more closely by transferring their research results into products.¹³⁸ In the 1990s, even state-run technology research institutes and private research

¹³⁴ ‘duiwai jinji maoyibu guanyu chukou xukezhen fenji guanli youguan wenti de tongzhi’ in *Zhonghua Renmin Gongheguo Fagui Huibian (Compilation of Laws and Regulations of the People’s Republic of China)* 1985, pp. 281-290.

¹³⁵ In 1999, more than four thousand enterprises were granted the export quotas through bidding. <http://www.sina.com.cn>

¹³⁶ Sun Jinjun, “fangzhiye ‘lihao’ zhong yeyou yinyou (Some Hidden Issues Concerning the Optimistic Estimation of Textile Industry)”, *Xinhua Yuebao (New China Monthly)*, No. 1, 2000, p. 90.

¹³⁷ NCNA, May 21, 2000.

¹³⁸ Foreign Trade Ministry, ‘guanyu waimao tizhi gaige yijian de baogao’, in *Zhonghua Renmin Gongheguo Fagui Huibian (Compilation of Laws and Regulations of the People’s Republic of China)*, 1984, pp. 378-383.

institutes were also empowered to export their products. In addition, all large enterprises and enterprise groups are required to organise their own research and development centres. The costs of research and development can be compensated through favourable loans and tax exemptions.

Preferential policies are the main policy instrument for promoting the export of high valued-added manufactures, machinery manufactures and consumer electronics in particular. The financial policies include: export duty exemption and various tax concessions, a special state fund for promoting export of these commodities, and special low-interest loans for technological upgrading, some preferential projects in particular, remitting of import duty on advanced equipment for technological upgrading, as well as some provisional measures. Such preferential policies vary from central to local governments. The enterprises with good export performance are granted special privileges in equipment import quotas and awards. These measures are particular to large enterprises of mechanical engineering in order to facilitate production of large and high-technology equipment.¹³⁹ The government demanded that in the ninth five-year Plan period (1996-2000) the export of machinery and electric/electronic products should account for 35 percent of the total export, and realise the shift from exporting low- technology products to capital- and technology-intensive machinery and electric/electronic products.¹⁴⁰

Export diversification has gained more importance in China's export-promotion strategy since the early 1990s. It has two meanings: improvement of export composition and geographical diversification, the former aiming at decreasing dependence on principal exported commodities by increasing the varieties of export commodities, the latter pursuing the access to new markets in order to decrease dependence on traditional principal markets such as Japan, America and the EU. The acceleration of export diversification also has such an importance that more enterprises enter into the world market with an increasing variety of products in order to resolve the dilemma of the over-capacity of production for most manufacturing sectors and the limited domestic market, such as mechanical engineering, textile and clothing, and consumer electronics. The new target regions are Southeast Asia, Latin America as well as the members of the Commonwealth of Independent States.

¹³⁹ 'guanyu jiuwu qijian jinyibu kuoda jidian chanpin chukou de yijian (The proposal to further promote export of electrical and machinery products in the period of the ninth five-year plan)'. <http://www.moftec.gov.cn>

¹⁴⁰ Guanyu jiuwu qijian jinyibu kuoda jidian chanpin chukou de yijian (Some proposals for further promoting export of machinery/electronic products in the period of ninth five-year plan, in <http://www.moftec.gov.cn>

3.4 The evolution of import administration

Many import-substitution practices are still retained. The system of import controls appears to have the multiple objectives of maintaining trade balance, upgrading technology and protecting infant industries. Compared with the export-promoting policies, the import liberalisation has always lagged behind. For instance, the state does not encourage import of 'expensive consumer goods (gaodang shangpin)'. This means that the import of such goods is under strict tariff and non-tariff controls. The pace of trade liberalisation with respect to two principal import-control instruments, tariff and non-tariff, is also unparalleled. The changes in domestic setting are the decisive factors influencing progress in this respect.

Nevertheless, for accession to the WTO, China must further trade liberalisation. To what extent China had made progress in this respect meant the pursuit of a balance between how to partly meet the requirements of its principal trade partners in order to promote the negotiations and how to maximise benefits from the partial liberalisation of trade control. Consequently, there appeared to be a close connection between the selective import liberalisations in different domestic contexts and negotiation periods for the accession to the WTO. While seeking to make domestic policies compatible with WTO requirements, the pursuit of maximum benefits both domestic and external has always dictated the liberalisation of import regime.

With regard to the import tariff system, high tariffs were imposed on capital goods and some intermediates as well as nonessential consumer goods, but very low tariffs on certain raw materials and intermediate inputs to complement the objectives of the plan. But this practice is not absolute. Because of the practice of replacing imports with domestic products, most imported commodities are those that the enterprises in China cannot produce or the production capacity cannot meet the needs. Import duty on the principal imported commodities is low, for instance, the general import tariff level for machinery equipment currently is only about 10 percent.¹⁴¹ Duty exemptions and reductions are also allowed for some imports required for technological upgrading.

The gradual reduction of Chinese import tariff levels in the 1990s indicated the influence of the negotiations for China's accession to the GATT/WTO. The reduction of overall tariff level provided new dynamics for furthering the negotiations, in particular in order to break the deadlock through selective concessions in import tariffs in exchange for concessions from the

¹⁴¹ Shi Guangsheng explained the reforms in the Chinese import duty system. May 15, 2000. <http://www.sina.com.cn>

trade partners. However, in the domestic context of the 1990s, the reduction of import tariff levels had a significant domestic societal and political background.

The concessional import arrangement for foreign investment is obviously unfavourable for domestic industries.¹⁴² In addition to various taxes, the state-owned enterprises must perform many social functions, such as supplying kindergartens, schools, hospitals, and pensions. Their competitiveness was further decreased in the 1990s with the rapidly increasing investments from the transnational companies with the goal of market access. The high import tariff does not protect domestic industries, facilitate reforming the state-owned enterprises or help upgrade technology, for it restricts the enterprises in importing materials, advanced technologies and equipment in order to improve the quality of products with the principal goal of strengthening their competitiveness in domestic and world markets, and impedes the effort of realising economies of scale.¹⁴³ In addition, the policies of the high tariff on imports for domestic enterprises and exemption from tax and import duties for foreign investments also encouraged corruption.¹⁴⁴

Furthermore, the desire to increase the central government revenue is also a cause leading to phasing out the concessional import arrangement. The revenue of the central government in the share of the GDP decreased from 34.4 percent in 1978 to 15.4 percent in 1993 and to 10.8 percent in 1995, mainly owing to worsening performance of the state-owned enterprises.¹⁴⁵ The Chinese government decided in 1996 to begin to unify the import tariff system by removing the concessional import arrangements in duties, and in the meantime to further reduce the import tariff rate. Undoubtedly, the revenue of the central and local governments was accordingly boosted by increasing import duties and various taxes. As the central government sought to unify the import tariff system and reduce the import tariff rate, it strengthened the campaign against smuggling.¹⁴⁶

¹⁴² For instance, in the 1980s, the state enterprises were required to pay corporate tax at the rate of 55 per cent, in contrast to the foreign investment in the Special Economic Zones (SEZs) at the rate of 16 percent corporate tax and joint ventures outside the zones paying 30 percent (plus 3 percent local tax); and foreign manufacturing companies typically enjoy a tax holiday (two tax-free years after the ventures start making profits and a further three years paying only 50 percent of the regular income tax rate).

¹⁴³ The high import tariff did not achieve the goals of promoting the development of some domestic industries. The Chinese automobile industry is a striking example. The Chinese automobile industry has always been regarded as one of the 'strategic industries' and been protected by a high import tariff rate (80-100%), as well as by other non-tariff restrictions from the competition of imported cars. The consequence is that currently China has about 120 automobile plants, and most of them only use 40 percent of their production capacity, leaving aside technology upgrading and international competitiveness altogether.

¹⁴⁴ Almost all imported products under the protection of the high tariff rates became the principal smuggled ones, such as cars, cigarettes, spirits, gasoline, steel etc. Smuggling and evading taxes became the principal income sources of some local government leaders, in particular in the coastal regions.

¹⁴⁵ Wang Huijong *et al*, in Linge (ed.): *China's New Spatial Economy*, p. 41.

¹⁴⁶ The customs duties in 1999 amounted to 100 billion yuan (12 billion US\$) and in 2000 to 220 billion yuan (27 billion US\$), about 2.5 percent of the GNP. The taxes imposed on the enterprises of foreign investments

The tendency is a reduction of the general tariff rate. In the 1990s, the average tariff level in the period from 1992 to 1999 was reduced from 43.2 percent to 15 per cent, and specific low tariffs were imposed on 196 imported commodities so as to facilitate industry restructuring.¹⁴⁷ According to WTO requirements, the average tariff level will be reduced to 10 percent by 2005. It also means the tariffs on some imported capital- and technology-intensive products will be further reduced.

Preferential policies in tax reduction and exemption currently are still the principal instruments to attract foreign investments, including investments by the transnational companies. The current differentiated reduction of tax on foreign-investment enterprises in different regions and sectors has become an effective policy instrument to promote technological upgrading and to help narrow regional disparities. These preferential policies encourage the foreign-investment enterprises to strengthen their involvement in research and development in China.¹⁴⁸ The adoption of differentiated import tariff preferences between foreign investments in coastal and inland regions seeks to attract more foreign investments into the inland regions.¹⁴⁹

While general tariff has been strikingly reduced, non-tariff instruments still remain in the administration of imports.¹⁵⁰ Such measures have varied at different times for different imported commodities. One result of such practices is the high percentage of industrial equipment in China's imports. In 1997, the primary products and industrial manufactures separately accounted for 16.4 percent and 83.6 percent. Non-tariff barriers in 1996 applied to

accounted in the period from 1995 to 1999 for 684 billion yuan, about 14.4 percent of the total amount of industrial and commercial taxes in this period. New China News Agency, March 29, 2000.

¹⁴⁷ MOFTEC.

¹⁴⁸ In 1998 the government decided the equipment of foreign investment (mainly that which domestic enterprises cannot manufacture) in the encouragement and less restriction categories can still be exempted from import duties. According to the new policies to promote foreign investments issued in 1999, any equipment and equipment parts as well as technologies of the research and development centres established by foreign-investment enterprises, can be exempted from import duties. Foreign-investment enterprises in China can be exempted from transactions tax and enterprise income tax provided they transfer technologies to China, and their income from technological transfer is exempted from transactions tax. The cost for research and development, in cases where its increase is higher than that of the previous year by 10 percent, 50 percent of the cost is remitted from the income taxes. For technological upgrading of the foreign investments in the category of encouragement, the imported technologies, equipment, and equipment parts are exempted from import duties; and the value-added tax is returned to them and the cost of purchasing equipment is remitted from the enterprise income tax, provided they purchase domestically produced equipment. Ma Xiuhong, 'Zhongguo xishou waizi de jinzhan ji xin zhengce (The new developments and new policies of China in winning foreign investments)', in *Xinhua Yuebao (New China Monthly)*, No. 8, 2000, p. 88.

¹⁴⁹ The inland provinces can formulate their own catalogues according to their advantages to win foreign investments. The equipment, equipment accessories, spare parts and technologies of the foreign invested projects in these catalogues are exempted of various import duties. The period of tax reducing or remitting for foreign investments in the category of encouragement will be prolonged; any foreign investments in China, if they reinvest and any enterprises with more than 25 percent of their investment in inland regions can be granted preferential treatments, and etc. *ibid.*, pp. 88-89.

¹⁵⁰ Such non-tariff instruments include the mandatory import plan, canalisation of imports, import licensing, and import quota controls, as well as foreign exchange allocation.

about one-third of all imports.¹⁵¹ Currently, three non-tariff control measures – quota licensing, specific import administrative control and voluntary import registering – are adopted to control the import of machinery and electric/electronic products. In 1999, fifteen products were subject to import quota control. The key large enterprises as well as enterprises that produce high-quality products and enterprises with good export performance enjoy privilege for the import quotas.¹⁵²

The principle of control of imports is to permit the import of advanced and high-technology equipment that China cannot produce, in order to minimise the adverse impacts on Chinese enterprises from the imports which are not subject to the state planning. Enterprises are encouraged to purchase as much domestically-produced equipment as possible to replace imported products.¹⁵³ When making effort to upgrade technology of the state-owned enterprises, only ‘advanced foreign equipment’ is permitted to be imported. Normally low import duties are granted to such imports. Purchasing of domestically-produced equipment is encouraged, provided such domestically-produced equipment is on an equal technological level with the imported products. The enterprises purchasing domestically-produced equipment are granted preferential reduction of 40 percent income tax.¹⁵⁴

The following statistics indicate the effect of these export promotion and import controlling policies (see Table 3. 1). In the two decades from 1978 to 2001, China’s foreign trade increased more than twenty-four-fold; the export growth surpassed the import growth (export twenty-seven-fold and import twenty-one-fold); and in most of the first decade trade maintained an imbalance with a Chinese deficit, but throughout the whole of the 1990s, with the exception of 1993, the trade balance was favourable to China.

Concerning China’s export composition, improvement was demonstrated by the rapid increasing of manufactured industrial products after the mid-1980s. From 1980 to 1997, the value of primary products increased from US\$ 9 billion to 24 billion, about 2.6 times; but the industrial manufactured products from US\$ 9 billion to 159 billion, about 17.6 times. The value of industrial manufactured products in 1997 was 6.6 times that of primary products, and

¹⁵¹ Nicholas Lardy (1998), *China’s Unfinished Economic Revolution*, p. 212.

¹⁵² ‘Jidian chanpin jinkou pei’e guanli shishi xize (The detailed implemented administrative regulations on import of machinery and electric products) 1999’, and ‘jidian chanpin jinkou guanli zhanxing banfa (The administrative provisions of import of machinery and electric products) 1994’.

¹⁵³ Taking the example the technology upgrading program in the textile industry, the state demands the textile enterprises should not ‘blindly purchase foreign advanced equipment’ and one principle is to replace imports with domestic products. ‘guojia yaoqiu fangzhi jigai xiangmu yao youxian xianyong guochan shebei (The state demands to give priority to the purchasing of domestically-produced equipment in the technological upgrading of the textile industry)’. <http://www.setc.gov.cn>

¹⁵⁴ ‘jishu gaizao guochan shebei touzi dimian qiye suodeshui zhanxing banfa (The provisional measures of reducing and exempting income tax of enterprises in purchasing domestically-produced equipment in technological upgrading)’.

the percentage of manufactured industrial products in the total export increased from 50 percent in 1980 to 87 percent of the total export in 1997. (See Table 3. 2)

3.5 Summary

The developments between the liberalised export promotion policies and retaining of non-tariff import-controlling policy instruments in different periods of the Open Policy clearly indicate that export promotion but not import liberalisation still dominates China's external commercial policies. According to GATT/WTO requirements, the general import tariff rate has been reduced, in particular for some products important for domestic technological upgrading. The retaining of non-tariff import-controlling policy instruments and various measures to promote replacement of imports by domestic products indicate that the evolution of China's trade regime is still distant from WTO requirements.

4 The evolution of China's policies to attract foreign investments

The evolution of the policy strategy in attracting foreign investments can be divided into two phases, from the end of the 1970s to the early 1990s and from 1993 to now. In the first period the emphasis of the policy strategy was to promote export through various beneficial policies to attract foreign investments with export orientation. In the second period foreign investments came to play multiple roles in addition to export promotion, and the principal policy instrument is now domestic market access. The policy strategy is to deal with the domestic problems by carrying out further liberalisation. Quality rather than quantity of foreign investments is emphasised.

4.1 Policies to attract foreign investment in the 1980s

Two factors were decisive in the policy strategy of attracting foreign investments in the 1980s, the requirement to rapidly generate foreign earnings and the prevailing ideological constraint of self-reliance. Hence, the launching of the policy of attracting foreign investment was only a cautious experiment in the early 1980s, with the principal goal to attract export-processing enterprises from the overseas Chinese. Foreign-investment enterprises were segregated within four 'Special Economic Zones' (SEZs) in two coastal provinces.

The upgrading of technology, learning of managerial skills and marketing were expected to be realised through joint venture, but there were strict requirements of Chinese ownership and managerial control.¹⁵⁵ It indicated the concern of the Chinese leadership about whether the operations of the foreign-investment enterprises could be placed under control. In this period, the foreign economic policies still sought to separate the domestic and the world market. Preferential tax concessions and various preferential measures concerning foreign investment seemed to be more attractive to the overseas-investment enterprises for export-processing. Only a few transnational companies were permitted to invest in China as special cases. For instance, Siemens was the first large German company to invest in China for it was involved in some important Chinese projects.

The SEZs appeared to be a copy of the export-processing zones of South Korea and Taiwan. But in the special Chinese context of transition from a centrally-planned to a market-oriented economy, the SEZs were attributed more functions, set up as 'laboratories' to conduct experiments in foreign investment and management skills, and served as 'windows' for inland regions to understand market mechanisms. In the SEZs, foreign-investment enterprises could benefit from many advantages, including various preferential tax concessions and better public facilities.¹⁵⁶

Such export-processing enterprises rapidly promoted China's exports,¹⁵⁷ but their part in upgrading technology was very marginal. Hong Kong and Taiwan served as principal sources of foreign investment,¹⁵⁸ of which a large part was not in manufacturing and most foreign-investment enterprises in manufacturing concentrated on labour-intensive manufactures, such as textiles and clothing, toys and footwear. Moreover, in 1991, of the 11,500 manufacturing enterprises (with a total foreign investment of US\$ 8,770 million), as many as 3,350 (US\$ 3,220 million) were 'heavily polluting ones.'¹⁵⁹ For this reason, the role of foreign investment in upgrading China's technology subsequently received greater emphasis later by the setting up of Economic and Technological Development Zones and High-Tech Zones in other open

¹⁵⁵ For instance, the chairman of the joint venture board had to be a Chinese and the Chinese share was not permitted to be under 50 percent.

¹⁵⁶ For instance, all goods produced in the SEZs can be exempted from export tax and other taxes, and the import for producing export goods was also tax free. In the case that more than 70% of their products were for export, the enterprises could benefit from further preferential tax concessions.

¹⁵⁷ In 1996 foreign-investment enterprises accounted for 43 percent of China's exports and 47 percent of the country's total trade. Godfrey Linge, in Godfrey Linge et al (1997), p. 10.

¹⁵⁸ During the 1979-92 period, more than US\$ 32,000 million of the total US\$ 38,800 million foreign direct investment was from the overseas Chinese. It accounted for 80 per cent of the total direct foreign investment. Noel Tracy, 'The South-East: the cutting edge of China's economic reform', in Godfrey Linge et al (1997), pp. 75-76.

¹⁵⁹ Ye Ruqiu (1996), 'Sustainable Development in China and International Trade', *International Environmental Affairs*, 8 (1), 16-31.

cities.¹⁶⁰ The ‘experiment’ was extended first to the whole coastal region and later further to other inland ‘open cities’. In the 1990s all provincial capitals were approved to become open cities and were granted policies similar to those towards the coastal open cities. Various types of opened zones spread throughout the whole of China.¹⁶¹ But the principal goal of attracting foreign investment was still export promotion, indicated by the coastal regional economic development strategy of making the coastal region ‘production bases for exportation’, a strategy formally put forward in 1988.

The success of China’s policies in attracting investment from the Western advanced countries in the 1980s was questionable, and it did not improve much in the first half of the 1990s. In the period from 1990 to 1996, 56 percent of the investment was for manufacturing, but only 7 percent for agriculture and communication. The investments of transnational companies have been concentrated in manufacturing industries such as transport vehicles, electric/electronic equipment, etc. with the principal goal of market access. A large part of the foreign investment was for non-manufacturing projects, such as hotels and entertainment facilities. Foreign-investment enterprises for manufacturing concentrated in consumer electronics and telecommunication sets, textiles and electrical equipment and mechanical engineering.¹⁶² The investment from advanced countries (Japan, the United States and the Western European countries) accounted only for 25 percent (by 1996 Japan 15.6% and America 6.6%), and only 2 percent was from the EU countries,¹⁶³ but the American and the EC investment was mainly for technology-intensive projects. Investments from Japan were realised mainly by Japanese government loans. Apparently, China’s policies in attracting foreign investment with the goal of export-promotion through preferential tax concessions were not attractive for the Western investors aiming at market access.

In addition, the preferential policies towards the foreign direct investment created an unfavourable environment for the operations and survival of national enterprises and widened the disparities between coastal regions concentrated with foreign-investment enterprises for export processing and for products to replace imports and the inland provinces concentrated with state-owned enterprises. This adverse development increasingly became an important political issue in the 1990s, as analysed in the next section.

¹⁶⁰ zhong wai he zi jingying qiye fa shishi tiaoli (Regulations to implement the Chinese-Foreign joint ventures law), issued in September 1983.

¹⁶¹ Such as SEZs, coastal open cities, border area open cities, economic and technological development zones (ETDZs), high-tech industrial development parks and bonded zones.

¹⁶² Zhang Fan & Zheng Jingping, ‘kuaguo gongsi dui zhongguo jingji jiegou he xiaolu de yingxiang (The influences of multi-national companies on Chinese economic structure and efficiency)’, in *Jingji yanjiu (Economic Studies)*, No. 1, 1999, p. 47.

¹⁶³ *Zhongguo DuiwaiJingji Maoyi Nianjian (Yearbook of Chinese Foreign Economy and Trade)*, 1997.

4.2 Policies to attract foreign investments in the 1990s: exchanging domestic market access for acquisition of foreign technologies

Foreign-investment enterprises in China normally have the following objectives: reducing costs for export products and (or) pursuing domestic market access. In general, the small and medium-sized enterprises from the overseas Chinese and a certain number of Japanese and American enterprises belong to the former, but most of the investors from other advanced countries, the transnational companies in particular, belong to the latter.

The concept of ‘exchanging domestic market access for acquisition of foreign technologies’, put into policy operation in 1993 gave the green light to continuing the process of China’s accession to the WTO and further reforming Chinese external economic institutions according to WTO rules. Its concrete meaning can only be defined in terms of policy practices, basically as a set of policies with the principal goal of replacing imports with products manufactured by foreign-investment enterprises in China. Various preferential policies facilitate the operation of foreign-investment enterprises which have high technologies. They are protected from the competition with imports by various tariff and non-tariff policy instruments.

The formulation of this concept in the early 1990s had a significant domestic social and political background, namely through attracting foreign investments to facilitate dealing with increasing domestic issues in the transition period. The preferential policies at least aim at attaining two strategic goals simultaneously. First, foreign-investment enterprises which have high technologies, mainly transnational and large companies, would be attracted to manufacture in China. This certainly facilitated replacing some imported items and accelerating technology upgrading of Chinese enterprises in manufacturing sectors. Second, foreign investments facilitated dealing with increasingly serious socio-economic issues, such as the demands to reduce unemployment, restructure state-owned enterprises and narrow regional disparities. These two aspects are combined together. As a result of putting this strategy into policy practice, some industrial sectors, both traditional and ‘strategic’, e.g. mechanical engineering, automobile and petrochemical, etc. have been permitted to open to foreign investments. The new policies have brought about rapid foreign-investment growth (see Table. 3. 3). This has also been demonstrated by the increase of the investment from the EU.

The new policy strategy mainly aims at attracting transnational companies which have advanced technologies. Joint venture is so far the main form of foreign-investment enterprises

in China. Foreign one-party investment must be export-oriented or produced to replace imports.¹⁶⁴ Foreign investors are required to give priority to Chinese raw materials and products in their purchasing, and if they have to import foreign raw materials and products, they must seek with their own means to maintain the balance of foreign earnings.¹⁶⁵ These requirements in fact compelled foreign-investment enterprises, despite the fact that their primary intention was pursuit of market access, to export their products manufactured in China in order to maintain the balance of foreign earnings. Consequently, the foreign-investment enterprises for exports continually increased. In 1999, the enterprises with exports of more than US\$ 10 million amounted to 1,441, and their exports accounted for 57 percent of the total exports by foreign-investment enterprises and 25.9 percent of total Chinese exports.¹⁶⁶

The policies towards foreign investors in the automobile industry provide a convincing example to explain the foreign-investment policies concerning infant industries. The establishment of an advanced automobile industry has always been a Chinese ambition. The final goal in developing this industry is to organise three large enterprise groups with international competitiveness by 2010, which have the capacity for research and development, manufacturing and marketing. Foreign investment in this industry will be permitted through joint ventures, but it must satisfy the following conditions: manufacturing the newest products, establishing research and development institutes in the enterprises, giving priority to domestically-produced spare parts and maintaining the balance of foreign exchange through export of the products of the joint ventures. In percentage terms, the Chinese share in the joint ventures cannot be below 50 percent; and more tax concession will be granted to the investors who purchase more domestically-produced spare parts.¹⁶⁷

Concerning services sectors, the Chinese government has agreed to open financing, insurance, telecoms, and foreign trade, as well as some other services sectors, 'by steps'.¹⁶⁸ However, some restrictions are and will be retained, and the loosening of the restrictions is a gradual process. In this respect, the Chinese government fully takes advantage of the WTO exceptions

¹⁶⁴ For permission to be granted, foreign one-party investment must satisfy either or both of these two conditions: first, adoption of sophisticated technologies, production of new products, saving materials and energy, enhancing the qualities and functions of the old products and the products replacing the imported products; second, the value of exportation superior to 50% of the value of total production, and the maintenance of the balance between export and import, or export exceeding import.

¹⁶⁵ 'zhongwai hezi jingying fa (The law of the PRC on Chinese-Foreign Contractual Joint Ventures)', 1983, articles 57 and 75. 'zhonghua renmin gongheguo waizi qiye fa (The Law of the PRC on Foreign-Capital Enterprises)', 1986, articles 15 and 18.

¹⁶⁶ <http://www.moftec.gov.cn>

¹⁶⁷ The State Planning Commission, 'qiche gongye changye zhengce (The policies for automobile industries)', 1994.

¹⁶⁸ Lianhe Zaobao, October 18, 2000.

for developing countries, with the principal goal of protecting some state-monopoly sectors, such as banking, telecommunication, transport-communication, etc. For instance, the state-monopoly telecommunication will be divided into several domestic firms, but foreign access to this sector can only be permitted through joint-venture and with share restrictions. For banking, restrictions are imposed on foreign financial institutions in dealing with the operation of Chinese currency. The positive developments in this respect might first occur in the inland regions, for both the pressure to reduce unemployment and the imperative to improve investment environment demand the central government to adopt more preferential policies towards these regions concerning foreign investment.

The above two cases seemingly indicate that the idea of reducing foreign dependence still plays a role in China's foreign-investment policies. The state continually seeks to exert control on foreign investments in some important and infant industries. However, taking account of the fact that a number of these sectors are still under the management of some central government organisations and their interests are closely linked with these organisations, it can be argued that the demand of protecting the interests of these state-monopoly infant industries has been the major factor obstructing the opening of these industries to foreign investors.

The opening of these infant industries to foreign investors may be accelerated, namely that the state seeks to guide foreign investments to preferred regions and sectors. So far foreign-investment enterprises have been concentrated in the coastal regions. Their operations are facilitated by the services of foreign financial institutions there. In contrast to this, the inland regions, partly due to the lack of such favourable conditions, are difficult to attract foreign investments there. Currently, regional disparities and unemployment have become the principal factors influencing political and social stability. Thus, the opening of more services sectors to foreign investors who are willing to invest in the inland provinces, as one part of a comprehensive package of policies to pursue smooth transition, is seemingly inevitable.

In short, China's policy framework concerning external economic exchanges has combined preferential and discriminating policy measures towards foreign investors. Such measures do not facilitate attracting foreign investments with the principal objective of market access. The building of a stable and conducive investment environment by granting equal treatments to foreign and domestic investors is a more appropriate choice.

5 Widening regional disparities, reforming state-owned enterprises and emergence of new economic development strategy

In China, regional disparities, namely the disparities between inland and coastal regions, and the difficulties of restructuring the state-owned enterprises are two sides of one coin. Due to historical factors, most of the important state-owned enterprises of traditional and defence-related industries spread in inland provinces.¹⁶⁹ Moreover, the difficult and long-term tasks in alleviating poverty of rural populations, reducing unemployment, promoting comprehensive developments in the minority-concentrated areas and pursuing sustainable economic development are mainly related to the inland regions.

The importance of the state-owned enterprises is demonstrated in the following aspects. First, the state-owned enterprises are so far the main employers of labour forces; by the end of the 1990s they possessed more than half of total national capital and a skilled labour force of 90 million. In the inland regions with fewer foreign-investment enterprises their roles in this respect are crucial. Second, they compose the stock of Chinese industries, the traditional and strategic industries in particular, concentrating a large number of well-educated technicians and skilled workers. Third, even in terms of export performance, the state-owned enterprises are now coming to play a strikingly active part in improving Chinese export composition by the export of manufactures and the supply of high-quality products.

Following China's accession to the WTO, the retaining of some strategic industries and developing their international competitiveness through supporting and developing the state-owned enterprises are not merely an issue of whether China can avoid the dependence on other advanced countries. More important, the enterprises of these industries, spreading in inland regions and functioning as important employees, relate to serious political and social issues arising in the 1990s in these regions. Faced with strong competition with imports and products by foreign-investment enterprises in the coastal regions after China's accession to the WTO, the restructuring of the state-owned enterprises will have more difficulties. The

¹⁶⁹ The emphasis of Chinese industrialisation was always laid on heavy industry sectors during the three decades from the early 1950s to the early 1980s. During the First Five Year Plan period (1953-57), only 5 of the 156 major projects were located along the eastern seaboard, and among these projects, 56 were located in the north-east, 33 in the north-west, and 27 in the north. In the period from 1964 to 1975, owing to the shift of national regional strategy from a 'balanced' to a 'strategic' distribution in the context of over-concern over external security, a 'Third-Line' area was created in the remote mountainous hinterland where defence facilities could be hidden. This area (mainly in the south-west but also in part of the north-west regions) accounted for 55 percent of the country's defence-related factories. By the mid-1970s some 16 million people were employed in the 29,000 Third-Line enterprises (including 600 of the country's 1,500 largest industrial plants). Many of these projects built in the 1950s and 1960s were by the end of the 1980s technologically out of date, inefficient and unprofitable. Wang Huijiong, *et al*, 'Regional Planning: Development of an Indigenous Framework', in George Linde (ed.). *China's New Spatial Economy, Heading towards 2020*, pp. 23-28.

survival and continual operations of these state-owned enterprises are directly related to the overall economic development and social stability in the whole country. Thus, it is necessary for the Chinese leadership to formulate a new development strategy, to incorporate the goals of promoting sustained economic growth, maintaining political and social stability and meeting the challenges arising from the accession to the WTO.

5.1 Widening regional disparities and state-owned enterprises reforms

The export-oriented foreign investment policies in the 1980s encouraged the entry of foreign investments in the coastal region, but they also had the less desirable effect of widening the regional disparities.

The situation of the state-owned enterprises with growing loss has deteriorated since the mid-1980s. In 1997 about 40% of state enterprises were loss-making and the loss amounted to 80 billion RMB.¹⁷⁰ The government had to provide subsidies (implicit financial subsidies and budget subsidies) till 1996, but such subsidies increasingly became a burden with the deteriorating government revenue. In this situation, to continue the preferential policies towards the foreign-investment enterprises would have contributed to strengthening their competitiveness on the Chinese market and accordingly to increasing the pressure on restructuring the state-owned enterprises. The central government decided to remove part of the preferential policies towards the foreign-investment enterprises in the coastal regions in the mid-1990s and to cancel the state subsidies to the state-owned enterprises in 1996. The main approach became supporting the reform of the enterprise management and technological upgrading through favourable funding and other policies rather than providing direct subsidies to maintain the operation of the enterprises, supplemented by creating an equal-competition environment through reduction of some preferential policies towards the foreign-investment enterprises.

The policy principle in restructuring the state-owned enterprises has undergone evolution, a shift from ‘grasping the large but deregulating the small enterprises’ (Zhuada fangxiao) to ‘grasping the large and helping the small enterprises’ (Zhuada fuxiao).¹⁷¹ Such a shift reveals the concern over the rapid increase in unemployment as well as its consequence, in particular in some regions concentrated with small enterprises. The efforts concentrate on five aspects: building up large and important equipment in the state-owned enterprises for some large

¹⁷⁰ *Far Eastern Economic Review* (FEER), February 18, 1999, p. 11.

¹⁷¹ Thomas G. Rawski, ‘China’s State Enterprises Reform—an Overseas Perspective’, *China Economic Review*, volume 8 (1), 1997, p. 92.

projects launched by the state, upgrading technologies of manufacturing through state financing, regrouping the state-owned enterprises into large enterprises or enterprise groups, encouraging the large enterprises to annex other small enterprises, closing some loss-making but helping the profit-yielding small enterprises. The principal goal is to support some Chinese enterprises with competitiveness in the market and build some large enterprises (groups) with international competitiveness, in order to make it easier for Chinese industries to bear the impacts after China's accession to the WTO through economies of scale, effective management and technological upgrading.

The state concentrated its resources to support about 520 large state-owned enterprises and enterprise-groups through various preferential policies in financing, technology upgrading and attracting foreign investment. Such policies also link to the efforts of building some 'pillar' industries (automobiles and automotive parts, petrochemicals, electric/electronic and mechanical engineering, and construction). Each enterprise group must organise its own research and development centres to upgrade the technology and develop new products. By the end of 1997, 120 enterprise groups of this kind had been organised, allocated in many important industrial sectors, such as automobiles, steel, electric power, the chemicals, aviation industry, computers, the pharmaceuticals, building materials, etc.¹⁷² The final goal of restructuring the state-owned enterprises is to establish a 'modern enterprise system' with modern managerial expertise, research and development capacity, marketing know-how, and high-quality products with domestic and international competitiveness.

The closing of the loss-making enterprises and regrouping of enterprises inevitably led to an increase in unemployment in some regions where there were concentrations of state-owned enterprises of mechanical engineering, chemicals and textiles, particularly in the Northeast region and in the remote inland provinces. The underdevelopment of the service sectors in the inland regions means that it is impossible to employ large numbers of the unemployed and laid-off workers.¹⁷³ This situation did not improve much in the second half of the 1990s.¹⁷⁴

In the latter part of the 1990s the government decided to open some 'strategic industries' mainly composed of state-owned enterprises and concentrating in inland regions for foreign investments but with various restrictions, such as mechanical engineering, chemical and light

¹⁷² See 'the list of pilot state enterprise groups (Guojia shidian qiye jituan mingdan)', in *Xinhua Yuebao (New China Monthly)*, 8, 1997, pp. 119-120.

¹⁷³ According to Chinese official statistics, by 1994 the urban unemployment rate remained between 3% -3.6%, but it did not include 30 million surplus employees of the state industries (the so-called 'laid-off' workers). The real unemployment rate was more like 15%-20%. *FEER*, October 30, 1997, p. 56.

¹⁷⁴ In 1998 the official number of urban unemployed was 11 million, not including 3-4 million workers who were being laid off from falling state-owned companies as the government attempted to turn them around. *FEER*, February 25, 1999, p. 47.

industries. Rather than export promotion, other goals seemingly become more important, such as pursuit of technological upgrading, gaining of managerial know-how and marketing, and reducing unemployment. The principal target is now the transnational enterprises. Some of the state-owned enterprises have been given a new vitality by an infusion of foreign capital, in so-called 'marry and connect' deals. In addition, to open more areas in the service sector for foreign investment (with various restrictions) can facilitate reducing the unemployment and winning foreign-investment enterprises for manufacturing. Thus, it seemed to be concluded that the strategic considerations in the foreign-investment policies, namely to protect some important manufacturing industries with a high concentration of state-owned enterprises from the competition of foreign-investment enterprises, had to give way to the urgent requirements of alleviating societal pressures due to increasing unemployment through appropriate foreign economic policies to support the enterprises in these important manufacturing industries. Such a change in foreign-investment policies is of substantial importance for the foreign investments in traditional industries, such as chemicals, mechanical engineering, etc. Some European transnational companies with international competitiveness in these sectors now got the chance to invest or enlarge their investments in China.

The concept of attracting foreign investments with market access evolved in the latter part of the 1990s to a policy of guiding foreign investments to the preferred projects in inland regions through more preferential policies: technological investments in the inland regions are the most likely to be permitted, and foreign-investment enterprises in these regions are more likely to gain real market access. The inland local governments and defence-related state-run corporations are granted more autonomy in attracting foreign investment.¹⁷⁵ Each province has specific projects according to its comparative advantages in natural resources and local social-economic demands. Foreign investments in the so-called 'pillar' industries in each province, particularly concerning the reform of the old industrial bases, are encouraged with much more preferential policies.¹⁷⁶ Foreign investors in some large and important state projects in agriculture, transport-communication, energy, raw materials, irrigation works and environment projects will be granted tax concessions as well as other special preferential treatment.

¹⁷⁵ For instance, they are permitted to approve large foreign investment projects under the ceiling of US\$ 30 million dollars without the central government's approval. See 'guowuyuan guanyu kuoda neidi sheng zizhiqu jihua danlieshi he guowuyuan youguan danwei xishou waishang zhijie touzi xiangmu shenpi quanxian de tongzhi (Circular of the State Council about Extending the Approval Power of the Inland Provinces, Autonomous Regions, Municipalities with Individual Planning and State Council Departments Concerned in Attracting Foreign Direct Investment Projects)', 1996.

¹⁷⁶ zhongxibu diqu waishang touzi youshi chanye mulu (Catalogue for Guiding Foreign Investments in the Advantageous Sectors in Inland Regions).

The government sought to concentrate financing, including the loans from foreign governments and international finance institutions, in order to accelerate construction of important infrastructure and environment projects in the inland regions. Undoubtedly, the launching of large projects puts forward new demands for importing foreign equipment, but it also opens new dimensions for foreign investors.

The issuing of catalogues by the central administration to guide foreign investments indicates the administration sought to play a more active role in 'guiding' foreign investments to the preferred projects. These catalogues are more inland-oriented. According to the 1997 catalogue,¹⁷⁷ foreign investments are divided into three categories: encouragement, restriction and prohibition. It granted more preferential policies to investment particularly suitable for the inland regions. The restrictions can be relaxed provided the foreign investments are made in the inland regions; the investors can profit more in the inland regions through special tax concessions, and the foreign investors in the coastal regions are encouraged to reinvest in the inland regions. Foreign-investment enterprises are asked to meet technological requirements.

The restriction category of foreign investments mainly concerns the industries with surplus domestic production capacity as well as low technologies,¹⁷⁸ the state-monopoly sectors, such as telecoms, services and finance, and some important or precious mineral productions.

Through such differential treatment of foreign investments, the government seeks to attain multiple goals, such as promoting the technological upgrading of foreign-investment enterprises in the coastal regions while transferring some of the labour-intensive foreign-investment enterprises into the inland regions, in order to accelerate economic growth and facilitate alleviating the serious unemployment in these regions.

However, the new policies seemed to take little effect. This is indicated by the following facts. 84 percent foreign investments still concentrated on industries (59.56 percent) and immobile (24.44 percent) by 1999. The inland regions (including 20 western and central provinces and one municipality accounted for only 12 percent of the total foreign investments in China, but the coastal regions 85 percent by 1999 (85 percent by 1990), among which only Guangdong accounted for 28.25 percent and Jiangsu 12.13 percent, in contrast to Xinjiang 0.11 percent, Ningxia 0.04 percent, Qinghai 0.01 percent, Gansu 0.13 percent, and Guizhou 0.13 percent.¹⁷⁹

Thus, the specially preferential policies obviously lack enough dynamics to attract foreign investments into inland regions. In this situation, the central government has to adopt more effective public measures to facilitate changing this situation, namely to formulate new

¹⁷⁷ zhidao waishang touzi fangxiang zhanxing guiding (Provisions guiding foreign investment orientations) 1995, Waishang touzi chanye zhidao mulu (Guiding Catalogue for Foreign Investment Sectors), 1998.

¹⁷⁸ For example, the sector of consumer electronics with an over-capacity.

¹⁷⁹ <http://www.moftec.gov.cn/>

policies of allocation, redistribution and stabilisation to support the inland regional developments.

5.2 Programme for inland region development

Wang and Hu outline five factors of the greatest importance for determining success or failure in attracting foreign investment: market size, rate of economic growth, infrastructure, human capital and preferential policy.¹⁸⁰ Among these factors the rate of economic growth and preferential policy are particularly important. Compared with the coastal regions, the inland regions generally are disadvantaged in these five factors: the lack of a sizeable market for the products of foreign investment, the relatively low rate of economic growth compared to the coastal regions, the backwardness of infrastructure facilities. Even the best universities, with a few exceptions, are concentrated in Beijing and Shanghai as well as other coastal metropolises. The high wages paid by the enterprises in the coastal regions, in particular the foreign-investment enterprises, further attract the well-educated youth to move from the inland to the coastal regions.

By the end of 1990, mainly relying on the beneficial policies, better infrastructure facilities and services, Chinese coastal regions accounted for around 85% of foreign investments,¹⁸¹ including most of the investment from the advanced industrial countries. In contrast to this, by 1994 the inland regions accounted for just 11 percent of Chinese foreign investment, despite having 60 percent of the population.¹⁸² In addition, the village and town enterprises for export processing employ large numbers of the countryside population, but in the inland regions the village and town enterprises are not developed sufficiently to employ the surplus village labour forces, and therefore become the main sources of flux of countryside population to look for working opportunities in the cities and the developed coastal regions in particular.¹⁸³ The linear relationship between the coastal regional bias of foreign economic policies and the widening regional disparities can be indicated by the divergence in income per capita between these two regions: in 1994 high income per capita (above 120 per cent of the national average) was concentrated in these eight coastal provinces and metropolitan centres (compared with

¹⁸⁰ Wang and Hu, *The Political Economy of Uneven Development, the Case of China*, pp. 157-158.

¹⁸¹ Wang Shiyuan, *Zhongguo Gaige Kaifang Shidian (Important Developments of Chinese Economic Reforms and Open Policy)*, p. 465.

¹⁸² *FEER*, April 18, 1996, p. 84.

¹⁸³ The number of migrant workers is 80 million according to the government's estimate, but other plausible estimates put the real total for 1996 at between 120 million and 140 million, and that by 2000 the surplus rural labour force will probably reach 140 million. In Godfrey Linge, 'An Overview: Towards Sustainable Development?' in Godfrey Linge *et al.*, p. 8.

four in 1978), and low income (below 80 per cent of the national average) in fourteen inland provinces (compared with ten in 1978); and four coastal provinces (Fujian, Zhejiang, Guangdong and Jiangsu) rose from low- and middle-income per capita provinces in 1978 to high income per capita province in 1994.¹⁸⁴ This situation is further deteriorating. In 1998, the income per capita in Shengzhen was 20,245 yuan, but in Xi'ning only 4,245 yuan.¹⁸⁵

Narrowing the regional disparities is not only important for maintaining long-term economic growth but also relates to national solidarity. Most of the ethnic minorities inhabit the Western provinces. The poverty of the ethnic minorities due to backward economic growth cannot encourage them to integrate in the Chinese community.

The largest part of China's mineral and fuel materials is concentrated in the inland regions.¹⁸⁶ Accordingly, the traditional industries such as iron and steel, energy, mechanical engineering, building materials, mining, etc., are also located in these regions. For a large country like China, these enterprises are vital factors for maintaining long-term economic growth and decreasing China's external dependence, despite the fact that currently it is more important to maintain the operation of these enterprises in order to alleviate unemployment. Foreign investors, if denied real market access, normally are not interested in these traditional inland industries operated by state-owned enterprises. In this context, only active state interventions can assist these enterprises to survive and develop.

The continually deteriorating situation in the inland regions in the 1990s compelled the central government to incorporate industry, and regional and external economic policy goals into one new comprehensive development strategy, while continuing the export-promotion strategy policies. The western regional development programme formulated in the latter part of the 1990s can be regarded as one component of the new development strategy. It implies the adjustment of the former coastal regional development strategy, in which the economic growth in the coastal provinces through export promotion played the locomotive role for the national economic development. Through the launching of the western regional development programme, China's sustained economic growth will be supported by two mutually complementary pillars, high-speed economic growth in the coastal region supported by the active export-oriented foreign-investment enterprises and the sustainable economic growth in the resources-rich internal regions with a high concentration of traditional industries.

Concerning industries, the emphasis of this programme is laid on supporting industries with local resources advantages, such as gas and petroleum, electric power generating, mineral

¹⁸⁴ Wang and Hu, p. 49.

¹⁸⁵ *Xinhua Yuebao (New China Monthly)*, No. 8, 1999, p. 75.

¹⁸⁶ The inland regions here mean western, central and north-eastern regions in China, including 18 provinces apart from the 11 coastal provinces and municipalities.

exploiting, important manufacturing enterprises, and agricultural products processing, reinforcing the efforts to restructure the traditional industries. By granting special preferential policies towards foreign investments, the central government seeks to attract more foreign-investment and national enterprises into the inland provinces.¹⁸⁷

The large projects for improving the infrastructure facilities can help the operations of many state-owned enterprises, such as mechanical engineering, steel, building and building materials. Such projects also have the multiple goals of restructuring these enterprises through advanced technologies, managerial know-how and technological upgrading. Undoubtedly, foreign investments can play a positive role in attaining these goals. Moreover, a series of environment protection projects aiming at pursuing a sustainable economic growth can also facilitate alleviating local unemployment and rural poverty in this region. The central government has begun to adopt more preferential policies to attract foreign investments into the inland regions in services sectors, such as tourism, commerce and insurances. With foreign, central and local financing, these projects may be attractive to foreign investors.

The launching of this programme has also important long-term political and social significations. Through a variety of large projects for supplying energy and electric power from the inland to the coastal regions and for improving infrastructures in the inland regions, the central government seeks to strengthen the economic connections between the inland and coastal regions by making the coastal provinces more 'inland-oriented', in order to create a 'domestic inter-regional interdependence'. Undoubtedly, as a part of improving the investment environment, the improvement of the infrastructures in the inland regions would certainly have positive influences on attracting foreign investments to these regions, provided it is accompanied by various extra-preferential policies. The alleviation of various societal and economic difficulties in the transition period and maintenance of the political and social stability might be facilitated by this programme.

According to the Ninth Five-Year Plan (1996-2000), the catalogue included: implementing favourable investment policies to encourage resource extraction; providing from government sources most of the investment funds needed for trans-regional infrastructure; readjusting the distribution of localities with processing industries; guiding resource-related and labour-intensive industries to resettle there; rationalising the prices of resource-related products to enhance self-development capabilities; implementing a regulated central government financial transfer payment system and gradually raising financial support; guiding more foreign

¹⁸⁷ For instance, in addition to the Catalogue to Guide Foreign Investments in Preferential Industries in Central and Western Regions, a new document has been issued to encourage foreign investments in exploiting mineral resources. Foreign investors now can participate in exploiting Chinese mineral resources in one-party investment or co-operation with Chinese enterprises, and be granted preferential treatments on import duty and taxing.

investment there; and raising the percentage of state policy-related loans going to central and west China which should get 'over 60 per cent' of soft loans provided by international financial agencies and foreign governments. The enterprises in coastal region will be encouraged to invest in the inland region.

Such a plan is a part of the emerging national cohesion policy, combining the policies of allocation, redistribution and stabilisation, with the aim of increasing the efficient supply of the factors of production and the competitiveness of the recipient regions and achieving convergence between regional economies. The goal of this plan is definite: by improving the infrastructures in the inland regions to facilitate attracting foreign investments and bringing the comparative advantages of the inland regions into full play. Through such comprehensive policies it is possible to facilitate alleviating the difficulties in the inland regions and forge closer economic connections between the inland and coastal regions. Undoubtedly, the accelerating developments in the inland regions will provide new dynamics supporting the sustained national economic growth and minimise the adverse external impact from possible international economic recessions or crises.

In order to promote transferring some foreign investments from the coastal region to or attracting more foreign investments into the inland provinces, the central government formulates inland-biased preferential foreign investment policies. The principal goal of these policies is to narrow the centre-periphery disparities within the country through policy adjustments. The specific category for each inland province to encourage foreign investment does not emphasise export-promotion. Environmental, agricultural, mineral production and some large energy projects have been opened to foreign investments. The projects of environmental protection as well as communication, electric power, irrigation works and postal services are granted special preferences in tax reducing or exemption.

In summary, the government has the intention to distinguish functions of foreign investment between the coastal and the inland regions. The coastal region focuses on attracting export-oriented and advanced technology-intensive foreign investments. For the inland region, the effort is to attract labour-intensive foreign-investment enterprises from the coastal regions and to guide foreign investments to more extensive sectors, such as infrastructures, traditional industries and environmental protection. In addition to the granting of more preferential policies and real market access to the foreign investments, the lowering of the technological requirements and the opening of services sectors to foreign investors, the inland regional provinces have obtained more autonomy in determining foreign investment projects. The government further concentrates financing on the target technological imports for the

preferred industrial projects – energy, petrochemicals, mechanical engineering and the electric power industry. Thus the technology-concentrated and export-oriented coastal region will become more dependent on the inland regions in electric power and raw materials supply and this will strengthen the economic linkage between the two regions. In addition, the launching of these projects might bring some long-term positive impact on imports and foreign investments. Concerning the extent of such impact on imports and investments from the EU, it will rely on the concrete projects.

6. Conclusion: between mercantilism and liberalisation

This chapter can only provide an oversimplified analysis of the evolution of Chinese economic institutions, both for reasons of space and because of the complexity and speed of institutional evolution. From the analysis one can conclude that, from the beginning of the Open Policy, mercantilist export promotion has been the principal goal, and reform of external economic institutions is mainly undertaken to advance this goal. This is demonstrated by the fact that developments in export promotion and import liberalisation have not been parallel. It is a controlled integration into the world market.

The tendency to trade liberalisation became more obvious in the 1990s, particularly after 1993. More measures were adopted to fulfil WTO requirements, while mainly concentrating on reducing import tariffs. Some administrative measures to control imports have been removed. However, so far such selective trade-liberalisation measures have not fundamentally changed the strategy of maximising benefits through partial integration in the world economy.

Such a conclusion can be supported by the following summary of the noteworthy features of current Chinese external economic policies. A combined strategy of preferential policies (various state subsidies such as duty and tax concessions, interest-free loans, special state export bank and export funding, etc.) and extensive granting of the rights of export aims at promoting exports and improving export composition by promoting the entry of more trade entities to the world market. The retaining of various tariff and non-tariff instruments to control imports supplemented by the reducing of import tariffs on selected imported commodities, mainly conducing to meeting various needs in domestic developments in different periods. Foreign investments are guided to preferred sectors and regions through various differentiated preferential or restrictive policies.

The phenomenon that the bulk of the investments from the advanced countries is from large or transnational companies indicates another serious problem facing Chinese policy practices in attracting foreign investments. China has not built up a transparent external economic legal

institution conforming to the WTO rules.¹⁸⁸ The policies are often changed according to demands in different domestic and local situations. In addition, local authorities have extensive autonomy to interpret these policies through local regulations. Their policy practice normally aims at satisfying local interests by steering the operations of foreign investment enterprises. Most foreign investment coming to China in the 1990s still concentrated in the Yangzi Delta and other coastal provinces. The relatively disciplined behaviour of the local governments in the coastal region was an important factor behind this bias, in addition to beneficial policies and reduced freight costs. More seriously, local interests have been increasingly linked with those of the foreign-investment enterprises, both to increase local revenue and to reduce local unemployment. Thus, local governments sought to formulate mutually competitive preferential policies in order to attract foreign investments and to protect the interests of the local foreign-investment enterprises and local markets through various administrative regulations with the goal of reducing competition and limiting the market share of the products of other regions. Consequently, several mutually blocked local markets have been emerging under the protection of the local governments through various unpublished local policies and regulations.

Another serious concern of foreign investors is the well-known divergence between the active legislation and inactive enforcement concerning intellectual rights protection. In a word, law making does not inevitably lead to enforcement.¹⁸⁹ Transnational companies, relying on their importance in upgrading China's technologies, increasing local revenue, alleviating local unemployment, etc., can relatively easily deal with the difficult problems they encounter by direct communication with central or local government organisations concerning external economic exchanges; but the small and medium-sized foreign-investment enterprises usually lack this ability. The problems accumulated over the past two decades cannot be solved in a short time. The gradual adoption of WTO rules can facilitate the reformation of a unified economic legal system and national market.

¹⁸⁸ The National People's Congress and its standing committee have enacted 390 laws and decisions concerning laws. The State Council has enacted more than 800 administrative regulations, and the provincial people's congresses have enacted 8,000 local laws and regulations. More than 140 laws and regulations need to be revised and more than 570 laws and regulations will be abolished. NCNA, 4 March, 2001.

¹⁸⁹ China is a party to the following multilateral agreements: Paris Convention for the Protection of Industrial Property (Stockholm Act, 1967), Patent Cooperation Treaty, Budapest Treaty on the International Recognition of the Deposit of Micro-organisms for Purposes of Registration of Trademarks, Nice Agreement concerning the International Classification of Goods and Services for the Purposes of the Registration of Trademarks (Geneva Act, 1977), Madrid Agreement concerning the International Registration of Trademarks (Stockholm Act, 1967), Berne Convention for the Protection of Literary and Artistic Works (Paris Act, 1971), Geneva Convention for the Protection of Producers of Phonograms, Washington Treaty on IP in respect of Integrated Circuits (signed, not ratified; treaty not in force).

Despite these problems, foreign investment continues to flow into China, currently accounting for about 80% of total foreign investments in Asian countries (not including Japan). The chief reasons for this are competition between foreign investors and the expected potential of the market size after China's accession to the WTO. Undoubtedly, various preferential policies for foreign-investment enterprises remain the principal policy instrument for attracting foreign investments.

However, as analysed in the former sections, China's various tariff and non-tariff measures to encourage the replacement of imports by domestic products has in fact led to many companies concluding that the sole way to gain real access to the Chinese market is to have a foot in the door, and the earlier the better. The demand to achieve economies of scale and to meet the requirement of maintaining a balance of foreign earnings may compel many foreign investors to export their products. The relatively good infrastructure and industrial facilities and, perhaps most importantly, the low labour costs provide advantageous conditions for manufacturing exported products. Many foreign-investment enterprises have changed (or partly changed) their original goal of pursuing immediate market access and began to make use of these advantageous conditions to manufacture for export. The pursuit of real market access is becoming a matter of future.

What role has the process of China's accession to the WTO played in reforming China's external economic institutions? The positive role played by this process is mainly demonstrated by reduction in import tariff levels. However, its role in removing the non-tariff trade barriers has so far been definitely marginal, although increasingly obvious, despite the fact that China accepts the principle of reciprocity, trade liberalisation, the replacement of government administration with market mechanisms, anti-dumping and anti-subsidies. China also benefits from special arrangements for less developed countries, such as protection of infant industries, measures designed to stimulate the trade balance, some restrictions on foreign investment in services sectors, etc. Perhaps because that China has not been a member of the WTO and after its accession to this organisation it will go through a transition period, it has greater autonomy than other WTO members. However, for the long-term interests of both China and its foreign investors, the compliance to WTO principles and rules is the sole choice, for this can further promote foreign companies to invest in China and retain foreign investments there.

China's external economic policy framework has evolved over two decades, and the evolution is still approximating to WTO rules. After accession to the WTO, the Chinese government has to pursue a balance between fulfilment of WTO requirements and maximisation of the

benefits. For the Chinese leadership, compliance with the liberal international trade regime can currently only be subject to the imperatives of maintaining economic growth and social stability. In the difficult and long-term transition period, it is to be expected that the compliance with the WTO rules, both in legislation and in practice, will be a long-term and difficult process. China must build up a new legal institutional system according to WTO rules and principles, but how fast it can attain this objective is foreseeable.

In the process of accession to the WTO, the Chinese government fully makes use of the external pressure to promote market-oriented reforms through partial compliance with WTO requirements. The obligation to fulfil WTO requirements has provided extra dynamics to break the frustrations from interests of sectors dominated by state-owned enterprises and represented by some governmental organisations. It also legitimises the central government's endeavours to establish uniform national institutions concerning foreign economic exchanges and to re-establish a unified internal market of scale.

This study has also demonstrated the role a strong state can play in controlling the process of integration into the world economy. China is pursuing a strategy of partial integration into the world economy, both to promote economic growth and to avoid excess dependence on foreign trade and investments. It also increasingly seeks to develop foreign economic exchanges to the task of solving domestic socio-economic issues. While the role of the state has shifted from commanding to 'macro guidance, active adjustments and control' (*hongguan zhidao he jiji tiaokong*), it is still influential and strong.

It can be concluded that China's external economic institutions are evolving to a hybrid of centrally-planned and market economic systems. It seeks to retain some effective administrative managing/controlling policy instruments, to produce incentives and apply pressure on enterprises through market mechanism, to devolve onto the local governments some powers of policy formulation and implementation in order to provide incentives, to promote exports by various preferential and efficient policies, to control imports by tariff and non-tariff measures, and to liberalise foreign-investment regime in order to facilitate the attaining of extensive domestic objectives. China's policies towards the EC/EU have been conducted in this context. More concretely, they represent the application of China's foreign-investment, export-promotion and implicit import-substitution policies in the special case of the EC/EU; however, due to the special importance of the European factor in China's domestic developments, these policies have different emphases and undergo some adjustments in different Chinese contexts and different periods.

IV. China's External Economic Policy Operations in the Case of the EC/EU

1 The European factor in Chinese external economic relations, a creature of historical evolution

From the foundation of the PRC to the end of the 1960s, trade constituted the sole contact between China and most Western European countries, serving as China's principal policy instrument available to exert marginal influence upon the policies of Western European countries towards China. However, the use of trade as political instrument and the pursuit of economic profits were not absolutely separated. In most cases they were connected together. This was demonstrated particularly in the trade with advanced Western countries. International constraints (mainly the relations between China and the former Soviet Union and the relations between China and the USA) constituted the principal factors influencing the economic exchanges between China and Western European countries, but in a particular period, domestic factors could not be ignored, as indicated by the re-emphasis of the principle of self-reliance after the mid-1960s and the adverse impact of the Cultural Revolution.

Before the establishment of the official relationship between China and the EC/EU, the change in the economic relations between China and Western European countries could be roughly divided into three periods, marked by the special relationships between China and the Soviet Union in the 1950s, the rupture between them in the early 1960s and China's Western-oriented international strategy in the 1970s. In the first period, the significance of Western Europe in China's external economic exchanges decreased to a marginal one mainly due to the establishment of the special Sino-Soviet economic relationship on the one hand. Even in this period, China still pursued to enlarge trade with Western European countries. On the other hand, the adverse impact of the Western economic embargo on China could not be overlooked. In the second period, Western Europe regained its importance in Chinese external relations. After Moscow withdrew its technological aid to China in the early 1960s, Beijing had to pursue replacement of the Soviet role with that of the Western European countries in China's technological upgrading. It also sought to promote the bilateral political relations with these countries by strengthening bilateral economic exchanges. But the domestic political developments in this period gradually became the principal constraints on the development of the bilateral economic relations. In this period, Western European policies to promote the

détente between the two blocs – ‘change through contacts’ – also extended to China. Consequently, there appeared a short-term boom in the bilateral trade. In the third period, Beijing’s Western-oriented international strategy as well as the *de facto* orientation towards Western Europe in operation of this strategy brought about the key important role played by Western Europe in promoting Chinese technological upgrading.

1.1 The special Soviet-Sino economic relations

The pursuit of obtaining Soviet technological and economic aid was one of the principal objectives for Beijing to establish special relationship with Moscow. The special Soviet-Sino economic relationship, mainly realised through Soviet technological aid, aimed at building a relatively comprehensive industrial system in China. Such a donor-recipient relationship greatly reduced China’s dependence on the West in advanced technologies.

China’s involvement in the Korean War fully demonstrated its bloc identity and its role in promoting the interests of the Communist camp. In turn Moscow decided to take further measures to strengthen the bilateral economic exchanges and to increase its aid on a large scale. In 1952, Moscow initially invited Beijing to send a delegation headed by the Chinese Premier to discuss the concrete programmes to realise Soviet technological aid. Stalin promised that Soviet-aided projects would be of first-class technology but low in price, and hoped that with Soviet aid China should have the capacity to produce automobiles, planes and warships after having implemented the first Five-Year Plan (FYP).¹⁹⁰

The individual planned projects of the whole Soviet technological aid programme in the 1950s were worked out in long-term conscientious discussions between the Chinese delegation and the Soviet experts. This programme as a whole, applauded by the Chinese, ‘completely demonstrates the spirit of an all-sided and overall aid to China and fully satisfies China’s needs in this period’.¹⁹¹ In the 1950s, the Soviet Union aided China with 141 projects. Between 1954 and 1963 it provided China with over 24,000 complete sets of scientific-technical documents, including 1,400 designs for major enterprises. Other measures included personnel training and the organisation of a national scientific and technological research system according to the Soviet model.¹⁹² With Soviet aid, in a short period China established

¹⁹⁰ Chen Zhilin, ‘Wushi nianda shulian dui zhongguo de jingji jishu yuanzhu (Soviet economic and technological aid to China in the 1950s)’ in *Zhonggong dangshi ziliao (Materials of the History of the Chinese Communist Party)*, No. 43, p. 170.

¹⁹¹ *Ibid.*, pp. 186-187.

¹⁹² For details of these programmes, see Lowell Dittmer, *Sino-Soviet Normalization and Its International Implications, 1945-1990*, pp. 18-21.

a relatively comprehensive industrial system, particularly in heavy and defence-related industries, including whole branches of industry that had never existed in China, such as the aviation and automobile industries.

1.2 The shift in the status of Western Europe in China's external economic relations in the period from the 1950s to the 1960s

The bloc identity had been clearly demonstrated in China's foreign trade policy even before the establishment of the special Sino-Soviet relationship. The CCP documents concerning the foreign trade of February 1949 highlighted that the primary goal of China's foreign trade was to satisfy the demands and interests of the Communist countries, and the trade with the capitalist countries could be taken into account only thereafter.¹⁹³ The detailed instruction to realise this policy principle further specified that no strategic materials could be exported to capitalist countries; only non-strategic materials, after having satisfied the demand of the Soviet Union and other new socialist states, could be considered for export to other countries.¹⁹⁴ Although part of these restrictions were removed or relaxed later, the prohibition of exporting strategic materials to capitalist countries was retained till the 1970s. These restrictions greatly changed the traditional composition of Chinese exports to Western European countries, limited China's export capability and had long-term detrimental influences on Chinese foreign trade.

With the transfer of the trade orientation from the West to the Soviet Union and other Eastern European countries, China's trade with non-socialist countries reduced from 74 percent in 1950 to 37 percent in 1951, and further declined to 18 percent in 1955. Correspondingly, the trade with the Soviet Union and other Eastern European countries increased from 33.5 percent in 1950 to 63.3 percent in 1951, and further increased to 82 percent in 1955.¹⁹⁵

In the 1960s, due to the rupture between China and the Soviet Union with the consequence of the Soviet withdrawal of its economic and technological aid, the Chinese government decided to turn its trade orientation towards the Western industrial countries, mainly Western European countries. In 1962-1963, the Chinese leadership decided to import 14 plants so as to enhance the technological level in some industry sectors. These complete plants, which were

¹⁹³ Central Committee of the CCP, 'duiwai maoyi de jue ding (Decision concerning Foreign Trade), February 16, 1949' and 'duiwai maoyi fangzhen wenti de zhishi (Directions on Foreign Trade Principle) February 16, 1949' in *Zhonggong Dangshi Ziliao (Material of the History of the CCP)*, No. 47, pp. 1-5.

¹⁹⁴ The list of products prohibited to be exported to capitalist countries included the principal Chinese exported mineral products, for instance, tungsten and tin. *Zhonggong Dangshi Ziliao*, No. 47, p. 32.

¹⁹⁵ Mah Feng-hwa, *The Foreign Trade of Mainland China*, p. 686, Table 5.

planned to be imported mainly from Western Europe, would greatly enhance China's technical level in the chemical industry, electric/electronic industry, oil, metallurgy and mining.¹⁹⁶ However, further Chinese efforts became abortive mainly due to the increasingly domestic radical leftist tendency and the outbreak of the Cultural Revolution in 1966. Consequently, the principle of self-reliance was interpreted as autarky in policy practice. From the mid-1960s to 1972 China did not pursue any large technological importation from Western Europe and other advanced countries.

Traditionally, Britain and Germany had been two major machinery and equipment suppliers for Chinese industry, which led to Chinese partiality for manufactured goods from them. Although Soviet technological aid greatly reduced their importance in the 1950s, China still sought to import machinery and industrial equipment from some Western European countries which the East Bloc countries could not supply. In the case of Britain, the export of raw materials and manufactured articles to China maintained an increasing tendency after 1953.¹⁹⁷ In Britain there existed a strong pro-China interest group among the British businessmen who had long engaged in trade with China. They were soon involved in the newly established organisation for trade with the Eastern bloc (the British Council for the Promotion of International Trade). The establishment of diplomatic relations between China and Britain at the level of charge d'affaires in 1954 contributed to promoting bilateral trade. Bilateral trade in 1954 accounted for US\$ 44 million, amounting to 1.8 percent of China's foreign trade, but in 1959 it increased to US\$ 124 million, amounting to 2.9 percent of China's foreign trade. In 1964 it decreased a little and accounted for US\$ 119 million, but amounted to 3.6 percent of China's foreign trade.¹⁹⁸

On the issue of the embargo on the PRC after its direct involvement in the Korean War, British policy indicated the dilemma from the outset. It imposed even more severe controls on the exported items to the PRC. In addition to the lists of normal embargoed commodities, the British government added 48 items of commodities prohibited to be exported to China. The Chinese controls were much wider than the Soviet bloc controls and a large number of goods (some 296 items) could be sent to Eastern Europe but were prohibited for export to China (China Differential).¹⁹⁹ However, it disapproved the entire embargo policy advocated and adopted by the American administration; and in 1958 London decided to remove unilaterally

¹⁹⁶ Zhao Dexing, *Zhonghua Renmin Gongheguo Jingji Shi (The History of the Economy of the People's Republic of China), 1949-1966*, He'nan, 1988, p. 711.

¹⁹⁷ Shao Wenguang, *China, Britain and Businessmen, Political and Commercial Relations 1949-57*, p. 65, table 2.

¹⁹⁸ Mah Feng-hwa, p. 689.

¹⁹⁹ Shao Wenguang, pp. 101-2.

the China Differential. It was followed by Belgium, Denmark, France, Japan, and the Netherlands.

France voted for and adhered to the United Nations embargo instituted in May 1951 and participated in the International Co-ordinating Committee on Strategic Trade with Communist Countries. Its control list for the PRC was larger than the list for the USSR. In 1958, it followed the British example and applied the same restrictions on the export of strategic goods to the PRC as were applied to the USSR and Eastern European countries. The bilateral trade between China and France during the 1950s remained at a relatively low level, accounting for US\$ 9 million in 1950, and in 1954 increased to US\$ 18 million, only amounting to 0.7 percent of China's foreign trade. In 1959 it increased to US\$ 56 million, amounting to 1.3 percent of China's foreign trade.²⁰⁰

The establishment of a diplomatic relationship with the PRC in 1964 did not immediately bring a French preference in China's foreign economic relations, although this was an objective of the French initiative in establishing the diplomatic relationship with China. In 1964 the bilateral trade accounted for US\$ 81 million, amounting to 2.4 percent of China's foreign trade.²⁰¹ The composition of its exports to China was an unfavourable factor for expanding the bilateral trade. Throughout the 1960s, despite the increase in the sale of industrial goods, its exports to China were primarily composed of agricultural products. The Chinese plan of increasing imports of manufactures and purchasing complete plants was suspended due to the outbreak of the Cultural Revolution in 1966.

Compared with Britain and France, China's relationship with West Germany was always confined to the bilateral economic exchanges. Two factors facilitated its status in China's external economic relations. China's traditional partiality for German manufactures had been fostered since the early 1930s when Chinese students returning from Germany came to play an important role in establishing China's modern mechanical engineering and chemical industries. In addition, in Chinese import from West Germany, chemicals, machinery and equipment, and other industrial materials accounted for more than ninety percent. Early in 1954 West Germany had become China's first trade partner in Western Europe. In 1964 China began to import plants from Germany. The setback in Beijing's effort to conclude an intergovernmental trade agreement with Bonn in 1964 did not significantly affect China's trade with West Germany.

A particularly important European role in China's external economic relations was forged by European export policies towards China in the 1950s and the 1960s with the following

²⁰⁰ Mah Feng-hwa, pp. 688-689.

²⁰¹ Mah Feng-hwa, p. 689.

features. They were less linked to ‘strategic concerns’ and the European countries were reluctant to be restricted by the American-advocated sanctions against China; and the exports concentrated on equipment of appropriate and civil technologies that China needed.

1.3 The trade between China and Western Europe in the 1970s

After 1972, Beijing managed to amply import industrial equipment and complete plants from Western European countries. The industrial and technological exhibitions held by France, Britain and West Germany in Beijing in the early 1970s were visited by some prominent government leaders, including Premier Zhou, and thousands of managers and engineers from various industrial sectors. Having established diplomatic relations with most of Western European states, the importance of trade as a policy instrument actually decreased. Comparable commercial conditions instead of political considerations became increasingly important in Chinese foreign trade practices. In this period, Western Europe played the principal role in upgrading China’s technologies. China began to combine technology transfer with the import of complete plants as well as key equipment that China could not manufacture. In order to eliminate the ideological impediment to the new technology-import programme, the moderate faction within the central leadership redefined the concept of self-reliance. Self-reliance now meant commanding the national economic lifelines mainly depending on the people’s abilities and wisdom. Under the precondition of respecting state sovereignty, mutual equality and mutual benefit, technological exchange with the outside world was not only necessary but also beneficial to the development of the national economy.²⁰² In short, the importation of technologies from the advanced countries was not in conflict with the principle of self-reliance but strengthened the capacities of self-reliance. Such a redefinition revealed that the moderate faction sought to transform the Western-oriented international strategy into concrete policies for attaining domestic goals, namely that in applying this strategy one principal goal was to strengthen the technological imports from the Western industrial countries in order to pursue technological progress.

The programme to accelerate economic growth formulated in 1973 by some Chinese leaders of the moderate faction demanded that the importing of advanced technologies be accelerated. It also demanded that leaders of every industrial sector know the advanced technological levels in the world, and make plans and adopt concrete measures for catching up with them. Concerning the financing of large scale importation, it proposed that the balance of exports

²⁰² Deng Xiaoping’s speech in the UN Assembly, 10. April, 1974. *People’s Daily*, 11 April, 1974.

and imports could be maintained by exporting coal and oil to Western Europe and Japan.²⁰³ These ideas were unusual and abnormal in the special context of the Cultural Revolution when self-reliance had been transformed into autarky.

In the mid-1970s, the effort in this respect was again frustrated by the intensifying factional conflict within the central leadership, and the effort of the moderate faction to increase technological imports from Western advanced countries was severely criticised by the radical leftist faction. This faction claimed that the large-scale technological imports were contrary to the doctrine of self-reliance.

This conflict was related to which faction would assume the leadership of China after Mao's death. For Mao, self-reliance implied minimising China's dependence on the outside world. Despite the fact that he had previously approved to strengthen the economic exchanges with the West, it was questionable that he still supported the moderate faction's efforts in this respect in the period between 1975 and 1976 when the transfer of power had become the critical issue in Chinese politics. As a tactical politician, he managed to maintain a delicate balance between the two factions and could therefore play the monopoly part of final adjudicator at all times and on all important issues. A series of campaigns motivated by him in the period from 1973 to 1976 tended to weaken the strengthened moderate faction. The consequence of this struggle was the temporary failure of the moderate faction, indicated by the fact that Deng Xiaoping was deprived of his power and position in the Party in 1976. One demonstration of the adverse consequences of the factional struggles in China's economic exchanges with the West was the breaking-off of the negotiations for concluding a trade agreement between China and the EC by the unilateral withdrawal of the Chinese delegation from the negotiations in 1976.²⁰⁴ But the frustration was short-lived and not significant because of the end of the Cultural Revolution with the death of Mao in the same year.

Two factors were decisive in enhancing the status of Western Europe in China's external economic relations in this period. First, compared with that of the United States, the control of the technological exports of Western European countries was much looser; and second, the improved political relationship between China and the West, the operations of West-oriented international strategy and the increasing importance of China in international politics in the 1970s facilitated the technology transfer from Western European countries to China. Undoubtedly, whether the American administration would have liked to close its eyes or not was also important, but American control over the Western European governments in this respect had undergone a decline.

²⁰³ *Dalu Zhongguo Yanjiu (Mainland China Studies, the former Feiqing Yuebao)*, Taipeih, 5. 1977, p. 82.

²⁰⁴ Kapur (1985), p. 39.

The bilateral economic exchanges between China and the EC made some further advances during this period, and in most years the balance of trade was in the EC's favour.²⁰⁵ In 1973, China imported 13 chemical fertiliser plants, four giant chemical fibre mills, three petroleum chemical industrial works, forty-three sets of coal combines, three giant power stations and a 1.7 meter rolling machine.²⁰⁶ The three petrochemical works were established in the coastal provinces for easy access to raw oil supplies. This arrangement provided advantageous conditions for investment from Western European chemical enterprises in these coastal provinces in the 1990s.

Compared to the frustrations from the short-lived factional conflicts within the Chinese leadership, the composition of Chinese exports with the bulk of primary products constituted the main long-term constraint on developing trade with the EC.²⁰⁷ In Chinese exports to the EC in 1978, products of animal origin accounted for 28 percent, silk and waste silk 26 percent, meat and edible meat offal 17 percent, man-made fibres (discontinuous) 16.6 percent, and wool and other animal hair 12.4 percent.²⁰⁸

In the early 1970s most of China's imports from the EC were composed of industrial equipment and manufactured products, such as heavy machinery, precision instruments, precious pearls and semi-precious stones, etc.²⁰⁹ By contrast, in 1973, 69 percent of China's importation from America was agricultural products and in 1974, 58 percent.²¹⁰ Western Europe therefore enjoyed an unusual position in Chinese development strategy focusing on technological progress. Such a status was enhanced in contrast to the United States in China's external economic relations.²¹¹

In summary, in the period from the 1950s to the 1970s the external economic exchanges were generally subject to China's international strategy. Despite the fact that trade was used as policy instrument to attain explicit political goals, the pursuit of technological progress through import of complete plants and advanced equipment was always a principal objective of China's external relations. Such a policy operation in turn promoted the importance of

²⁰⁵ Kapur, (1985) p. 42, Table 2.5.

²⁰⁶ Alexander Eckstein, 'China's trade policies', *Foreign Affairs*, No. 1, 1975.

²⁰⁷ Taking the example of Chinese export composition in 1978, industrial and mineral products accounted for 37.4 percent, agricultural and sideline products (processed) 35 percent and agricultural and sideline products (raw) 27.6 percent. in Kapur (1986), p. 66, table 3:6.

²⁰⁸ Calculated by the author according to Table 3:4 Principal items of Chinese exports to EEC, in Kapur (1986), p.65.

²⁰⁹ Kapur (1986), pp. 65-66, Table 3.5.

²¹⁰ Harry Harding, p. 366, Table A-4.

²¹¹ The bilateral trade between China and the United States accounted for US\$ 92.4 million in 1972, in 1973 it increased to \$752.6 million and in 1974 further to \$921.1 million. However, the Chinese deficit in 1973 accounted for \$625.6 million and in 1974 increased to \$692.5 million. The large trade deficit compelled the Chinese government to cease the import of agricultural products from America in 1975 and 1976 in order to reduce the deficit. in Harry Harding, p. 364, Table A-2.

Western Europe in China's external economic relations. Western European countries also adopted relatively loose trade policies towards China. In this context, the 'European factor in China's domestic development' emerged, namely a unique European importance in Chinese efforts to promote industrial technological upgrading, particularly in the traditional industries. In the new Chinese domestic context after the Cultural Revolution and in terms of the new foreign policy principle, namely to accelerate economic growth through integration in the world economy and to concentrate resources on economic development by avoiding involvement in any international conflicts, the 'European factor' in China's external relations, represented by the role played by the EC/EU, can be partly explained in political economic terms. It has not the nature of 'hegemony', as that of the United States, and strengthening the economic exchanges with it contributes to China's implicit intentions to reduce dependence on any single economic power.²¹² However, such a strategic consideration has been gradually replaced by the requirements to cope with more important domestic socio-economic issues in the difficult transition period, and become closely linked to the domestic industrial policies and regional policies. The European factor was first indicated in the bilateral trade agreement of 1978, in which China agreed to give favourable consideration in the imports from the EC, and would see to it that Community exporters had the possibility of participating fully in opportunities for trade with China.²¹³

2 China's external economic policy operations in the case of the EC/EU in the context of the Open Policy

China's policy operations towards the EC/EU have been still conducted within its general external economic policy framework. Leaving aside the fact that external economic policies are the main and most efficient policy instruments of the EC/EU towards the third countries, the shift in the principal goal of China's foreign policy strategy from the ensuring of external security to the pursuit of maximum economic benefits dictates that China's policies towards the EC/EU mainly contribute to economic development. In the new Chinese context of the Open Policy, the 'European factor' is indicated in three aspects: the importance of the EC/EU as one of the principal target market of export promotion, the role played by the EC/EU in Chinese efforts to upgrade technologies, and the increasingly important parts played by the European investment enterprises in alleviating domestic socio-economic pressure in the 1990s.

²¹² See also chapter II, 5. pp. 46-49.

²¹³ Trade Agreement between the European Economic Community and the People's Republic of China, 1978, article 4; in Kapur (1986), p. 160.

The policy operations aimed at bringing the European factor into full play in order to promote domestic developments. The policies to attain these three goals are combined together, but for convenience of analysis, they will be individually dealt with.

2.1 Export-promotion policies in the case of the EC/EU

As analysed previously, China's export promotion policies through foreign trade institutional reforms brought about striking foreign trade growth. Such a growth also appeared in China's trade with the EC/EU.²¹⁴ After 1988, there always existed a trade deficit in the EU's trade with China. In the period 1981 to 2001, export from the EC/EU to China increased about fifteen-fold, but the import from China increased about thirty-two-fold, obviously higher than the export.

The actual importance of the trade with China also underwent unparalleled changes. The percentage of the export of the EC/EU to China in its total export increased from 1.7 percent in 1985 to 2.4 percent in 1996, but its import from China in the same period increased from 1.0 percent to 5.2 percent in total extra-EU import.

The differentiated preferences of the commercial policies of the EC/EU towards its trade partners and the demand to protect its declining industries, the labour-intensive industries in particular, made it difficult for some Chinese products to enter the European market, despite the fact that the EC/EU gradually reduced the quantitative restrictions on the imports of Chinese manufactures in the 1980s and the 1990s to fulfil its commitments to decrease non-tariff barriers. In addition, many Chinese labour-intensive products not only threaten some European industries, but also constitute increasing competition with other developing countries. For this reason, the principal Chinese export-promotion efforts concentrate on increasing the percentage of the high value-added (normally also technology-intensive) manufactures, the mechanical and electric/electronic products in particular. The composition of European imports from China, with the increase in processed and diversified products,

²¹⁴ There is a difference between Chinese and EU statistics due to different statistical approaches. According to Chinese statistics, the EU's deficit in the trade with China first appeared in 1996. But according to EU's statistics, the deficit appeared in 1988. The difference is due to the fact that the EU's statistics include transshipments of goods passing through Hong Kong. It is possible that each of the two parties sought to increase its leverage through statistical cheating.

	China's trade with the EC/EU						
	million US\$ (selected years)						
	1985	1987	1991	1993	1995	1996	1997
export	2384	3892	6739	11693	19258	19886	23865
import	6700	7261	8402	14415	21313	19883	19205
balance	-4316	-3368	-1663	-2718	-2055	3	4660

Calculated by the author according to *Zhongguo Tongji Lianjian (Yearbook of Chinese Statistics)*, various years.

seems to show the success in this respect. In 2000, over one-third of these were products of electric/electronic and mechanical engineering industries, followed by games and toys (8.4%), clothing accessories (6%), leather goods (4%), electric/electronic equipment (3.7%), plastics (3.6%) and optical instruments (3.2%).²¹⁵

Various preferential export-promoting policies and measures, the granting of the export right to more entities (trade companies, enterprises, institutes, etc) and the launch of bidding for export quotas facilitate attaining the goals both to fully utilise the quotas and to increase the export of other products without quantitative restrictions. These measures adopted in the latter part of the 1990s to remove the controls on exporters were, to a large extent, to rapidly promote Chinese exports in order to alleviate the difficulties in industrial restructuring. Such difficulties are particularly demonstrated by the dilemma that most manufacturing sectors have surplus capacity of production but domestic market is limited. After the launching of process of the negotiations for the accession to the WTO, China seemed to obtain a more favourable external environment for the operation of its export-promotion policies. Its major trade partners, including the EC/EU, reduced the quantitative restrictions on the imports of some Chinese manufactures in order to exchange China's concessions and to accelerate the negotiation process.

The accession to the world market is one important means to maintain the operation of some Chinese enterprises, which usually belong to the industrial sectors with surplus capacity of production, such as mechanical engineering and consumer electronics. The increase in the exports of mechanical and electronic products to the EC/EU mainly took place in the 1990s. It can be regarded as the result of the combination of preferential policies that sought to promote simultaneously technological upgrading, foreign technological investments, export-composition improvement and market diversification. Various preferential policies to promote exports aim at attainment of the goals that the exported items have competitiveness in prices and the export composition shifts to one mainly made up by high value-added electronic/electric products. The state-owned enterprises play the principal role in promoting Chinese manufactures exports depending on their better capacity in research and development, quality control and better advanced technologies. Most of the competitive technology-intensive products for exports are produced by state-owned enterprises and joint ventures, such as motorcycles, consumer electronics, personal computers, etc. For instance, the Chinese TV set industry first increased its exports to the developing countries, and after gaining better technologies and quality control the TV sets manufactured in China become very competitive

²¹⁵ Eurostat, <http://www.europa.eu.int/comm>

Chinese products in the world market with good quality but at low price. The export of the products made by Chinese TV-set enterprises has also begun to constitute increasing threat to European consumer electronics enterprises and have always been the target of anti-dumping. However, such high value added products only account for a small part in China's exports to the EC. It seems to reveal that the strengthening of the EC's anti-dumping measures against Chinese exported products does not really show the substantial extent of the threat they have constituted to European industries.

As analysed in the former chapter, export-promotion and the replacement of imports by domestic products are two principal goals of Chinese policies to attract foreign investment. The increase in European-investment enterprises in China also contributes to the striking growth of Chinese export to the EC/EU. Most of the European-investment enterprises coming in China in the 1990s are concentrated in the coastal region with the original principal goal of market access. However, some foreign-investment enterprises have transformed, at least partly, the original goal of market access into export processing, taking account only of the requirement that the foreign-investment enterprises must maintain the balance of payments of foreign earnings. More and more investors pursue a strengthening of their competitiveness in the global market by making use of the relatively low labour costs, good production facilities and favourable access to raw materials for export processing, or at least combine the hope of market access (or more concretely to have a foot in China earlier) and export part of their products. For instance, the exports of EU-investment enterprises accounted for US\$ 457 million in 1991, but in 1999 they amounted to US\$ 12.66 billion.²¹⁶ Undoubtedly, for European-investment enterprises, the most familiar market is still Europe. The result was that the percentage of manufactures in the export to the EC/EU in 1998 was 91.7%, obviously higher than the average in China's total exports (80%).²¹⁷

The following statistics indicate that during one decade (1987-97) the export of manufactured products to the EC/EU increased about 3.4-fold but the import from the EC/EU only 1.3-fold. This appears to indicate that the status of the EU in Chinese technological imports is decreasing. But the EU still maintains an important role in China's efforts in restructuring industries and upgrading technology. The extremely high-level European standard requirements in security, environmental protection, durability, etc, compel the Chinese enterprises, at least partly, to change their traditional practices in gaining competitiveness in the international market mainly relying on low prices. They have to strengthen the co-

²¹⁶ <http://www.moftec.gov.cn>

²¹⁷ Zhang Jianhong, 'zhong-ou shangpin maoyi yanjiui' in *Shijie Jingji Yanjiu (The Study of World Economy)*, No. 2, 2000; p. 57.

operations with European partners and make more efforts to combine imports of equipment with technological upgrading. It has always been in planning to improve China's export composition in the case of the EU with the imported equipment, materials, patents and improvement of marketing. In addition, European market mechanism provides extra dynamics accelerating the restructuring of domestic industries and upgrading of technology. For instance, the export of machinery and vehicles to the EC/EU increased 25-fold (from 0.4 billion Ecu to 10 billion Ecu); the manufactured articles about 2-fold (from 2.4 billion Ecu to 4.5 billion Ecu), and chemical products 4.5-fold (from 0.4 billion Ecu to 1.8 billion Ecu). (See table 4. 2)

The following analysis helps to explain the decrease in the EU's exports to China. As early as in the 1980s China changed its policy in technological imports, namely that only key equipment and component parts that China cannot produce rather than complete plants can be permitted to be imported. This was at that time partly as an effort to eliminate the trade deficit. Further steps came to be adopted to combine imports of advanced equipment with technology transfer in order to replace imports of manufactures by domestic products. The domestic technological upgrading in the past two decades, promoted both by the technology transfer of foreign-investment enterprises mainly from the transnational companies and by the policies to enhance domestic technological progress, inevitably decreases the dependence on the imports of some European manufactures. As a result of this, only the advanced equipment that China cannot manufacture has the competitiveness in China and can enter the Chinese market.

The adverse impact of high import tariffs (32% in 1992) on the import of materials, machinery and electrical manufactures from the EC/EU, is difficult to estimate. A large part of the imports belong to the advanced equipment relating to China's technological upgrading, normally that China cannot produce or cannot produce domestically in a volume sufficient to meet the demands. In this case, usually a cutting of import tariffs is applied. In addition, the MFN status of the EC in China's foreign trade means the minimum import tariff rates to be applied. Thus, it can be concluded that non-tariff means are the main barriers to the European exports, namely that most of the imported products from the EC/EU are under administrative control, such as the machinery and electric/electronic products, chemical and petrochemical products. According to Chinese policies in controlling imports of machinery and electronic equipment, only advanced and high-tech equipment is permitted to be imported. Quotas are imposed on those products likely to threaten Chinese enterprises owing to high-volume imports; non-quantitative control is exerted on those that Chinese enterprises cannot produce

or are just beginning to produce, and the purchasing is through open bidding.²¹⁸ In the competition to enter the Chinese market, the European products had some disadvantages. For instance, even though the European products have advantages in technology or quality, their high prices weakened their competitiveness in the Chinese market. Various preferential policies to promote replacement of imports by domestically-manufactured products and to attract foreign-investment enterprises to manufacture in China have led to the result that in the case of most of the imported items, Chinese industries have managed, given appropriate technologies, to replace them with domestic products. In addition, in contrast to the Americans with the help of the overseas Chinese, the European enterprises were relatively less familiar with the 'Chinese market mechanism' and the Chinese local governmental organisations. In the Chinese market mechanism of the current period, personal contacts still play important role in facilitating market access.

Moreover, a high percentage of China's imports is for manufacturing in foreign-investment enterprises. In 1994 about 46 percent of Chinese imports were for manufacturing in foreign-investment enterprises;²¹⁹ the relatively low percentage of European investments in China in the period from the 1980s to the early 1990s was also one factor leading to the decline in exports from the EC/EU to China. For instance, the import of European-investment enterprises accounted for US\$ 7.875 billion, contrast to US\$ 14.2 billion in the case of Japan in 1994. In 1999, the imports of EU-investment enterprises amounted to US\$ 12.5 billion, but still much less than those of Japanese-investment enterprises (US\$ 21.4 billion).²²⁰

Undoubtedly, some European products with international competitiveness, which fall in the category of non-essential items, are subject to high import tariffs, such as cars (currently 80-100 percent), cosmetics (currently 30 percent) and spirits (currently 65 percent). Such high import tariffs on some important European products actually constitute barriers to their entry into the Chinese market and limit the market share. Some foreign-investment enterprises are compelled to invest and produce in China if they hope to obtain real market access. For instance, more and more automobile enterprises have determined to invest in China because of high import tariffs and heavy competition among them.

However, the 'European factor in China's economic development' currently still demonstrates its importance in China's effort to upgrade technologies through technological imports,

²¹⁸ *Jidian chanpin jinkou guanli zhanxing banfa (The provisional measures to administer the import of machinery and electric products)*, 1994.

²¹⁹ Elena Ianchovichina, *et al*, *Assessing the implications of merchandise trade liberalisation in China's accession to WTO*, World Bank, June 23, 2000, Table 2: contribution of different firms to China's trade, 1994, p. 7.

²²⁰ <http://www.moftec.gov.cn>

indicated by the composition of China's imports from the EC with the domination of capital- and technology-intensive commodities. Although the total value of exports from the EC/EU to China is behind Japan and the United States, in China's import of capital- and technology-intensive commodities, the EC has been in second place since the end of the 1970s, only behind Japan (Japanese exports to China have been supported by Japanese government loans). Concerning such products, vehicles, electric/electronic equipment, machinery and mechanical equipment currently made up 60% of the EU's exports to China. Such an export composition reflects China's needs and the EU's comparative technological advantages.

The import composition with the emphasis on machinery and electric/electronic equipment with high technologies that Chinese enterprise cannot employ and the policy of control on import of non-essential commodities inevitably lead to the fact that China's imports are concentrated on a few countries of the EC/EU, mainly France, Germany, Italy, Netherlands and Britain, and even on a few companies which have products with advanced technologies and international competitiveness. For instance, the exports of these five EC member states to China in 1993 accounted for 90 percent (US\$ 12.1 billion) of the total imports from the EC (US\$ 13.4 billion), and among the five countries, the imports from Germany accounted for 50 percent (US\$ 6 billion).²²¹ In 2000, it still accounted for 28 percent.²²²

In addition to the fact that during the period from 1995 to 2001, the total EU trade deficit continued to increase, two trends in the bilateral trade became increasingly obvious. First, thirteen of fifteen EU member states had deficit in their trade with China in this period, including five major Chinese trade partners.²²³ This trend seemed to support the EU to strengthen its commercial defence in the case of China and tend to impose definitive anti-dumping duties in the 1990s, taking account of the EU's decision-making rules in this respect. Second, the share of agricultural products in the bilateral trade continually decreased, 2.8 percent in 2000, as against 4.7 percent in 1995. Between 1995 and 2000, European exports of the agricultural products to China rose by 11.8% per year, whilst European imports of industrial products soared at an average annual rate of 22%.²²⁴ Without changing of export composition, namely, the increasing of the exports of agricultural and some other industrial products by demanding China to reduce its import duties and remove non-tariff restrictions, it is difficult to reverse these two trends. The agreement between China and the EU on China's accession to the WTO seems to reveal the consideration in this respect.

²²¹ Calculated by the author according to *Zhongguo Tongji Nianjian (Yearbook of Chinese Statistics)* 1994.

²²² Eurostat, <http://www.europa.eu.int/comm>

²²³ Eurostat, <http://www.europa.eu.int/comm>

²²⁴ Eurostat, <http://www.europa.eu.int/comm>

In the agreement concerning China's accession in the WTO, China agrees to substantially reduce import tariffs on over 150 leading European exports – machinery, ceramics and glass, textiles, clothing, footwear and leather goods, cosmetics, wines and spirits. Agreed tariffs are down to 8-10%.²²⁵ The increase in the export of these products represents the extensive European sectoral interests, and might bring about some positive impact in changing the adverse situation that China's imports from the EU concentrate on a few EC/EU member states and on technology- and capital-intensive manufactures. The reduction in import tariffs on these European products might facilitate promoting European exports to China by changing export composition through an increase in exports of non-essential and agricultural products. For instance, China agrees to gradually cut the import tariff of cars down to 25% by 2005. But China rejected EU demands for car import tariffs lower than the reduction offered to Washington.²²⁶

2.2 The policy operations to attract investments from the EC/EU

The importance of Western Europe in Chinese external economic relations in the new Chinese context of the Open Policy can only be estimated by comparison with other principal Chinese economic partners, namely the overseas Chinese, Japan and the United States, now that foreign investments in manufacturing have become the principal means for China to obtain advanced and appropriate technologies.

As analysed in the former chapter, the overseas-Chinese-investment enterprises only played marginal role in Chinese technological upgrading. In fact, the flux of such overseas-Chinese-investment enterprises in China means the transfer of the declining industries to China. This facilitates restructuring the industries in the NICs in Asia. More concretely, when China received the transfer of these declining labour-intensive export-processing industries, the NICs turned back to receive the transfer of part of the Japanese capital- and technology-intensive industries. Consequently, in the new integrated Eastern Asian regional economic structure, China appears to depend further on labour-intensive manufacturing investments in order to maintain its economic growth.

However, the competitiveness of Chinese labour-intensive manufactures in the world market mainly relies on their low prices. This is facilitated by low labour costs and various preferential export-promotion policies towards foreign-investment enterprises for export

²²⁵ European Trade Commissioner Pascal Lamy's Declaration on China's WTO accession, <http://europa.eu.int/comm/trade/bilateral/china/prc.htm>

²²⁶ Financial Times, May 20, 2000.

processing. Any developing country can adopt same or similar policies to attract foreign-investment enterprises in order to produce low-price manufactures. In addition, the similarity between the export composition of China and other developing countries with labour-intensive manufactures such as textile products, footwear and toys as the bulk of exports means Chinese labour-intensive manufactures will meet increasing competition in the world market.

The foreign-investment enterprises from advanced countries, namely Japan and America, played an important role in upgrading Chinese manufacturing. The investment from these two countries separately accounted for 7.6 and 8.2 percent in the period from 1979 to 1994, but a large part was in non-manufacturing sectors, such as hotels and restaurants. Japanese enterprises have been transferring some traditional capital- and technology-intensive sectors in manufacturing to other countries with low labour costs and available resources. The positive part played by Japanese-investment enterprises in developing China's consumer-electronics sector can never be underestimated. Through technological imports and innovation China has established a consumer-electronics sector with international competitiveness.

The investment from the EU accounted for only 2 percent of Chinese total foreign investment by 1994, but was concentrated on manufacturing sectors. Normally, the capital volume of each investment project represents its technological contents. The following statistics appeared to reveal the differences in this respect between the investments from Japan, America and some EC member states. In the period between 1979 and 1992, the average capital volume of each investment project was US\$ 1.64 million for Japan, US\$ 1.49 million for America, US\$ 3.82 million for Britain, US\$ 2.83 million for France, and US\$ 4.86 million for Germany.²²⁷ Obviously, the average technological contents of the investment projects from these three EC countries were much higher than that of Japanese and American investment projects. In 1999, the EU-investment projects accounted for 5.28 percent of Chinese total foreign-investment projects, but the capital volume (utilised) accounted for 11.11 percent of the total volume (utilised) of foreign investments. In contrast, the Japanese-investment projects accounted for 6.90 percent, but the capital volume accounted only for 7.37 percent. In the case of America, the projects accounted for 11.99 percent, but the capital volume only 10.46 percent.²²⁸ Thus, it can be concluded that European investments concentrate on high technologies.

Maintaining an average share of Chinese trade with its three principal trade partners (Japan, the United States and the EC/EU) was considered as a means to decrease the dependence on

²²⁷ MOFTEC.

²²⁸ <http://www.moftec.gov.cn>

any of them, as analysed before.²²⁹ In the case of attracting foreign investment, a similar consideration also exists. But it later becomes more subject to the demands from the changing domestic settings and domestic objectives.

As analysed in the previous chapter, foreign investment, joint venture in particular, is the principal approach for China to upgrade technology and improve marketing. Local sourcing and/or technology transfer, export performance and maintaining payment balance of foreign exchange are the conditions for permitting foreign direct investments. These three basic requirements are not attractive to the European investors with the principal goal of market access. By the end of the 1990s China's success in attracting European investments was limited, indicated by the fact that despite rapid increase, the investment from the EU member states was only half as much as that from Japan and the United States.

By 1993 only 2 percent of China's total foreign investments were from the EC. Despite the low percentage of European investment in Chinese total foreign investment, it was highly appreciated by the Chinese. Most European investors concentrated their investments, with the character of large average investment capital volume and high technological content, on Chinese preferred projects and on manufacturing. And it is a prevalent view that the European investors are more willing to transfer technologies, compared with Japanese investors,²³⁰ and European-investment enterprises usually have good outcomes. When foreign investments begin to play an increasingly important role in attaining some socio-economic objectives in this transition period, any foreign investments facilitating the attainment of these objectives are welcome. However, concerning some important industrial sectors and strategic projects, technology transfer and the concern of external dependence are two crucial factors in determining the acceptance of foreign investments and the forming of economic partnerships. For these reasons, the European-investment enterprises are always welcome.

In the adjustments of foreign-investment policies, it is likely that the Chinese government has also taken it into account that the 'European factor' should play a more important role in this transition period and in the pursuit of sustainable development, in particular in restructuring state-owned enterprises in some traditional and important sectors.²³¹ On the one hand, the

²²⁹ See chapter II, 5. pp. 46-49.

²³⁰ David Bennett, *et al*, prepared for European Commission Directorate General I, China and European Economic Security: Study on medium to long term impact of technology transfer to China, 1999.

²³¹ For instance, Chinese government specially agrees to raise the local ceiling of foreign investment in the automobile industry from US\$ 30 million to \$150 million in the agreement with the EU on China's accession to the WTO and has removed some other restrictions. Chinese government accelerates the process to organise three or largest automobile enterprise groups with the capacity of research and development, co-operating with foreign investors to sustain the impact on this industry after the participation in the WTO. Such a change of policies to win large foreign investment in automobile should facilitate restructuring Chinese automobile industry. Volkswagen's investment in Shanghai and in Changchun is only one case.

Chinese government is eager to guide foreign investments to the inland regions and state-owned enterprises; on the other hand, as late-comers, the European investors are eager to enter China in order not to lag behind in the competition with Japanese and American investors.

Undoubtedly, the inland-development programmes can also be regarded as part of practice of the strategy to maintain high economic growth through enlargement of domestic demand, and new foreign-investment policies are not European oriented. However, taking into account of some factors favourable to the EU, these policies and programmes might have long-term positive influences on the imports and investments from Europe. Facing increasing trade imbalance between the EU and China, Chinese government must increase imports from the EU in order to fulfil its obligations. As usual, such an increase in imports might be oriented to some target projects, namely the preferred projects have priority to import material and equipment they need. Currently, the launched projects are concentrated on energy supplying, the building of electric power stations, transport communications, telecommunication, the building and reforming of railways, etc. Meanwhile, the inland-development programmes stress more preferential policies towards foreign investments in services sectors and environmental protection projects, etc. In these aspects, European industrial enterprises have technological advantages.

In some new civil technologies, such as the environmental protection technologies, agricultural products processing, and transport and communication, the European industries have particular competitiveness. These technologies are what the Chinese currently are eager to develop in order to maintain sustainable economic development, in particular for accelerating economic growth in the inland regions.

It is not unreasonable to conclude, that opening more branches of services sectors for foreign investments, tourism and insurance in particular, and the opening of more traditional and strategic industries in the latter part of the 1990s promoted European investments in this period. The inland development programme with comprehensive projects to improve infrastructure facilities, restructure traditional industries, import agricultural processing and environmental protection technologies might provide better chances for European investors, as late comers, to expand their investments in the newly opened sectors and new regions.²³²

This inland development programme as well as the new measures and policies to realise this programme seems to be of importance for the EC/EU, both in increasing its exports to and in

²³² The branches of services, according to Chinese planning, will become the main sectors to increase employment, achieving 33 percent of the total employment in the period from 2001 to 2005. Only relying on domestic resources it is difficult to attain this goal.

European investments in China. Most of the sectors opened to foreign investments are those with European competitiveness. In addition, as indicated by the experience gained in the coastal regions, foreign investments in services, in particular banking and insurance, can promote foreign investments in manufacturing. For some regions, the development of tourism and agricultural processing is the sole means to accelerate local economic growth. In these aspects, the Europeans have managerial and technological know-how.

It is better to replace the term ‘advanced technology’ with ‘appropriate technology’ in the case of China’s policy to attract foreign investment. ‘Advanced technology’ does not mean ‘technology appropriate for China’, but ‘appropriate technology’ has this meaning. In the case of China at this stage, acquisition of appropriate technological capability is more important, taking into consideration the varieties of technological levels between enterprises and sectors.²³³ Despite some concerns about European competitiveness in advanced technology sectors in relations with the US and Japan, European technologies in traditional industries, such as raw materials, steel, mechanical engineering, coal, chemicals and pharmaceuticals, etc, are particularly appropriate for restructuring China’s state-owned enterprises of traditional industries, which are mostly concentrated in the inland provinces.

Most of the European investments came in the 1990s (particularly after 1993), with the goal of holding a stake in the Chinese market, after the launching of the policies of granting market access in exchange for technology transfer and the opening of more traditional industrial sectors for foreign investments. Since the launching of this new policy strategy, the EC/EU has become the main source of foreign investment, technological investment in particular, in China,. Its status has surpassed that of Japan and the United States. In 1999, 11 percent of the total foreign investments in China were from the EU, compared with 7.43 from Japan and 10.86 from the United States.²³⁴

As late comers, most of the European investment enterprises continue to be concentrated in the coastal regions. According to an investigation carried out in 1995, among 231 Japanese or German projects (including 76 German projects), the projects allocated in inland region (29 projects) only amounted to 13 percent, with only 5 projects for energy, mineral and metal processing as well as other basic industries, and no projects for agriculture.²³⁵ Such a strategy of investment was not in conformance with the Chinese government’s current intention to

²³³ David Bennett *et al*, 1999.

²³⁴ European Commission Delegation in China, *Foreign Direct Investment in China* (1999), <http://www.edc.org.cn/trad>

²³⁵ Wang Zhile, ‘Shijie zhuming kuaguo gongsi zaihua touzi diaoyan baogao (An investigation report on the investments in China from the famous transnational companies)’, in *zhong wai guanli daobao*, No. 1, 1996, pp.7-8.

guide foreign investment into the inland regions in order to facilitate narrowing regional disparities and restructuring state-owned enterprises in traditional industrial sectors.

European investors seemingly overestimated the potential Chinese market size. In this context, the goal of some European investors has shifted from the pursuit of Chinese domestic market access to a combination of market access and the building of production bases in China to produce for Asia. For instance, the largest co-invested project between BASF and Sinopec in Nanjing, with a total investment of US\$ 2.6 billion, plans to provide 70 percent of the export of the crude oil streamcracker (Rohbenzin-Trennanlage) of BASF to Asia by 2010.²³⁶

The European transnational companies are so far the principal investors in China, such as BASF, Hoechst, Bayer, and Siemens. About 75 percent of the EU investment projects are from these three EU countries: Germany, France and Britain. Taking the example of Germany, by the end of 1995, among the ten top German companies, except for BMW, nine had invested in 76 projects in China, among which Siemens alone had 30 projects.²³⁷ Most of the projects are concentrated in coastal regions and belong to the 'pillar industries' of each coastal province, such as telecommunication and electronic equipment, consumer electronics, electrical equipment, mechanical engineering, automobile, and pharmaceutical and petrochemical industry.

In China, any appropriate technology can be regarded as advanced. The European investments played an important role in upgrading Chinese technology and replacing imports by domestic products in some important industries. For instance, fifty projects of the investment from Japan and Germany had produced by 1995 17 products that Chinese domestic enterprises had been unable to produce.²³⁸ Undoubtedly, this tendency still continues. With the increase in foreign-investment enterprises and technology transfer from the EU in the late 1990s, it can be expected that more and more imported manufactures will be replaced by domestic products. For instance, in 1999, 2/3 of foreign technology transfers to China were from the EU.²³⁹

More importantly, some large European enterprises have induced many small and medium-sized European enterprises to invest in China to continue their production linkages with the large enterprises in the new market. European automobile industry has become the dominant foreign investor and partner in this sector. Three largest Chinese automobile enterprise groups have selected European automobile companies as co-operating partners, Renault and Volkswagen. For instance, Volkswagen has persuaded some small and medium-sized enterprises to invest in China to produce component parts for Volkswagen in Shanghai. In

²³⁶ Frankfurter Allgemeine, BASF: Bau der Anlage in China beginnt im Januar, 9. Dezember 2000.

²³⁷ Wang Zhile, in *Zhongwai guanli daobao*, No. 1, 1996, p. 6.

²³⁸ *Ibid.*, p. 11.

²³⁹ NCNA, March 13, 2000.

addition to its role in upgrading the general technology of the Chinese automobile industry, its role in reducing unemployment in some regions and restructuring two of the largest Chinese automobile enterprise groups is not marginal.

3 Conclusion

The status of the EC/EU in three major aspects of China's external relations – import, export and foreign investment – has undergone great changes. The EU is now the third-largest market for China's exports, but its status as a source of imports has slipped to the seventh place. It still retains the status of principal technology exporter in China's external economic relations, but its importance in this respect is declining. The striking imbalance between the growth of Chinese exports to and Chinese imports from the EU indicates the EU's increasing importance as a potential market for Chinese manufactures. This is a consequence of Chinese export-promotion policies. In the context of implementing the policy of replacing imports by domestic products through technological upgrading and the policy of attracting foreign-investment enterprises in manufacturing, its status is shifting from that of principal trade partner to that of trade-investment partner.

The increasing trade imbalance appears to indicate that China's import policies successfully control the composition of the EU's exports to China. European exports to China concentrate on material and equipment for European-investment enterprises and technological upgrading. This control has the consequence that China's imports from the EU are concentrated in a few industrial sectors. Such control contributes to protecting some domestic industries and promoting technology upgrading. Consequently, only a few EU industrial sectors manufacturing products of high technology or having large investments in China have benefited from the exports to China, but the products of many other European sectors, in particular some declining, labour-intensive manufacturing industries, the agricultural sector, etc., have found it difficult to enter the Chinese market due to high import tariffs and various non-tariff administrative measures. Such a composition of the EU's exports to China is particularly unfavourable to some Southern EU member states. As a result of this, promoting the products of these sectors into China has become a main objective of the EU's commercial policies towards China. This is indicated in the outcomes of the negotiations on China's accession to the WTO, as analysed in the next chapter.

The Chinese government is seeking to decrease regional disparities; on the other hand, however, it has to strengthen Chinese traditional industries in order to absorb the likely

impacts after the accession to the WTO, while making preparations to fulfil its obligations to this organisation. European importance in China's foreign economic relations is likely to shift further towards the area of investment and technological upgrading in Chinese traditional industries. This is particularly important for the enterprises in inland regions. In this situation, it is inevitable that the EU will strengthen its role in seeking to improve the conditions for EU investments. Concerning the efforts to expand EU exports to China, it is true that reducing import tariffs and removing non-tariff barriers might increase the competitiveness of some European products in the Chinese market as well as introduce new items (some agro-products in particular) there.

As the analysis in the former chapter has indicated, China's policies in winning foreign investments have not provided real market access. After China's accession to the WTO, this situation will certainly alter. But the building of a really conducive and transparent environment for foreign investors is a long and gradual process.

The striking increase of European investments in China during the 1990s was mainly attributed to three factors: growing Chinese market size due to sustained economic growth, the formulation by China of a policy of 'granting market access in exchange for technology transfer' to attract foreign investment, and a lack of dynamics for economic growth in Europe. Such an increase of European investment in China chiefly by large and transnational companies poses new problems for the EU in its external economic relations. More concretely, it demands a more active European engagement in China, not only to protect and promote the interests of large companies with high technologies, but also those of small and medium-sized enterprises with high or appropriate technologies, which have been drawn into investing in China as component parts suppliers in order to maintain their traditional ties with the large companies. In addition, the EU – or more concretely, the Commission – has not gained the same dominant competence in certain key policy domains and grey areas concerning investments, such as the protection of intellectual property rights, as it has gained in trade. Consequently, the Commission can only be delegated with similar powers by the EU member states, explicitly or implicitly. Pro-activeness in strengthening its ties with the enterprises and in launching a series of programmes in this respect might promote its success in this respect. As analysed in the former chapter, the relations with China provide both opportunities and challenges for the EU. In this respect, the EU, the member states and private interests alike have found shared concerns and objectives. In dealing with the relations with China, such pro-activeness on the part of the Commission is perhaps the appropriate approach for maintaining and promoting its status among the EU institutions.

V. Economic Policies of the EC/EU towards China: Pursuit of Trade Liberalisation according to the WTO-based Rules

1 Institutional framework concerning the policy domains in the case of China

So far economic exchanges still constitute the principal component of the relations between China and the EU, despite the fact that the political dialogues between the two parties have extended to some issues within the domain of the Common Foreign and Security Policy (CFSP). This means that the EU's policies towards China fall mainly under the Community's competence and Community method still dominates the principal policy-making in the case of China, which seeks to maintain a delicate balance of responsibilities among different EU institutions through relatively clearly defined functions in terms of the Treaty of Rome in policy making. Among the four major institutions of the Community, the Commission and the Council of Ministers are the two mostly involved in this respect in the external relations of the EC/EU, the Commission in particular.

The completion of the European Single Market was a means of survival.²⁴⁰ Through removal of various individual national policy barriers, deregulation and regulation, it sought to strengthen European competitiveness by restructuring and forming a common market of European scale. Its principal goal is both to meet the increasing demands by domestic economic interest groups of the pursuit of maximum benefits in a larger domestic market and to meet increasing external challenges with a common European frontier. It is realised on the issue area that all EC member states have shared interests. Thus, it seems to be a tendency that the member states are willing or have to delegate more of their economic policies to the Community. But such delegation can only be realised on some issue areas with shared interest when they all have to meet external challenges and increasing internal pressures. As for the Community, it faces the task of incorporating different policies of individual member states with regard to trade, development cooperation, investment, technology transfer, etc, into a 'common external economic policy'.

The transformation from the Community to the Union has significant importance for the EU's external relations. In terms of Article 11 of the Treaty on European Union (TEU), at least three objectives are related to its relations with China: to preserve peace and strengthen

²⁴⁰ Neill Nugent (1999), *The Government and Politics of the European Union*, , p. 322.

international security; to promote international cooperation in order to develop and consolidate democracy and the rule of law, and respect for human rights and fundamental freedoms. Four policy instruments: principles and guidelines, common strategies, joint actions, and common positions, provide the possibility of creating a more active and powerful European role in world politics. In the case of China, some positive developments have emerged, indicated by the formulation of the EU's common strategy towards China, the building of new mechanisms to strengthen the high-level contacts, etc.

The main executive role of the Council (as well as the European Council) is to set guidelines and objectives for the Commission, monitor the work of the Commission in the implementation of the guidelines, delegate short-term responsibilities to the Commission, execute policies, and adopt new policy competencies for the EU. The Council is restricted under pillar one to taking decisions only on the basis of Commission proposals and in most cases decisions are made by qualified majority. Consequently, in the Community competence the member states have no automatic right of veto, but can block decisions on the 'ground of national interests.' As for the Parliament, is largely limited to, at best, consultations and information sharing. With the building of the annual Sino-EU meeting mechanism since 1998 to discuss increasingly extensive issues concerning bilateral relations and some important international issues of common concern to the two parties, a new tendency is the presidency of the European Council, together with the president of the Commission, came to play a limited but increasingly important role in the EU's relations with China. According to EU institutional arrangements, usually he might rely on the Secretariat of the Council of Ministers. But in the case of China, he might more rely on the Commission for the preparations for the bilateral summit meetings, for most of the topics for discussion are related to cooperation programmes and concrete issues in the bilateral relations. Thus, despite the fact that EU intergovernmental institutions came to become more deeply involved in the bilateral relations than before, the Commission's importance in the new mechanism of the bilateral relations has not been decreased.

The Commission has been at the heart of pressing the case for, and has put forward specific proposals in relation to all of the major issues that have been at the heart of the EU agenda. It has its own administrative culture, institutional interests, policy objectives, and supporting societal groups. As a result, the Commission has powerful incentives and significant political and administrative resources to pursue an agenda independently of the governments of the EC/EU.²⁴¹ But it is bound to pay close attention to the Council's wishes to undertake any

²⁴¹ Simon Hix, *The Political System of the European Union*, p. 54.

studies and submit to the Council any appropriate proposals that the Council considers desirable for the attainment of the common objectives. Playing the role of ‘policy entrepreneur’, the Commission can develop to respond to opportunities for action, and even to create such opportunities. Acting as a ‘purposeful opportunist’, it has employed a variety of techniques aimed at expanding the scope of Community competence and developing its executive power.²⁴² The team within the Commission dealing with the EU’s foreign relations, in addition to the Commission president, currently consists of five Commissioners: the Commissioner for External Relations, Commissioner for Trade, Commissioner for Enlargement, Commissioner for Development and Commissioner for Monetary Affairs.²⁴³

The scope of the EU’s external relations are extending. The extending overlap between political and economic policies and the connection between trade and investment bring about more grey areas and the ambiguity of the competence between institutions, mainly concerning the Council and the Commission. In short, which of the two EU institutions can play a significant role in the EU’s external relations largely relies on its capacity in policy-initiating and exploitation of grey areas. For the Commission, the initiative in policy proposal and effective policy implementation might facilitate the delegation of more power to it by the member states. Such delegation may broaden its competence.

The completion of the Single Market and the amendments in the Treaty on European Union seek to meet the internal and external demands in the new situations of the 1990s. The Single European Market involves the approximation (or harmonisation) of the laws, regulations or administrative provisions of the Member States that directly affect the establishment or functioning of the common market. In addition, the EC seeks to increasingly incorporate various policy instruments into one uniform policy framework at the Community level. The launching of the WTO brought about more mixed policy domains, such as services, intellectual property rights, etc., let alone some cross-cut policy domains such as the policies in development co-operation. The Treaty of Amsterdam, Article 133 (5) enables the Member States, acting unanimously, to extend exclusive EU competence to include services, without having to change the treaty.

The appointment of a Commissioner for external relations is to ensure the consistency of the external activities of the EU as a whole in the context of its external relations, security, economic and development policies, fully associate the Commission with the work carried out in the CFSP field and strengthen the co-operation between the Council and the Commission. Beside the High Representative in the Council for the CFSP, the responsibility of the

²⁴² *Ibid.*, pp. 52-55.

²⁴³ http://europa.eu.int/comm/external_relations/news/patten.

Commissioner for external relations is to share or to take a large part in the implementation and representation of the CFSP. He is co-ordinator within the Commission among different directorates-general involved in the EU's external relations and the standing foreign representative of the Commission in concrete measures to implement the CFSP. Chris Patten, the current Commissioner for foreign relations and the former final British governor in Hong Kong, is likely to play a more personal role in strengthening the EU's relations with China relying on his knowledge and experiences in this respect.

The EU's trade policy is concerned not only with promoting the general liberalisation of trade, but also with ensuring that the consequences of this are not damaging. Free trade agreements are the primary tool of its foreign policy, even if also a disputed one. The Council retains overall responsibility for setting EU trade policy. At the political level, domestic pressures usually went more in the direction of protection than liberalisation. As the European recession in the early 1990s began to bite, it became harder for the Commission to resist political pressures for the use of commercial defence instruments. However, two developments seem to offset the protectionist pressures mainly from some European associations of declining sectors. First, transnational companies with increasing investments abroad and strong lobbying capacity demand further liberalisation. In addition, the EU's trade policies towards the third countries are under the constraints of the GATT/WTO norms and rules. Thus, the adoption of any commercial defence measures must be a compromise between the GATT/WTO rules and domestic demands, liberal and protectionist. More concretely, such measures must be essentially in accordance with the WTO rules.

In the case of China, even though by the end of 2001 it had not been a WTO member state, the EU, either from the consideration of accelerating China's accession to this global trade organisation or from the requirements of fulfilling WTO obligations, could not adopt excessively protectionist measures against China's export practices. In addition, now that external economic policy is the principal policy instrument in the EU's external relations and economic exchanges have composed the major part of the bilateral relations, the applying of appropriate economic policies is one of the major conditions for maintaining friendship with China. The friendship is not only the precondition for the co-operation between the two emerging important actors in world politics and economy, but also requisite for the promotion of bilateral trade. This also helps the operations of European-investment enterprises in China. Thus, concerning the policies towards China in different sectors and policy areas, the EC/EU has different faces, liberal or protectionist.

However, two developments in the EU institutional arrangements are obviously unfavourable for China's export-promotion efforts. First, the completion of the Single Market and the replacement of qualified majority voting by simple majority voting concerning anti-dumping cases in the Council make the imposition of definitive anti-dumping duties easier. Second, all the countries participating in the EC/EU in the two enlargements in the 1980s and the 1990s have relatively fewer economic contacts with China, both with regard to investment and export. But the completion of the Single Market has the consequence that China's low-priced products can be freely accessible to the markets of these countries. The combination of these two factors is perhaps one factor causing the increase in anti-dumping cases concerning China in the 1990s.

Faced with external opportunities and challenges, the supranational EU institutions, the member states and various interest groups in Europe might more easily find shared-interest areas and are more willing to cooperate or coordinate in policy formulation and implementation. Thus for the supranational institutions, the Commission in particular, what is most important is to select relevant issue areas to engage in, with appropriate means, to a convenient extent and in proper time. Such engagements can facilitate positive developments in these aspects, and thereby to expand its competence. Appropriate constructive engagement in China's developments, while meeting the increasing European internal demands, can be easily accepted by Chinese government. The upgrading of political dialogues and the increase of various programmes in order to strengthen cooperation might be effective means to attain the goal of increasing mutual understanding and information exchanges.

The Commission, delegated with rule-making powers to define what constitute 'unfair competitive practices' and 'discrimination practices', manages the EU's Common External Tariff to introduce preventive measures in order to protect the EU market. It is the foremost target for lobbying. China's policies with regard to imports and foreign investment might lead to the consequence that transnational companies play the most important role in lobbying. They are both important investors in China and most important members in the European sectoral associations. Some are also the members of the European Round Table of Industrialists, the most influential European business interest forum. Consequently, they may play an important role in demanding the expansion of the EU's engagements in China. They can encourage the EU both to adopt liberal and protectionist policy instruments. This is totally determined by the need to ensure their interests in China and in Europe. For instance, some major European consumer-electronic companies are both important European investors in China and principal advocates for initiating anti-dumping against the import of competitive

Chinese consumer-electronic products. On the other hand, China's export-promotion policy practices may compel declining European industrial sectors to strengthen lobbying at both European and national levels for the adoption of more protectionist measures against Chinese exports to the EU.

In the objective-setting phase of the negotiations, interest groups and non-government organisations (NGOs) can impose their influences due to the Commission's active encouragement of input from important constituencies in order to help it shape specific negotiating objectives. In some cases, detailed negotiating positions cannot be established without NGO input, and the Commission's efforts in this respect have brought about positive results. One example is the improvement of market access for European exporters and investors. In addition, the Commission also encourages new channels of communication, in order to obtain adequate information or to establish a single point of contact.²⁴⁴ In the phase of legislation drafting involving in the Commission, the Commissioners and (or) their Cabinets, DGs, and various committees normally must undergo public and private consultations. Some of the Commission services have become entirely dependent upon the information, expertise and other resources which the sector interest groups bring to public affairs.²⁴⁵

Two factors directly relate to the influences of the interest groups on the low policies of the EC/EU: their links to the Commission and their degrees of organisation. The Commission prefers actors who have the ability to provide it with the authoritative collective opinion; and where interests are well organised groups, they can therefore be more effective. Where sectors are characterised by small firms, interest representation is weak. However, this is not absolute. If such small firms are concentrated in some regions and some member states, and their interests are represented by the regions and countries, their influences are never marginal. The strong influence of the European textile sector on the EU's policies to control textile imports is only one example. In addition, the Commission has obviously strengthened its links with the small and medium-sized enterprises since the early 1990s through a series of programmes and new strategies to support them in international competition, such as market access strategy, development strategy for small and medium-size enterprises, etc.

Two routes – the national and European – can be taken for the interests groups to exert influence on the decision making at the European level. In the 1990s the tendency was that increasingly the European route was taken, partly because of the 'openness initiatives' launched by the Commission aiming at more transparency of decision making and partly

²⁴⁴ Stephen Woolcock, in Helen Wallace and William Wallace (eds. 2000), *Policy-Making in the European Community*, pp. 380-381.

²⁴⁵ Justin Greenwood (1997) *Representing Interests in the European Union*, p. 122.

because of more access to each other in information supplying between the Commission and the interest groups. Early in 1992 national EU organisations involved in the trade with China came together to form the Euro-China Business Association in an effort to liaise and co-operate more effectively. In addition, the European investors in China represented by transnational companies have created more grey areas concerning investments, services and protection of intellectual property. This new situation demands the Commission's initiatives in formulating some coherent policies at the European level, and in policy implementation it began to coordinate initiatives with EU member states. One example to reveal the Commission's efforts to forge its own and independent links with private sector interests in the case of China is the organisation of the European Union Chamber of Commerce in China. This organisation has direct and close links with the Commission's delegation in Beijing. For some NGOs, e.g. the organisations concerning human rights and environmental protection, since there are no counterpart organisations in China, they have to more depend on the European route in order to incorporate their demands into the Community's policies towards China. The European route include the Commission, Parliament and the Council. Such efforts undoubtedly facilitate the broadening of the policy networks with the Commission as the centre.

In the Commission's advisory committee network the consultative committees are composed of representatives of sector interests. Business interests have always dominated European-level interest representation, in part because of the history of the EU as an economic community and in part because of the institutional arrangements. For instance, according to the procedure rules in anti-dumping, the complaints from the sectors injured by the dumping are the primary condition for the procedures and such interest groups also provide information for the Commission. Concerning quantitative restrictions, there are also similar cases.

The Commission has the preference of maintaining its status and broadening its competence. The broadening of the scope of its involvement through its activism facilitates strengthening the governing coalition and the policy networks. The ongoing power game in the EU legislative process motivates the supranational institutions of the EU, the Commission in particular, intentionally to look for expertise and respond to demands from the non-national interest groups in order to expedite its legislative initiation and management of the policy operation. Such increasing contacts between the Commission and non-national interest groups strengthen its status in the decision-making procedure and maintain its role as principal policy initiator.

The success in involving the relations with third countries and in solving the issues in the mixed area can also strengthen and even broaden its competence. In particular in the case of the countries like China, which has potential market size, high economic growth rate, various unregulated economic policy measures in the transition period and strong state institutions in dealing with foreign partners; both private actors and member states have the common interest to strengthen the Community engagement in order to form a more effective and stronger policy actor of European scale. In short, the policies towards China are the most appropriate selective supply by the Commission to the member states and private actors, and the management of relations with China provides increasing opportunities for the Commission's purposeful engagements. Such engagements facilitate expanding the scope of Community competence and develops its executive power. The new bilateral high-level political dialogue framework institutionalised in the late 1990s appears to demonstrate this. Now the Commission with the Commissioner for External Relations can have direct contacts with Chinese foreign ministry, and its connections with other central government organisations and local governments are becoming increasingly intimate after the launch of various programmes to enlarge the EU's constructive engagement in China. One result of the Commission's activism was that the Chinese premier visited the Commission in 2000, for the first time in twenty-five years since the establishment of the official bilateral relationship.

In addition to the negotiations for its accession to the GATT/WTO, China's export-promotion policies, various tariff and non-tariff barriers to market access and unregulated policies in dealing with foreign direct investments should encourage strong European business interest group lobbying. Two types of European economic interest groups, as components of the policy coalitions and networks, can be expected to be particularly active in this respect: transnational and large companies, which have a global outlook and demand intervention at the European level to facilitate their interests in China, mainly to form an order-framework based on WTO rules so as to realise real market access; and sector associations, in particular the associations of vulnerable sectors, which demand more protection at the European level against Chinese competition. The decision to retain quantitative restrictions on some Chinese exported products is a direct outcome of protecting the interest of the European sectors concerned, but it is also a policy instrument to exchange market access to China.²⁴⁶ The demands from these two types of economic interest groups constitute the principal domestic pressure on the EU's policy making and implementation towards China. Compared to the economic interest groups, the not-for-profit organisations, such as human rights and

²⁴⁶ COM (2000) 091.

environmental protection organisations, seem to have less significant influences in the EU's policies towards China. But their influence is increasing, indicated by the fact that some of their demands have been incorporated in the development co-operation policy area through increasing programmes launched by the EU. The environmental protection organisations, having been formally incorporated in the EU's policy framework, seem to play a more active role than those of human rights. Some of their demands are in conformity with Chinese efforts to pursue sustainable economic growth and therefore can be easily incorporated in the EU's concrete policies towards China.

2 State-trading country/non-market economy, developing country, special market economy or emerging economy, the shift of China's definition in the external relations of the EC/EU

In the external economic policy domains of the EC/EU, the pyramid of preferences towards individual regions indicates geopolitical considerations and historical linkages: The 'near abroad' is always on the top of the pyramid, followed by the ACP countries (the former European colonies).²⁴⁷ Such differentiated policy preferences stem mainly from the concern to avoid negative impacts on security and social stability of Europe, but are also preparations for the planned or expected enlargement. In the new context of the 1990s, when the importance of the colonial past weakened, the pursuit of economic benefit came to become more important. The countries with high economic growth and potential market-size became major targets in the EU's external relations. Since the establishment of the bilateral relations, domestic constraints (mainly economic interests) rather than these two considerations have always been the principal factors dictating the policies of the EC/EU towards China.

All imports from the state-trading countries or recently the non-market economies, the countries with a centrally-planned economy and a state-monopoly trade system, were subject to the special provisions applied to them, and for them punitive sanctions were more readily and easily applied. Generally speaking, protectionism constituted the principal feature of the trade policies of the EC/EU towards state-trading or non-market economy countries.

In the 1970s and 1980s, the EC's policies towards the state-trading countries had double features: various trade defence measures combined with unilateral preferential trade arrangements, the European countries in particular, from case to case. Through this combination the EC sought to achieve multiple objectives, such as to protect vulnerable EC

²⁴⁷ Gabriel Gloeckler *et al*, *Guide to EU Policies*, pp. 152-155.

industries and to promote détente in Europe. Since all of the state-trading countries were not member states of the GATT, they could not automatically enjoy the MFN treatment in their trade with the EC. Thus the extent of preferential arrangements in the policies of the EC depended on their importance in the EC's geopolitical considerations. In the case of Romania, it had already obtained the tariff concessions on its exports to the EC under the GSP scheme before its agreement with the EC taking effect in January 1981, but quota restrictions on its products were abolished or suspended according to the products concerned.²⁴⁸

China had been placed in the list of state-trading countries early in 1970,²⁴⁹ but both the 1978 and the 1985 agreements avoided clear defining China's status in the EC external economic relations: developing or state-trading country (non-market economy). The basic characters of the policies of the EC/EU can be summed up as follows: to treat China basically as a state-trading country but complemented with some preferential policies towards both developing country and country in transition on the case-to-case basis. In the 1980s China's status in the EC's external economic relations was improved, despite its being a non-GATT country.²⁵⁰

This should be attributed to the following factors: its resolute support for the European integration, the demand to maintain a good political relationship with China in order to facilitate the long-term interests of the EC in the competition with America and Japan, and to support China's market-oriented economic reforms and integration into the world economy.

After twenty years of market-oriented economic reforms and Open Policy, China was formally removed from the category of 'non-market economic countries' and was defined as 'special market economy' in anti-dumping cases in 1998. Domestic price information is used in anti-dumping investigation if the existence of market conditions can be shown. Flexibility is a key aspect of the new rules, which allow decisions to be taken on a case-by-case base. The enterprises involved in anti-dumping investigations must present evidence that the producing and selling of the goods are in conformity with market conditions,²⁵¹ or as an 'emerging economy' in the EU's external economic policy framework, referring to those developing countries currently undergoing deep economic reforms and rapid industrialisation.²⁵² In the case of China, this means not only a country undergoing deep

²⁴⁸ R. C. Hine (1985), *The Political Economy of European Trade – An Introduction to the Trade Policies of the EEC*, p. 248.

²⁴⁹ Xiao Zhi Yue (1993), *The EC and China*, p. 11, footnote 3.

²⁵⁰ One indication of China's improved status in EC's external relations was the granting of the GSP to China in 1980, soon after it had begun the process of economic reforms and Open Policy in the end of 1970s. Such a decision granted China a relatively preferential status in EC's external economic relations. In addition, in the 1980s most of the anti-dumping procedures in the case of China were ended with price-undertaking.

²⁵¹ Verordnung (EG) Nr. 905/98, 27. 04, 98, in *Amtsblatt der Europäischen Gemeinschaften* L 128/18, 30. 4, 98.

²⁵² COM (1996) 344.

economic reforms and rapid industrialisation, but also a country in the transition from a centrally-planned to a market economy. Such a new definition does not imply a significant improvement of China's status in the EU's external economic relations, for 'deep economic reforms' means risks in this period of transition (undisciplined trade behaviour) and 'rapid industrialisation' means differentiation from most other developing countries. In short, it must be treated 'specially'.

The ambiguity in defining China's status in the external relations of the EC/EU contributes to the pursuit of both principle and flexibility in policy operation. On the one hand, by implicitly treating China as a state-trading country through concrete policy operation, the EC/EU can more effectively make use of commercial defence policy instruments to provide better protection to the vulnerable European industries and discipline Chinese trade behaviour; on the other hand without the restriction from the clear and fixed definition it retains enough policy flexibility to maintain good relations with China through a variety of preferential treatments in the development co-operation policy domains in different cases and at different time.

According to the norms of the GATT/WTO, trade liberalisation is not unconditional. Members of this organisation have sufficient room in transforming the norms of liberalism into actual policy practices. By the end of 2001 China had not obtained a WTO membership. Thus, the bilateral relationship mechanism provided the EC/EU relatively more flexibility in adopting its policies towards China according to different domestic contexts and China's external economic policy behaviour. The policy adjustments became more important in the 1990s in order to encourage China's accession to the WTO, which relates directly to the time and extent of the EU's market access to China.

3 The evolution of institutional arrangements in trade and economic co-operation between the EC/EU and China

3.1 The 1978 and 1985 agreements between China and the EC: a summary

As a non-preferential trade agreement, the 1978 trade agreement constitutes the legal framework in the aspect of bilateral trade. It consisted of the MFN clauses, but sought to distinguish China from members of a customs union or free trade area, neighbouring countries and members of the GATT.²⁵³

²⁵³ Article 2, para 2 of the Trade Agreement.

According to the clause concerning balance of trade, the two contracting parties are to make every effort to ‘foster the harmonious expansion of their reciprocal trade and to help, each by its own means’, to attain this goal; and the Joint Committee was responsible for recommending concrete measures.²⁵⁴

The measures available to safeguard trade include the re-imposition of quantitative restriction, tightening existing quotas, increasing customs duties and taking any other ‘general commercial measures’ it deems necessary.²⁵⁵ Thus, quantitative restrictions, anti-dumping measures, and special commercial policy instruments, together with the safeguard clause and limited MFN treatment, made up the EC’s legal framework in its trade with China.²⁵⁶ With regard to any trade problems that may arise, there should be ‘friendly consultation’ before any safeguard measure is taken. This obligation to consult was incorporated at China’s insistence.²⁵⁷ However, there is an exception ‘where the situation does not admit any delay’. The Community promised to ‘strive’ to remove quantitative restrictions on imports from China. ‘To this end it will endeavour progressively to introduce measures extending the list of products for which imports from China have liberalised and to increase the amounts of quotas’²⁵⁸ In turn, China agreed to ‘ensure that Community exporters have the possibility of participating fully in opportunities for trade with China’.²⁵⁹

The context for concluding the agreement of 1985 was different from that of 1978 in two aspects. First, the agreement of 1978 was no longer fitted into the new developments and failed to meet the new demands owing to the launch of China’s market-oriented economic reforms and the Open Policy. Second, by the conclusion of this agreement, China had concluded trade and economic co-operation agreements with all EC member states except Ireland. For the EC, the agreement on trade and economic co-operation with a third country is normally ‘the most potent tool of influence in foreign policy’.²⁶⁰ Thus the conclusion of such an agreement was not only a policy practice similar to the Member States at the Community level but also a demonstration of the EC’s positive response to the new developments in China.

Composed of three parts – trade, economic co-operation, and investment – this agreement retained all principal stipulations concerning trade in that of 1978, including clauses concerning most favoured nation, safeguard, trade balance, and price. Compared to that of

²⁵⁴ Article 3 of the Trade Agreement.

²⁵⁵ Xiao Zhi Yue, p. 30.

²⁵⁶ Xiao Zhi Yue, p. 32.

²⁵⁷ Kapur (1985), p. 42 & pp. 47-48.

²⁵⁸ Article 4, para 2 of the Trade Agreement.

²⁵⁹ Article 4, para 1 of the Trade Agreement.

²⁶⁰ John Peterson and Elizabeth Bomberg, *Decision-making in the European Union*, p. 104.

1978, with regard to trade dispute settlement, it imposed more restriction on, but does not impede, unilateral actions taken before consultations; for ‘in an exceptional case, however, where the situation does not admit any delay, either Contracting Party may take measures, but must endeavour as far as possible to hold friendly consultations before doing so’.²⁶¹ It retains enough autonomy in adopting trade defence measures towards China. In all cases so far it has been the EC’s right to enforce such unilateral actions before any consultation taking place. Another piece of progress was that this agreement acknowledged the different levels of development between the two contracting parties.²⁶² However, such a confirmation by the Community did not mean that it would classify China as a developing country in bilateral trade relations, nor did it change the Agreement from a non-preferential into a preferential one.²⁶³ It could be regarded at most as an implicit recognition that China’s economic development level was similar to that of most other developing countries. But such a confirmation facilitated the Community’s continuing its development activities in China. The two parties decided to extend their relations to an economic cooperation in all spheres as long as they fall within the EC’s competence, in particular, industry and mining, agriculture, agar-industry, science and technology, energy, transport and communications, environmental protection, and co-operation in third countries.²⁶⁴ Both parties encouraged various forms of industrial and technological cooperation and facilitate and promote joint production and joint ventures, common exploitation of resources, the transfer of technology, cooperation between financial institutions, the organisation of seminars and symposia, consultancy services, technical assistance, contact and visits between individuals, delegations and economic organisations, and continuous exchange of information relevant to commercial and economic cooperation.²⁶⁵

Reflecting the interests of both sides to facilitate the investments from Europe to China, this agreement includes an investment clause: ‘the two contracting parties shall agree, within the framework of their respective laws, rules and policies, to promote and encourage greater and mutually beneficial investment.’²⁶⁶

The provision concerning economic cooperation and investment only provides a general scheme but fails to include any practical details regarding economic cooperation. Such an arrangement reflects the Community’s lack of full competence in this respect. Thus, effective

²⁶¹ Art. 6 of the Agreement.

²⁶² Art. 13 of the Agreement.

²⁶³ Xiao Zhi Yue, p. 56.

²⁶⁴ Art. 10 of the Agreement.

²⁶⁵ Art. 11 of the Agreement.

²⁶⁶ Article 12 (1) of the 1985 Agreement.

implementation of this agreement relies on the Commission's initiatives and engagements through a variety of programmes. This is reflected in the EU's policies towards China in the 1990s.

3.2 The evolution of management of the imports of textile products from China

3.2.1 The changing European and Chinese contexts

China has become one of the leading textile products exporters to the EC/EU. In the period from 1978 to 1998 the increase was fifty-five fold. The increase is striking, despite the enlargement of the EC/EU from the mid-1980s to the 1990s from 9 to 15 member states.²⁶⁷ For China, the export of textile products has always been of strategic importance.²⁶⁸ It is possible that the exports of textile products will again become the most important of Chinese exported manufactures with the removal of quantitative restriction by 2005 according to the new WTO requirements to replace Multifibre Agreement (MFA) with Agreement on Textiles and Clothing (ATC).

The management of textile imports has always been the striking feature of the trade policies of the advanced countries. The EC/EU does not have a natural competitive advantage as substantial parts of this sector are highly labour intensive, in spite of its technological advantages in yarn and cloth. Between 1988 and 1994, with imports rising by about 80 percent, the textiles sector accounted for nearly one-third of jobs lost in the EU.²⁶⁹ However, some specific features of this sector – such as the fact that this industry is mainly composed of small and medium-sized enterprises, which concentrate in some regions and in some Southern Community countries in particular; and international competition becomes intensifying due to the fact that textile exports for many developing countries serve as the main means to generate foreign earnings – strengthen its importance in alleviating regional unemployment (women in particular).

²⁶⁷ Its textile products export to the EC in 1978 accounted for 127.3 million Ecu, but increased to 7 billion Ecu in 1998. <http://www.ecd.org.cn/pr/press99>

²⁶⁸ The sector of textile and clothing currently employs a work force of about 10 million, and 47 per cent of the total production value of this sector is realised through exports. Its importance for Chinese exports can be indicated by the following statistics: in 1980 the value of exports of textile products was \$3.268 billion, accounting for 17.9 per cent of Chinese total exports; in 1998, the value increased to \$42.9 billion, accounting for 21.54 per cent of Chinese total exports. The increase was twelve-fold. The rate of increase is striking, but it mainly depends on the increase in exports to the regions and countries without quantitative control; this accounts for about 80 per cent of the increase. Sun Jinjun, "fangzhiye 'nihao' zhong yeyou yinyou", in *Xinghua Yuebao* (*New China Monthly*), No. 1, 2000, p. 90.

²⁶⁹ John Peterson and Elizabeth Bomberg, p. 113.

Similar difficulties also exist in restructuring Chinese textile and clothing sector, particularly the state-owned enterprises producing silk, yarn and cloth. In addition, the state-owned textile and clothing enterprises are facing increasing challenges from village enterprises as well as from foreign-investment enterprises, which, relying on the low labour costs and their better marketing, constitute the real threat to the state-owned enterprises. For the Chinese, one effective approach to facilitate restructuring this sector is to expand the exports of low-priced textile and clothing products. The basic feature of the policy practice is that the state imposes strict control on the export of some textile products subject to quantitative restrictions in terms of bilateral agreements with its trade partners but encourages the export of the products not subject to quantitative restrictions.

The export of Chinese low-priced textile products to the EC/EU not only threatens the European textile industry, but also constitutes increasing competition between the textile industry of China and some developing countries. Thus the EC/EU was under four-fold pressure on the issue of Chinese textile imports: it has to fulfil its obligation to the GATT/WTO to gradually lift the quantitative restrictions, the European textile and clothing sector requires for a strengthening protection, the developing countries ask to increase their textile exports to the EC and China demands for the reducing of quantitative restrictions.

In addition, the Chinese government has long imposed strict management on the silk industry, from purchasing raw materials to production, in order to maximise profits from this industry with Chinese raw material monopoly. China produces 70 percent of the world's raw silk. For this reason, the administration of the state monopoly (including that of local governments) might operate preferential policies towards Chinese producers and local enterprises. More seriously, in the context of decentralisation, local governments are gradually obtaining a monopoly on this industry from raw material supply to trade of manufactured products. Consequently, the regular foreign trade channels have been disrupted. Moreover, without close contacts between Chinese and European enterprises, problems might arise in raw material supply related to supply channels and product qualities. Such practices impeded European textile industry access to this important textile raw material for high-quality products. Many up-market EU firms are now increasingly carrying out their manufacturing in China. Guaranteeing the supply of high-quality raw materials and strengthening the protection of intellectual property rights are two important conditions for protecting their interests.

The evolution of the textile regime indicates multiple objectives: to impose strict quantitative control, to guarantee the demands of European enterprises in raw material supply, to discipline the behaviour of Chinese exporters, to protect European intellectual property rights,

to promote European investments in China, and to promote the mutual interests by improving the existing management framework, establishing new channels to strengthen co-operations between the textile industries on both sides.

Thus, the evolution of the bilateral textile control regime indicated three tendencies: the EC/EU gradually increases the annual quotas for Chinese textile imports; but in the meantime it both expands the quantitative restriction ranges of textile products and reinforces the control measures; and it strengthens its engagement to ensure European textile enterprises benefit from cooperation with Chinese textile industries in raw materials supply and protection of European intellectual rights.

3.2.2 The 1979 textile agreement

The agreement on textile products of 1979 covered textile raw materials and textile products of wool and fine animal hair, cotton and man-made fibres.²⁷⁰ It established the legal mechanism to manage Chinese textile exports to the EC, such as quota arrangements, base level (annual level to which the export quantity of a particular product is restrained), growth rate (increase rate over the level of the previous year, below 6 percent) and flexibility, the basket extractor mechanism (the EC's unilateral right to impose restrictions on previously unrestricted products whenever the Community considered it necessary), price clause (a provision to prevent low-priced Chinese products from distorting the Community market), anti-surge clause (the Community's right to request Chinese smooth utilisation of the agreed quotas), double administrative control (quota management for a textile product exported to the EC by obtaining of an export licence issued by Chinese authorities and corresponding import authorisation by EC authorities), and Chinese guarantee of raw materials supply to the EC. A textile committee was set up under the provisions of the textile agreement, which was granted a wide range of powers, such as the power to conduct the consultations provided for under the agreement as well as deal with any other problem arising from the application of the agreement.²⁷¹

Taking into consideration that China was not a member of MFA (China became a member of MFA in 1984), this agreement was even more favourable towards China than normal MFA II bilateral agreements concluded between the Community and other less developed countries. The Community agreed to significantly increase the quotas for non-sensitive Chinese textile

²⁷⁰ The 1979 EEC-China textile agreement, OJ L389, 1986.

²⁷¹ Article 16, para 1 of the agreement.

products and increase Chinese textile exports to the EC from 20,000 tons a year to 40,000 tons a year.²⁷²

3.2.3 The 1984 supplementary protocol²⁷³

China became a member of MFA in 1984, and the MFA III was in operation, which included new provisions to protect textile importing countries.²⁷⁴ To accommodate to these changes, in the 1984 Supplementary Protocol the Community tightened up restrictions on imports of textiles from China by putting five more categories of textile products from China under limits, and imposing some 34 new restrictions on imports of textiles to various parts of the Community. In return for the imposition of these additional restrictions the Community agreed to increase the amounts of certain quotas including some of those relating to highly sensitive products.²⁷⁵ It dropped the price clause of the 1979 textile agreement, owing to strict quantitative restrictions on imported textile products and Chinese market-oriented economic reforms. In addition, it granted the Community the power to take unilateral action in such circumstances if a consultation failed to result in any agreement. Taking account of the confusion arising from the decentralisation of Chinese foreign trade administration as well as increasing foreign-investment enterprises for export processing in this sector, the Supplementary Protocol contained an anti-circumvention clause, an outward processing clause, an anti-fraud clause, and an intellectual property rights clause.

3.2.4 The 1988 and 1999 textile agreements²⁷⁶

The 1988 textile agreement was concluded in the context that China had become one of the top textile suppliers to the Community, and according to the Community statistics the Community had begun to show a deficit in the trade with China. The Community continued its traditional approach: increasing the amount of base quotas for Chinese textile products but expanding the quantitative control ranges by introducing quantitative restrictions on a number of textile products which were not subject to quantitative restrictions under the previous textile agreements, as a result of amendments to the system of textile product categories made

²⁷² Xiao Zhi Yue, p. 68.

²⁷³ The 1984 supplementary protocol, OJ L198, 1984.

²⁷⁴ Xiao Zhi Yue, p. 76.

²⁷⁵ Xiao Zhi Yue, p. 76.

²⁷⁶ The 1988 EEC-China Textile Agreement, OJ L380, 1988; and the 1999 EU-China Textile Agreement, OJ L 12, 1999.

necessary by the introduction of the Harmonised System nomenclature.²⁷⁷ In the meantime, in order to make the European textile industry benefit from the trade with China and protect the European producers' rights, China undertook to supply more raw silk and both parties agreed to resolve problems relating to intellectual property through consultation.

The subsequent negotiations of the MFA agreements resulted in agreements in the form of an exchange of letters. The 1999 agreement modified appreciably and extended the previous agreement. It adjusted the quotas and maintained the double control frame, namely that the Chinese authorities continue to manage quotas by issuing export licences, and the EU authorities cover the import.

*3.2.5 The 1995 agreement on trade in textile products not covered by the 1988 textile agreement*²⁷⁸

The new WTO mechanism demands bringing all textile goods under normal WTO rules over a period of time, but the agreement of 1995 is more a result of the completion of the Single Market—the abolishment of the border control within the EU means the national trade regimes with the third countries in some products must be replaced by EU trade agreements in order to harmonise the rules and to minimise potential adverse impacts owing to the free movement of goods in the internal market. For instance, Germany had not imposed quantitative restrictions on the import of silk products.

The 1995 agreement has brought under control the trade in textile raw materials and textile products (textile raw materials, textile products other than those of wool and fine animal hair, cotton and man-made fibres, namely silk, linen and ramie products) which was not covered by the MFA bilateral agreement of 1988 but formerly covered by Council Regulation (EC) No 517/94 (unilateral arrangements). The EC's control range now covers all textile imports from China, both the products under the MFA and under the non-MFA framework.

It contains all provisions in the former bilateral MFA agreement, including the clauses of the double checking system, anti-surge, guarantee of raw material supply, exports to China from the Community, consultation, anti-fraud, outward processing, arrangement of quotas, and an additional specific clause of strengthening co-operation between the two parties.

This agreement seeks to ensure the interests of European textile and clothing industries by demanding Chinese government fulfil its commitments in production and supply of raw silk

²⁷⁷ Xiao Zhi Yue, p. 83.

²⁷⁸ The 1995 Agreement on Trade in Textile Products Not Covered by the 1988 Textile Agreement, OJ L 104, 1995.

when the Chinese government is seeking to transform the management on silk industry from state monopoly to market mechanism. For this purpose, it contains a comprehensive article concerning strengthening co-operation between the textile sectors of both parties, including: facilitating the contacts between both sides in the industrial, commercial and technological fields, in order to strengthen the co-operation; promoting the exchange of visits by persons, groups and delegations and assisting the organisation of fairs and exhibitions of mutual interest; and encouraging investments that may promote increased integration between silk industries and technological exchanges, establishing a system of grading and standards for silk and of appropriate common methods of testing; and organising an arbitration body to address possible disputes concerning the fulfilment of conditions and terms.²⁷⁹

3.2.6 Summary

As one EU document acknowledged, China's accession to the WTO constitutes a major challenge for the sector of textile and clothing because of China's immense production and export potential. China will benefit from the ATC rules from the date of entry into the WTO. On the other hand, the accession of China will provide new opportunities for European exporters. In the EU's bilateral and multilateral relations, social aspects of globalisation of trade are to be emphasised, and access to markets will be defended for the sake of the reciprocity of commitments and compliance with obligations.²⁸⁰ All agreements concluded in the 1990s assented that these arrangements will be compliant to the WTO rules after China's accession to this organisation. Thus the agreements concerning the textile sector serve not to regulate Chinese textile export to the EU, but also as a policy instrument to accelerate the process of China's accession to this organisation by demanding China make more concessions. The completion of the regime in the control of the imports of Chinese textile products laid by a series of MFA agreements from 1979 to 1999 and the non-MFA agreement of 1995 indicated the attempt to pursue a balance between the EU's commitments to the WTO in liberalising the textile imports and more active engagement in protecting and promoting the interests of this declining industry in Europe. This was also partly as a reaction to Chinese export-promotion policies and practices. It has formed a more effective and uniform Community management regime on the import of all textile products from China by replacing the regimes of the individual EU member states concerning the import of textile products.

²⁷⁹ Article 10 of the 1995 Agreement on Trade in Textile products not Covered by the 1988 Textile Agreement.

²⁸⁰ SEC (2000) 1531, Commission Report on the Implementation of the Action Plan to Increase the Competitiveness of the European Textile and Clothing Industry, COM (97), 454.

After the completion of the quantitative restriction regime, the emphasis has been shifted to building a cooperation regime, as a preparation for China's accession to the WTO and the expected liberalisation of trade in this sector. This comprehensive regime promotes better integration and cooperation between the textile industries of both sides. It also facilitates disciplining Chinese trade practices and decreasing the potential adverse impacts on the EU's textile industries after 2005 owing to the launching of the ATC.

4 General System Preference (GSP) in the case of China

4.1 The new trend of the GSP

In the 1990s the EU's development co-operation policy frame became more politicised and more oriented towards the most disadvantaged developing countries, in addition to its three basic socio-economic objectives: sustainable economic and social development, the campaign against poverty in the developing countries, and smooth and gradual integration of the developing countries into the world economy. Development cooperation is politically conditioned: aid should be conditioned upon the development of democracy, good governance, human rights and basic rights in recipient states.²⁸¹ Moreover, the EU's development cooperation policies should co-ordinate with the policies pursued by the Member States, and more support should be given to the less developing countries.²⁸²

Accordingly, the GSP, as one principal and effective external policy instrument in this respect, has become more politicised and more pragmatic. The new GSP scheme after 1995, rather than merely promoting industrialisation in the developing countries by promoting exports of semi-finished and finished products from developing countries through suspension or reduction of duties, is more oriented towards the least-developed countries. It incorporates economic, social, and political goals into one policy framework. It places new emphasis on the human element and environmental concerns, and links total or partial withdrawal of GSP preference to the following cases: forced labour of any kind, export of the products produced by prisoners, unfair trade activities, and an obvious ineffectiveness of the customs control on exporting or transiting of narcotic drugs. Environmental protection standards for the first time entered into the GSP scheme.

²⁸¹ TEC article 130u. 2.

²⁸² TEC article 130u. 1.

The 'graduation' mechanism of the new GSP indicates greater orientation towards the least developed countries. The standard of 'graduation' is determined by two factors, the development index of a nation (US\$ 6,000 GNP per capita) and an industrial specialisation indicator. The countries with a GNP over US\$ 6,000 per capita lost the GSP treatment after 1996, (those under US\$ 6,000 per capita after 1998). By introducing the development index and the industrial specialisation indicator, it becomes easier to assess one state's economic performance and to adjust GSP levels accordingly, and the advanced developing countries are excluded from benefiting from the GSP.

In the operation of the GSP, it is a principle that for sensitive as well as for semi-sensitive and non-sensitive products, an individual supplier country must not exceed a definite import maximum. The purpose of the maximum amount regulation is to allow for the differential commercial strength of developing countries and to prevent particularly competitive countries from exhausting the quota on their own. In two circumstances the GSP preference is withdrawn, provided the exported products of a certain kind from a country are over 25 percent of the total imports by the EU under the GSP arrangements (the former arrangements were 50 percent) or the level of the exported goods exported to the EU under the GSP arrangements increases well over that of 1993. This facilitates impeding the possible emerging dominance of some countries in some sectors in their trade relations with the EC/EU.

Replacing both the tariff ceilings and the duty-free quotas of the former GSP scheme, preferential tariffs have been modulated according to the sensitivity of products. The new GSP scheme divides the manufactured products into four categories with differential preferential import duties: very sensitive: mainly textile products; sensitive products: extensive items including some chemical products, products of light industry, some kinds of footwear, materials and products of copper and aluminium, some consumer-electronics products, and some machinery products; semi-sensitive: extensive items including some chemical products, products of steel and iron, materials and products of lead and zinc, some machinery and electronic products, as well as some products of light industry; and non-sensitive: extensive items of industrial products not included in the above three categories. The more sensitive a product, the smaller the preferential tariff margin is. The preferential tariff margins are respectively 15 percent, 25 percent, 65 percent and 100 percent. Such a new scheme, while being more orientated towards the least-developed countries, also seeks to minimise the adverse impacts of this preferential policy instrument on the European

traditional but also declining industries. Consequently, it is questionable that this scheme can really promote the industrialisation in the developing countries.

4.2 The GSP in the case of China in the 1980s

The granting of the GSP to China from 1 January 1980 had more the function of political signal, This at least demonstrates the EC's support for China's market-oriented reform, while partly satisfying the Chinese demand to be distinguished from the East-bloc countries. The GSP was one policy instrument contributing to 'creating favourable conditions for trade between them (China and the EC)'.²⁸³ But its strict restrictions on quantities and products falling in the GSP category revealed the intention to minimise the possible adverse impacts on European industries.

In the early 1980s how to increase China's exports to the EC was the central issue in bilateral relations. China lacked items suitable for the European market; and in order to regain trade balance, it reduced imports and increased exports of some sensitive products. Consequently, its exports to the EC increased 43% but imports decreased 18% in 1980. In this period, Chinese products exported to the EC, with the exception of a few, such as textile products, did not constitute a threat to most of the European industries. In order to promote China's exports to the EC, under strict quantitative restrictions, some sensitive products were also granted GSP.

However, the complexity of the GSP impeded maximising benefit from it. In addition, the margin of the preference tariffs varied from low to high according to the degree of sophistication of the manufactures. Consequently only the advanced developing countries profited most from the GSP scheme. This was also the case of China in the early 1980s. The Chinese lack of knowledge of the GSP and the lack of contacts between the businesses of both sides constrained the Chinese to increase China's exports to the EC by fully utilising preferential arrangements. To improve marketing through the establishment of contacts between the enterprises of both sides was the main concern in the 1980s. In March 1982, the Commission sent a delegation to organise a seminar in China, particularly discussing the preference regulations for agricultural and textile products, two major Chinese exported products, as well as the special regulations fit for China.²⁸⁴ In 1981, 1985 and 1988 the Commission separately organised three business week exhibiting Chinese exported products

²⁸³ Agreement of 1985, article 2.

²⁸⁴ Bull. EG 3-1982, 2.2.20, p. 65.

in Brussels.²⁸⁵ In addition, under quantitative restrictions the EC gradually increased the number of items in the GSP list in the 1980s. Such a practice of selective liberalisation of quantitative restrictions on the imports from China sought to strike a balance between China's demands for favourable treatments in the framework of the Common Commercial Policy and the protection of some European sectoral interests. The shift in Chinese export composition from primary products to increasingly complicated manufactures partly revealed the positive role of the GSP in promoting Chinese exports.

4.3 The new GSP in the case of China

In the new GSP scheme the granting of the GSP preference to China is mainly in terms of the industrial specialisation indicator, namely that some sectors have reached a sufficient level of export penetration. Such an indicator has the implicit goal of limiting some sectors of some countries in establishing very appreciable shares of the European market, in order thus to protect some European industrial sectors and to control the penetration of some foreign manufactures in the European market.

The new GSP scheme has some impacts on Chinese exports to the EU. First, textile products, as the 'very sensitive' products, are granted lowest tariff preference (15 percent). This in fact discourages Chinese textile exports to the EU.²⁸⁶ Second, in terms of the development index of the new GSP, about 41 percent of Chinese exports to the EU should come to 'graduate' in 1998, most of which belong to the manufactures with traditional competitiveness.²⁸⁷ Third, according to the industrial specialisation indicator, some Chinese products, mainly textile products and bags, lost the tariff preference as soon as the new GSP became effective. Afterwards, more and more Chinese products, including some principal Chinese products, lost the tariff preference. From this perspective, the new GSP scheme impedes Chinese export-promotion ambition and practices. In addition, Chinese trade administrative authorities had to strengthen the co-ordination in quota granting in order to postpone the time of graduation of some principal manufactures by maintaining the volume of export of these products to the EU under the 25 percent ceiling.

Moreover, the new GSP scheme, by linking environmental protection to the preferential arrangements and by emphasising international standards of labour rights, seeks to promote

²⁸⁵ Bull. EG 4-1981, p.p. 14—16. Bull. EG. 12-1985, 2.3.33. p. 106. Bull. EG. 3-1988, 2.2.41, p. 105.

²⁸⁶ According to Chinese statistics, the textile export to the EC in 1996 decreased 9.5 percent compared to that in 1995.

²⁸⁷ Tian Chunhua, 'oumeng duihua maoyi zhengce ji woguo duice (the trade policies of the EU towards China and our countermeasures)', in *Guoji Maoyi Wenti (the Problems of International Trade)*, 1993, No. 3, pp. 25-28.

the progress in these two respects. The Commission has admitted that the implementation of the scheme's graduation mechanism will necessarily reduce the advantages previously enjoyed by China, and approved the proposal that, in the event of applications from China, the Commission would examine carefully whether China meets the requested standard (international standards of labour rights and environmental protection).²⁸⁸ Undoubtedly, this is a promise without any binding force. Currently, the share of total China's exports to the EU under GSP amounts to around 30 percent.²⁸⁹ This might be the outcome of China's efforts in strengthening co-ordinations among exporters in order to postpone the graduation. More possibly, the granting of the GSP preference to some Chinese manufactures reveals the EU's intention of retaining some preferential treatments towards developing countries in the case of China. This can promote the bilateral trade. Politically, this arrangement facilitates maintaining friendly relations with this increasingly important economic and political power. In sum, in terms of the new GSP scheme, a large part of Chinese manufactures exported to the EU has lost the principal preference granted to a developing country. Thus, despite the removal of China from the list of non-market countries, some preferential policies towards it have also been lifted. China has to change its traditional approach of export-promotion by relying on increase in the volume of a few principal manufactures and accelerate the improvement of export composition. In addition, according to the original regulations, the manufactures with European component parts can continually be granted the GSP. Thus Chinese manufactures exported to the EU, if containing imported component parts, have to make use of as many European component parts as possible in order to be continually granted the GSP. By these new regulations, the new GSP scheme also facilitates European exports.

5 Policy instruments of commercial defence

5.1 Anti-dumping, a general survey

In terms of Article 113 of the EC Treaty, the EC has the exclusive competence to take measures to protect trade in case of dumping or subsidies. The Commission receives complaints from member states or industries which think themselves injured or under threat, carries out the investigations, and imposes provisional duties, but the definitive anti-dumping duties are adopted by the Council. In the 1990s, as a price paid for French support for Uruguay Round agreement, by a simple majority vote rather than qualified majority vote the

²⁸⁸ COM (1998) 181.

²⁸⁹ <http://europa.eu.int/comm>

EU's commercial defence instruments, including anti-dumping procedures, became easier to deploy.²⁹⁰

The regulations of the EC/EU concerning anti-dumping are based on the GATT anti-dumping codes, dumping being defined as selling a product in the Community at a price below its 'normal value', which is usually the actual sale price on the domestic market of the exporting country, or the cost of production in the country of origin.²⁹¹

Material injury to Community producers is the necessary factor leading to the EC interventions, in addition to the fact of dumping. The injury at issue must be suffered by an industry as a whole (or a major part of it) and must be material. 'Industry' is normally taken to be the narrowest sector of production which can be identified, either all manufacturers of the same product or those who account for a major proportion of the Community production. Various European-level interest representations of sectors of manufacturing, such as the European Chemical Industry Council, the European Bicycle Manufacturer Association, etc, are principal actors participating in the anti-dumping proceedings. The injury to 'Community interests' is the principle in determining anti-dumping, but the 'Community interests' are usually interpreted as the interests of Community producers.

The Community contains special rules to deal with the imports from state-trading countries, and employs a method referring to a third market economy (analogue country) in order to determine the normal value in the non-market economy, in assessing whether there is a case of dumping. The guideline in selecting an analogue country is not clear and definite. According to the 1988 Regulation, the sole guideline is a general obligation on the Community to determine normal value 'in an appropriate and not unreasonable manner'.²⁹² In practice, the Commission developed a set of rules concerning the selection of an analogue country: (a) the comparability between the proposed analogue country and the non-market economy country concerned in the structure of the manufacturing process in the relevant industry and in the production processes and the scale of production; (b) the competitiveness of the market, mainly concerning a reasonable proportion between production costs and price levels; (c) the availability of the information on production in the suggested analogue country; (d) the market economy country accused of dumping to be used as an analogue for the non-market economy country; (e) the similarity of the product in the analogue country; (f) other possible factors such as the similarity of access to raw materials and the level of economic

²⁹⁰ John Peterson and Elizabeth Bomberg, p. 106.

²⁹¹ COM (2000) 440 final.

²⁹² Article 2 (5) of the Regulation and Appendix 1, OJL 209, 1988.

development.²⁹³ In the 1980s, the Eastern European block accounted for 8 percent of EC imports but 24 percent of its anti-dumping cases.²⁹⁴ This indicates that the state-trading countries were the principal anti-dumping targets.

The current anti-dumping and anti-subsidy investigations in the Community entered into force between March 1996 and April 1998. In addition to the 'Community interest test', the 'lesser duty rule' is another principle of the practice. In the first aspect, the current EU provisions require three main tests before anti-dumping duties can be applied: evidence of dumping; injury or the threat of injury to a European industry; and a demonstration that the imposition of anti-dumping duties would be in the 'Community interest'.²⁹⁵ The overall 'interest of the Community', which covers all economic interests involved, including the interests of the domestic industry, users and consumers, is the basis for anti-dumping measures. Undoubtedly, with regard to the 'Community interest test', the interests of preserving employment in the Community are carefully considered. Thus, the 'Community interest' is normally interpreted as the interest of Community producers. In the second aspect, the measures imposed by the Community should be lower than the dumping or subsidy margin, if such a lower duty rate is sufficient to protect the Community industry adequately. In accordance with the recommendation of the Essen summit, a preferential rule only applies to the Central and Eastern European Countries (CEECs) in the anti-dumping proceeding, replacing punitive duties with price undertakings, and certain preferential rules apply to the CEECs and Turkey.²⁹⁶ These rules concerning anti-dumping have at least three significations: first, such preferential rules obviously facilitate the transition of these countries and preparation for the Eastern enlargement; second, the anti-dumping procedures become more easily and readily applicable to the other third countries; and third, it is a more appropriate policy instrument to use.

5.2 Anti-dumping in the case of China

The EC's first anti-dumping proceedings against China began in 1979, just at the time when the Chinese government began to practice the new export-promotion policy strategy through decentralisation of the foreign trade administration. Since the mid-1980s roughly five to ten percent of the EC's anti-dumping proceedings per year concerned Chinese products. This fact indicated, to some extent, the correlation between Chinese export-promotion practices and the

²⁹³ Xiao Zhi Yue, pp. 92-93.

²⁹⁴ Ludger Schuknecht, p. 125.

²⁹⁵ Stephen Woolcock, in Hellen Wallace and William Wallace (eds.), p. 389.

²⁹⁶ COM (2000) 440 final, p. 20.

EC's anti-dumping proceedings. Undoubtedly, the competitiveness of Chinese products in European market currently still depends on their low prices.

In the 1980s most of the anti-dumping proceedings were ended with the price undertaking offered by Chinese exporters, which undertook to respect minimum prices, normally 6 percent of the export prices. Compared to definitive anti-dumping duties, such a price undertaking did not lead to the exclusion of Chinese goods involved in anti-dumping proceedings from the Community market.

In the case of China, the EC's past practice indicated the trend of selecting an analogue country with a much higher level of economic development, with the result that a positive finding is more likely.²⁹⁷ The analogue countries extended from the United States to some developing countries. But the fact that some developing countries were unwilling to become the analogue countries in the anti-dumping proceedings concerning China was also a factor leading to this consequence. Provided that there is competition between China and some developing countries in exporting similar or same products to the developed countries, the exclusion of Chinese products in the international market through anti-dumping is favourable for those developing countries in increasing the export of their products of the same kind. In the latter part of the 1990s, more developing countries at similar developing level, such as Mexico and India, were selected as the analogue country in the anti-dumping proceedings concerning China. This seemed to indicate that the EU, while strengthening the anti-dumping measures against Chinese exporters, was becoming more careful in selecting the analogue countries. This practice may facilitate attaining two goals: regulating Chinese trade practices in order to meet domestic demands and alleviating Chinese complaints.

The removal of China from the category of the non-market economies in 1998 does not significantly improve the Chinese status in the case of anti-dumping. The Regulation (EC) No 905/98 built a 'special market economy regime' applicable in anti-dumping cases concerning Russia and China, which allows for market economy status to be granted on an individual basis to companies in China and Russia; a case-by-case approach is applied in investigations whereby exporters may apply for market economy treatment only if evidence is brought.

This special market economy regime includes five criteria.²⁹⁸ But the EU continues the traditional practice of selecting analogue countries in anti-dumping investigations in the case

²⁹⁷ Xiao Zhi Yue, p. 93.

²⁹⁸ (a) decisions of applicant firms related to prices, costs, inputs, sales, investments are made in response to market signals and without significant State interference; (b) firms have one clear set of basic accounting records independently audited in line with international accounting standards; (c) the production costs and financial situation of firms are not subject to any significant distortions carried over from the former non-market economy system; (d) firms are subject to bankruptcy and property laws which guarantee legal certainty and stability, and

of China, with the reason that ‘most of the applicant companies did not have a clear set of accounting records or did not have any accounting records at all’.²⁹⁹ Thus in most anti-dumping proceedings, the practice ‘individual anti-dumping duty for all enterprises of that country involved in the anti-dumping charges’ is still continued. However, this new regulation provides the possibility of dealing with the anti-dumping on an individual basis, which is particularly favourable to the foreign one-party investment enterprises including the European investment enterprises, for they can provide a ‘clear set of basic accounting records independently audited in line with international accounting standards’. Some Chinese enterprises began to apply for case-by-case investigation when involved in anti-dumping proceedings.

Piet Eckhout compared the percentage of anti-dumping in the case of China in all the EC/EU’s anti-dumping proceedings via statistics and concluded that China has become the principal target of EC/EU’s anti-dumping in the 1990s. From 1993 to 1995 almost half of the EC/EU’s definitive anti-dumping duties were imposed on Chinese exports. Compared with the one tenth of 1992, this should indicate that the EC imposed stricter regulations on Chinese exports.³⁰⁰

This argument can be supported by the imposition of anti-dumping duties rather than price undertakings in the case of China. In 42 anti-dumping proceedings ended with anti-dumping duties and price undertakings from 1979 to 1992, the imposition of anti-dumping duties was 52% (22 out of 42).³⁰¹ This indicates that in this period the anti-dumping punishment was relatively appropriate. Afterwards, all exported products involved in anti-dumping proceedings ended with punishments were imposed anti-dumping duties. From 1993 to 1999 thirty-three anti-dumping duties were imposed on Chinese exporters.³⁰² In contrast to this, another thirty-three anti-dumping proceedings against European exporters (mainly the former East bloc countries) as well as some exporters from the six developing countries (India, Mexico, the Philippines, South Africa, Thailand) ended with price undertakings.³⁰³ This statistic indicates that more severe punishment was imposed on Chinese exporters, and price undertaking appears no more to be applied in the case of China, at least currently.

The increase in the EU’s anti-dumping proceedings correlated with the rapid increase in foreign-investment enterprises in China in the 1990s, many of which were for export-

(e) exchange rate conversions are carried out at the market rate. Regulation (EC) No. 905/98 of the Council, 27 April, 1998, in OJL, 128, 30. 4. 98.

²⁹⁹ COM (2000) 440 final, p. 23.

³⁰⁰ <http://eiop/texte/1997-007ahtm>

³⁰¹ Xiao Zhi Yue, p. 88.

³⁰² COM (2000) 440 final, pp. 163-166.

³⁰³ COM (2000) 440 final, pp. 185-188.

proceedings, or in some sense to avoid becoming anti-dumping targets by transferring production to China, such as some investment enterprises from South Korea and Japan. Thus, a large number of anti-dumping proceedings in the 1990s were against the products of foreign-investment enterprises, including some of the European investments. The prevailing practice of selecting analogue countries in anti-dumping proceedings concerning Chinese exports had adverse impacts on foreign investors with export orientation, for the whole sector is involved in anti-dumping proceedings if any enterprises found to be dumping.

More and more principal Chinese exported labour-intensive goods, such as footwear, handbags, powdered activated carbon, and some mineral and chemical products with raw material advantage, were involved in the anti-dumping proceedings in the 1990s. Particularly striking is the fact that the number of anti-dumping proceedings against Chinese exporters in 1999 dramatically increased to 12. This seemed to be a consequence of Chinese efforts to maintain export growth through export diversification after the Asian financial crisis in 1997, in which the EU is becoming one of the principal targets of export promotion.

However, to some extent there existed a correlation between the evolution of Chinese export-promotion policies and the increase in anti-dumping proceedings in the 1990s. The new export-promotion policies promoted the entry of numerous trade entities into world market. Since many provinces have similar industrial systems consisting of enterprises producing identical manufactures, in the context that the administrative organisations seek to reduce the control on exports, it is very likely for these enterprises producing same manufactures to compete with each other in the international market. Consequently, Chinese exports have the feature both of low prices and large volume. Such export practices undoubtedly had a more adverse impact on some European industries. Therefore, in some anti-dumping cases in the late 1990s, prices and market share both were considered as material injury.³⁰⁴

Some Chinese enterprises, owing to their ignorance of the antidumping regulations and procedures or overlooking the serious consequences of the EU's practice in anti-dumping proceedings of selecting analogue countries to identify dumping, were very inactive in dealing with the proceedings. By 1994, none of Chinese enterprises involved in dumping had responded to the anti-dumping proceedings. For this reason, the central government had to intervene in the matter and issued in 1997 a document demanding that any enterprises involved in anti-dumping investigations must report to the chamber of commerce and actively

³⁰⁴ For instance, in the case of yellow phosphorus, 1999, material injury was indicated by: 1. the imports of the product concerned from the PRC having increased overall and in absolute terms of market share; 2. negative impact on the quantity sold and the level of the prices charged by the Community producer, resulting in substantial adverse effects on the overall performance, the financial situation and the employment situation of the Community industry.

respond to the anti-dumping proceedings.³⁰⁵ Relying on their professional knowledge, the chambers of commerce take on the responsibility of representing the Chinese enterprises in dealing with the anti-dumping issues. The Chinese government was also directly involved in the anti-dumping issues with the EU and some member states through official channels.

The allocation of anti-dumping proceedings concentrates on five sectors: chemical products, mineral products, machinery products, textile and light industry products, and electronic products. (See Table 5. 2) These are the sectors with the greatest export potential due to the advantages of access to raw materials, over-capacity of production and low labour cost. The anti-dumping proceedings after 1992 increased in particular in three sectors: products of mechanical engineering, textile and light industry, and consumer electronics. Compared with the cases in the former periods, more high value-added machinery and electronic manufactures had anti-dumping duties imposed on them.³⁰⁶ This tendency seemed to indicate that some Chinese exported items have begun to constitute an increasing threat to the European technological-intensive sectors, as China made great efforts to improve the export composition by increasing the export of manufactured goods, in particular machinery and electronic products. This could be demonstrated by the protracted anti-dumping proceedings against China's TV sets, one of the high-value-added Chinese manufactures with international competitiveness. The proceedings were ended with the imposition of around 45 percent definitive anti-dumping duties on the TV sets produced in China. Thus, China's TV sets have been excluded from the European market since the late 1990s.

5.3 Quantitative restrictions (QR) on non-textile exported products

The EC/EU maintained a number of QRs against its trade partners, particularly against the countries falling into the category of non-market economies. The Community has the discretion to impose QRs unilaterally on selected imports.

In conformity with the principles of the Single Market, the EC/EU unilaterally eliminated the national quantitative restrictions and established Community procedure for administrative quantitative control and uniform criteria applying to all Community importers in 1994. In the period from the 1980s to the 1990s, in terms of the requirements of the GATT/WTO to gradually lift quantitative restrictions in order to facilitate the liberalisation of world trade, the EC gradually reduced the quantitative restrictions on the imports from China in the process of

³⁰⁵ guanyu guli he ducu qiye canjia guowai fan qingxiao anjian yingsu de ruogan guiding (Some stipulations about encouraging and urging enterprises to respond to foreign anti-dumping proceedings), 10. 03, 1999.

³⁰⁶ For details of the items involved in anti-dumping charges in the 1990s, see COM (2000) 440 final, Annex O, Table 5.3.

China's accession to the GATT/WTO. In 1994 the EC/EU imposed quantitative restrictions on seven important Chinese exported products, in addition to textile products, including footwear, toys, radio receivers, gloves, glass utensils, pottery and porcelain products. Currently the EU maintains quantitative restrictions on textile products, footwear and tableware. Two of these three products (textile and footwear) are the most important Chinese products in world market. The enlargement of export of these two products can facilitate the operation of this labour-intensive industry mainly composed of small and medium-sized enterprises. It is also one industry concentrated with overseas Chinese investments and village enterprises. It plays an important role in reducing unemployment.

The primary goal of maintaining quantitative restrictions is to minimise the adverse impact on some vulnerable European industries from the imports of Chinese low-priced products. Through maintenance of quantitative restrictions, the EC seeks to maintain the prices of European products, to limit the market share of Chinese products, and to facilitate the restructuring of the small and medium-sized enterprises.³⁰⁷

The QRs are not only a defence instrument but also an approach to reinforce the EU's leverage in dealing with its trade partners. As the Commission acknowledged, the substantial improvement of Chinese market access could play a key role in exchanging the liberalisation of the existing quantitative restrictions, and this depends on whether China fulfils its promise to eliminate its quantitative restrictions on imports by 2005.³⁰⁸ The removal of quantitative restrictions should be pursued as part of an overall market opening strategy and in the context of the WTO accession negotiations.³⁰⁹

³⁰⁷ Sensitivity is the principal criterion for maintaining the quantitative restrictions on some of the imports from China. It is determined by the following elements: low price, the share of market, the scale of the European enterprises as well as their geographical concentration, the enormous export potential of the Chinese industry. Concerning price, in the case of footwear, the gap currently is 4.70 ECU/unit of Chinese products as compared to 21.13/unit of European products. The imported tableware is usually well below European prices both for porcelain and chinaware and for earthenware. Thus retaining quotas may have limited the quantity of Chinese imports and therefore may maintain the prices of European products. With regard to the market share, the share volume of imports of Chinese footwear accounts for 33.4% of all EC imports; and the tableware more than one quarter. The footwear and tableware sectors with labour-intensive character are principally constituted by small and medium enterprises and are in a difficult restructuring process, and the imports of low-priced foreign products increase the difficulties in this process and unemployment. Moreover, in the case of tableware, some Chinese producers not only copy European designs but also sell such copied products in Europe at much lower prices than the European products. In addition, the EU's exports of the products of both sectors to China are virtually nil. Owing to the above elements, the enterprises of these two sectors strongly support the maintenance of the quantitative restrictions. COM (2000) 091.

³⁰⁸ COM (2000) 091.

³⁰⁹ COM (1998) 181

5.4 Summary

From the analysis of the evolution of the EU's two principal commercial defence policy instruments, we can see the pursuit of a reconciliation between protecting its vulnerable industries facing Chinese export policy practices and fulfilling its commitments to the WTO in lifting the non-tariff barriers in the process of China's accession to the WTO. The result is two tendencies developing in parallel. First, the EU gradually decreased its quantitative restrictions on the imports from China, in particular after the launching of the WTO, but still retained this policy instrument towards some principal Chinese export manufactures in order to attain double objectives: to protect the EU's vulnerable industries and increase its leverage to obtain real access to Chinese market. Meanwhile, it strengthened the WTO-permitted trade-defence instrument, namely the anti-dumping, against Chinese export-promotion practices. The strengthening of the anti-dumping measures against the imports from China, such as the greater resort to definitive anti-dumping duties rather than price undertakings, is likely to indicate that anti-dumping has become the principal instrument to protect vulnerable European industries and discipline Chinese export-promotion practices.

The anti-dumping measures were particularly strengthened in the 1990s, when China had become the principal trade partner of the EC/EU and its trade surplus continually increased, amounting to 30 billion Ecu in 1999. In the context that the EU has lifted almost all quantitative restrictions on the imports from China but China still retains various tariff and non-tariff barriers impeding the increase in the EU's exports to China, the signification of strengthening the commercial defence measures means that the bilateral trade must be operated on the basis of reciprocity and disciplined trade practices, through the WTO rule-based policy framework to pursue sustainable trade development. Thus, the new anti-dumping measures concerning China also serve as an instrument pressing the Chinese administrative authorities to accelerate the elimination of state-trading practices, explicit and implicit, and more actively engage in disciplining Chinese exporters' practices.

The EU's practices in issue of anti-dumping against Chinese exported products are regarded by Chinese export administrative organisations as an indication that the EU still treats China as a state-trading country in the EU's external trade relations. The unilateral resort to anti-dumping measures by the EU, while promoting Chinese administrative organisations to strengthen the engagements in disciplining the exporters' practices, increases the difficulties that the Chinese government faces in dealing with increasing socio-economic issues. Thus, it

seems to be necessary for the two sides to establish a new mechanism to reduce the injuries of anti-dumping on bilateral relations after China's accession to the WTO.

6. Other approaches to facilitate the building of a common European economic policy framework in the case of China in the 1990s

6.1 The EU's global market access strategy

The EU launched its global market access strategy in 1995, almost at the same time as the WTO began to operate. The main goal of this strategy is to provide a mechanism for Community firms and industries to act against trade barriers affecting their access to third country markets. This strategy is particularly helpful for the small and medium-sized enterprises, which lack information and the capacity to deal with the third countries. The establishing of the Market Access Database provides an interactive means of communication between business and the European authorities through information collection and supply. On this basis, the EU seeks to remove barriers through bilateral consultation with the third country and the mechanism of the WTO.

The principal targets of this strategy are countries with potential market size, among which some countries are in the transition from centrally-planned to market economy and in the process of integrating into the world market, in particular the developing countries with high protectionism, such as China and India, and some former Soviet member states.³¹⁰ This strategy, with the explicit intention to remove various barriers to market access through the role of a European-scale actor (the Commission), incorporating actors possibly involved in the foreign market access according to the WTO agreements, including member states, large and small enterprises, trade companies, etc, facilitates building an external economic policy network with the Commission as the centre. Such an effort strengthens the contact between the supranational institution and actors at various sub-European levels, the small and medium-sized enterprises in particular.

³¹⁰ Annual report from the Article 133 Committee on the implementation of the EU Market Access Strategy and recommendations for the next phase, 13 September 1999. http://www.europa.eu.int/comm/mk_access

6.2 Involvement of the EC/EU in technology transfer in the case of China

As analysed in the previous chapters, pursuing technological progress is one principal goal in Chinese external economic relations, in particular in the relations with the EC/EU. The two principal goals of Chinese policies to attract foreign investments – export promotion and the replacement of imports by domestic products through technology transfer from foreign investors – are mutually associated in most cases. Foreign investments play important roles in promoting Chinese technological upgrading, managerial know-how, marketing, improvement of export-composition, etc. Usually, high-technology investments can be attracted only by granting market access. Most of the direct investments from the EC/EU belong to the latter, i.e. pursuit of market access through technology transfer and production in China.

For the technology suppliers, determining what technologies can be transferred depends on the following factors: the degree of sensitivity of the technologies, whether the receiver is an ally or a potential competitor, and whether the suppliers' interests can be protected after the technology transfer. More important, the success of the control must be based on the appropriate estimation of the technological level of the recipient country.

The sensitivity of the technologies is the determinant element of the transfer. Concerning the sensitivity of the technologies, they can be divided into three categories: military, civil and dual-use technologies. 'Dual-use' items, defined as goods and technology developed for civil uses, can be used for military applications or to produce weapons. The control on export of military and dual-use items (goods and technology) always exists. After the completion of the Single Market, the EU has strengthened its control over the transfer of dual-use technologies by adding the European level control regime above the existing member states' control regimes and established full harmonisation of some of these controls, while re-delegating all other decisions to national authorities.³¹¹ This framework serves as complementation to that of the EU member states.

Dual-used items are or may be intended, in their entirety or in part, for use in connection with the development, production, handling, operation, maintenance, storage, detection, identification or dissemination of chemical, biological or nuclear weapons or the development, production, maintenance or storage of missiles capable of delivering such weapons.³¹² Such a definition is directly connected with the EU's commitments according international agreements concerning proliferation of nuclear, chemical and biological weapons. It

³¹¹ Regulation 3381/94 EC, COM (98) 257 final.

³¹² Article 4, *ibid.*

obviously is a very strict definition, and does not play important roles in limiting the European enterprises to export their normal military technologies.

According to the EU's dual-use technological transfer regime, it is only a few 'friendly' countries, including Japan and the United States and some central and eastern European countries as candidates for EU membership, to which the dual-use products or technologies can be freely exported. Embargoes on the export of the dual-use products are imposed on the 'country of concern'. The EU seemingly seeks to give a stricter definition to the countries of concern, namely the countries under international embargo, such as Iraq,³¹³ and to narrow the number of such countries. As the export control regime is based on a 'mutual recognition' approach of differing national policies rather than on effective development of a common policy, it relies to a very large extent on administrative cooperation between national authorities to bridge the gaps between member states' policies and procedures. However, so far it has not succeeded in creating an effective common export control regime and the result of this control is dissatisfying.³¹⁴ It indicates that with regard to some external economic issues falling into the CFSP domains, the Community competence is still very limited. In addition, the control of such dual-use items seems marginal importance in the case of China.

In the case of China, the foreign-investment policy strategy with the emphasis on export promotion and technological upgrading has greatly promoted technological progress. The new co-operation with Moscow in military technologies greatly reduced Chinese dependence on Western military technologies, with the consequence that China's dependence on defence-related technological transfer from the West has greatly reduced. On the other hand, concerning civil and military technologies, the government adopts various policy instruments to accelerate technologic upgrading and innovations, such as preferential financing, concentration resources on the research of some important technologies. Thus, China's dependence on imports and transfer of foreign technologies is relatively limited.

Undoubtedly, the EU maintained some control on the exports to China.³¹⁵ Such control is directly related to the promotion or limitation of European exports to and investments in China. In a context where China has made great progress in technological upgrading and there is increasing competition between European enterprises, between EU member states and between European and other countries, what is more important for the European enterprises is what items they can export to China. In addition, China is not a pure recipient of advanced technologies. In some areas of technologies, particularly in the areas of aerospace and biology,

³¹³ Council Regulation No. 3381/94, OJL367 of 31.12. 94.

³¹⁴ COM (1998) 258.

³¹⁵ Kapur (1985), p. 80.

it also has innovations. The launching of co-operation between the EU and China in aerospace in the mid-1990s appears to reveal the marginal extent of EU's control on technology transfer in the case of China.

Thus, the emphasis of the EU appears to be placed on the long-term consequence of the technology transfer, namely that the technology transfer will create a potential competitor in the long-term prospect.³¹⁶ Taking the example of intellectual property rights, according to one study, 78 percent of the companies interviewed are concerned about protection of their intellectual property.³¹⁷ In this respect, taking into account that most European investment enterprises concentrate on manufacturing sectors, chemicals and pharmaceuticals, mechanical engineering and telecommunications in particular, and most of them are large or transnational companies, it can be expected that the pressure from European investors to realise an efficient European engagement in China to protect their interests is by no means marginal. The conclusion between the EU and China of agreements on protection of European intellectual property rights means that the Europeans enjoy the same treatment as that granted to the Americans. The EU-China Intellectual Property Rights Co-operation Programme is only one case indicating the shift in the efforts from agreement to practice to help the Chinese government realise its commitments in this respect.

6.3 Opportunity-oriented co-operation in basic scientific research and technological development

China has been defined as an 'emerging economy' by the EU, and the co-operation with China in basic scientific research and technological development is 'opportunity-oriented'. This means an arrangement to create a web of scientific partnership in targeted areas, both for mutual benefit and as an important step in the establishment of new structured relationships with countries of particular strategic importance for the EU.³¹⁸ These opportunity-oriented cooperative initiatives aim at high-technology sectors conducive to the promotion of European science and technology innovation in the emerging markets. The bilateral agreement of co-operation in science and technology of 1998 stipulate reciprocal participation in research entities of each side, joint organisation of scientific seminars, conferences, symposia and workshops, concerted actions, exchanges and sharing of equipment and materials. The Commission further identified the following sectors as sectors of mutual interest for

³¹⁶ David Bennett *et al*, 'China and European Economic Security: Study on Medium to Long Term Impact of Technology Transfer to China', (prepared for European Commission Directorate General I), July 1999.

³¹⁷ *Ibid*.

³¹⁸ COM (1996) 344.

technology co-operation with China: non-nuclear energy, environmental protection, life sciences, material sciences, information and communication technologies. These identified six sectors reveal the idea to co-ordinate the co-operation programmes with Chinese high priorities indicated by the China's 863 plan.³¹⁹ This plan aims at developing advanced technologies in the domains key to China's future developments. In the period of the eighth and ninth five-year plans fifty important research subjects were included in this plan. To attain the goals set in this plan, the government concentrates financing on establishing national research and development bases and laboratories. The scientific and technological cooperation agreement concluded in 2000 between the two parties further strengthened protection of intellectual property by jointly developing a technology management plan (TMP) mechanism.³²⁰

6.4 Constructive engagements for long-term shared interests

In the 1990s the EU strengthened its constructive engagements in China, indicated not only by the increase of financing but also by a variety of programmes. In the first respect, the financing of the programmes in the period 1996-98 accounted for 11 percent of the co-operation budget in Asia (contrast to 5.8 % in the period from 1991-95).³²¹

Unlike the EU's involvement in other regions with the principal goal of reducing poverty, the main intention of its engagements in China seems to shift from alleviating poverty to facilitating the attainment of long-term European goals, namely engaging China further in the international community through an upgraded political dialogue and launching various programmes aiming at supporting China's continued process of economic and social reforms and transition to an open society based upon the rule of law, integrating China further into the world economy, and raising the EU's profile in China. Thus, the bilateral relationship has been transformed by these programmes into one with multiple goals and more structured contacts.

Such new European initiatives in constructive engagements can mainly be regarded as a European response to the developments in China, but the primary objective is to promote long-term European interests in China, economic interests in particular. This is indicated by the selection of programmes for such engagements.

³¹⁹ This plan includes eight technological domains: biotechnology, aerospace, information, lasers, automation, energy, new materials, and ocean technologies. The details of this plan can be obtained at <http://www.863.org.cn>

³²⁰ Agreement for scientific and technological cooperation between the EC and the PRC, 2000, annex: intellectual property rights.

³²¹ European Commission/ODI database 1999.

It also seeks to combine its concern of environmental degradation, poverty reduction, human rights, minorities in China, etc, with China's programmes for inland developments. The EU's programmes launched in the latter part of the 1990s (see Table 5. 3) revealed that the EU seeks to focus on supporting the overall reform process. The emphasis of these programmes was particularly put on human resources development. They cover basic education, environmental protection, technical assistance and expertise, transferring of know-how and training. They sought to co-ordinate with Chinese efforts in the domains with shared interests, such as associating pursuit of sustainable economic growth with poverty alleviation in minority-concentrated Chinese inland regions (Qinghai, Ningxia and Yunnan) through certain programmes, and the minorities involved in these programs include Tibetan, Hui and Yi peoples.

The programmes of co-operation in education reveal a wide variety of goals, including an increase of the understanding of Europe and European integration; exchanging of students; improving of managerial know-how in the enterprises; the training in economic policy making and institutions, law, public administration, urban and regional policy, environmental planning, education, social security systems, health care, etc to improve the civil administration; and to contribute direct, practical relevance and applications of European studies to China's development and systemic reform efforts, through short training workshops to disseminate European experience.

These programmes indicate the influences of extensive European interests and public demands. They also appear to show the Community's ambition to raise its profile and its intention to facilitate solving certain urgent issues of dispute in the bilateral relations. But it is the business interests that dominate the EU's initiatives in launching these programmes. Undoubtedly, the best approach to promote European economic interests in China is to maintain China's sustained economic growth and social stability while further integrating China into the world economy. For this purpose, the EU's programmes so far mainly concentrate on capacity building (mainly concerning the Chinese administrative organisations) by providing technical assistance with the main purpose to promote the Chinese government to fulfil its WTO obligations.

One principal goal of these programmes is to support China's preparations for its accession to the WTO and its full compliance with the WTO rules. The EU's engagements in these respects mainly associated with law, regulation and market access conditions; and the emphasis was placed on training personnel at the Chinese administration level engaged in the preparation and administration of regulations, particularly those relevant to WTO obligations,

procedures for complying with notification requirements, operation of the WTO disputes system and procedures for implementation of WTO decisions.³²² In addition to the EU-China Intellectual Property Rights Co-operation Program, two of the EU's programmes relate to this respect. The training programmes in transparency of public procurement extend to all personnel involved in the process of public procurement, including the legislators, executors, procurement officials, and bidders. In addition, through the co-operation programme in statistics, the EU seeks not only to strengthen the capacity of the Chinese administration to provide accurate, timely and internationally comparable statistical data to enable policy makers to monitor the development of the economy, but also facilitate solving the issue of the divergence between the two sides relating to the bilateral trade. In summary, the strategic approach is to create a durable and conducive environment in terms of WTO rules and norms in order to realise real market access both for goods and for investments.

A few EU programmes also cautiously touch the issues within the competence of the CFSP, such as the improvement of human rights in China; but the emphasis is placed on 'good governance', namely to promote progress in this respect through 'rule of law'. The EU's engagements are mainly confined to technical assistance, such as training village governance to support Chinese democratisation 'beginning from the grass-roots level', and the co-operation focuses on training Chinese legal professionals, including Chinese lawyers, judges and prosecutors, administrators, arbitrators, legislators and opinion forming academics, as well as a large number of small legal projects. A constructive approach is demonstrated by incorporating the engagements in the development co-operation policy framework and through dialogues at the expert level.

7 Conclusion: towards a WTO-rule based economic policy framework

As the new strategy towards Asia clearly stated that the principal motive of the EU to extend its involvement in Asia is 'in the first instance primarily economic'.³²³ The policy emphasis is laid on de facto market access for both trade in goods and services and a conducive

³²² For instance, the EU-China Intellectual Property Rights Cooperation Programme aims at supporting the Chinese government to develop a modern and effective system for the protection of intellectual property corresponding to international standards, including administrative and legal structures, the development of a clear understanding amongst policy-makers, government officials, industrialists and other intellectual property rights practitioners. Areas of this programme fall under three main categories: providing legal expertise for the development of legislation, institution strengthening by streamlining systems and procedures with modern management methods and improving intellectual property rights awareness amongst intellectual property rights institutions and consumers.

³²³ COM (1994) 314 final.

environment for trading and investment. The co-operation is particularly focussed on the areas where the co-operation will be beneficial to Community interests.³²⁴

The evolution of the EU's economic policies towards China revealed that the adjustments were in accordance with the changing situational contexts both in China and in Europe. It can be divided into two phases, with 1990 as the dividing line. In the 1990s, it can be concluded that the idea of 'fair trade' has dominated the EU's trade policies towards China and reciprocity has replaced unilateral preference policy practices.

For the Chinese government, the key concern in the negotiation of China's accession to the WTO was how to minimise the adverse socio-economic impacts brought about by the accession, as the assumption of WTO obligations inevitably touches more difficult domestic issues arising in the 1990s. Thus the EU's principal concern is to obtain real market access after China's accession, particularly in the context of a continually increasing deficit in the trade with China, but this demand can be met only by continually promoting China's economic liberalisation and alleviating the difficulties in the transition period through selected preferential policies towards China. The EU's policies seemingly indicate the pursuit of the reconciliation between the pursuit of urgent economic benefits and the establishment of long-term institutionalised stable policy framework in terms of the WTO rules. China's accession to the WTO must be on 'commercially sound conditions', but they can be implemented gradually and step by step in line with China's domestic reform programme.³²⁵ The tendency of the EU's policies towards China is aimed at building a WTO rule-based bilateral economic relationship. The negotiations with China on its accession to the WTO are 'to iron out such barriers (tariff and non-tariff) and help create an open Chinese economy that benefits European and global interests alike'.³²⁶

³²⁴ The co-operation areas include business co-operation between European companies and their Asian counterparts, better links with European business associations and chambers of commerce by the formation of a business association at the European level; co-operation in the fields of science and technology and research and development, particularly in the advanced fields such as information and communication technologies, industrial, and materials technologies and biotechnology, the establishment of European technology centres especially in key sectors where Europe has a comparative advantage; support for trade promotion, to facilitate European agricultural products, particularly processed ones, to enter Asian markets, and co-operation in the field of environment.

³²⁵ <http://europa.eu.int/comm/trade/bilateral/china/faqs.htm>

³²⁶ Under the WTO principles (transparency, national treatment and non-discrimination), the EU demands to offer real market access for industrial and agricultural goods by cutting tariffs significantly and adhering to the Information Technology Agreement and by removing all non-tariff barriers, to remove the current monopolies on foreign trade and enable all Chinese or foreign nationals to engage in foreign trade; to provide substantial opening of China's services market in distribution, telecommunications, financial services, professional services, tourism, travel and medical services; to remove all restrictions on the legal form of establishment, lift geographic restrictions and those on the scope of permitted activity, and remove pre-establishment conditions, as well as export performance requirements and export subsidies; to rapidly implement the WTO TRIPS Agreement and full enforcement and protection of intellectual property rights; to establish a transparent, open and competitive procurement regime so as to secure China's membership of the WTO Agreement on Government Procurement

The 'bilateral market-access package' is the most efficient approach to pursue reciprocal market access and adopt various forms of retaliation. Around China's accession to the WTO, the EU seeks to build a new policy framework with an appropriate balance of technical assistance, enforcement and multilateral monitoring. The emphasis of the EU's technical assistance is placed on the preparations for the WTO accession, in particular via the amendment of Chinese domestic laws and regulations in order to construct a sound and transparent regulatory framework for investment and via better enforcement of Chinese regulations on intellectual property rights, and to develop a specific post-accession dialogue with China to ensure the implementation of its WTO commitments both during the phasing-in period and beyond. Obviously, the primary goal of the technical assistance is to obtain real permanent market access through the EU's engagement in China's institutional transformation around its WTO accession. Such a policy behaviour, lacking the feature of hegemony, should be more easily acceptable for China.

The published details of the treaty on China's accession to the WTO seem to indicate that the EU, as the single actor representing extensive European interests, had to incorporate the demands from each level of the European economic interests into a package in a multi-level game in the negotiation with China. The demands came from the member states, regional and sectoral interests, in particular the EU Southern countries and some sectors whose importance in economic growth and employment both at the state and regional levels is never marginal; but exports of the products in these sectors are actually impeded by the high Chinese import-tariff rates. Nevertheless, the reduction of import tariffs on these products, with a few exceptions, does not have substantial impacts on the Chinese sectors concerned. For instance, its concessions on reduction of import tariffs concerning the processed European agricultural products, such as butter, cheese, and so on, compared to the concessions on the import of large volumes of corn, wheat, meat and so on from America, seem to have only a marginal adverse impact on the agricultural sector.

The treaty requirements focused on the tariff-reduction of some products that are competitive but have difficulties entering the Chinese market due to the high import tariffs, such as personal cars, processed agricultural products, clothing, building materials, etc. In addition, the treaty sought to help the sectors with strong European competitiveness, such as services, to enter China. Obviously, increase in export of most of these products has not only sectoral importance, but also important significations for some regions and member states. For

as part of the WTO accession package, for China has the largest procurement market in the world and failure to obtain access to that market would significantly reduce the overall value of the market access package; and to join the WTO-related Civil Aircraft Code.

instance, the increase in the export of agricultural products has important signification for the EU Southern countries which normally have fewer economic exchanges with China. The reduction of the import tariff on personal cars is perhaps most helpful for the automobile industries in other EU countries, when the co-operations between China and Europe in this sector are mainly concentrated on German automobile industries. Naturally, the EU's requirements in these respects seemed to be less difficult for China to accept, for some products have long since entered the Chinese market, but the high import tariff encourages smuggling and the high prices of these products in the Chinese market limits their consumption. Undoubtedly, the EU's success in dealing with China on these issues relates not only to the expansion of the European interests in China, but also to the status of the EU institutions, in particular the Commission and the Council.

Concerning the market-access conditions of some 'infant industries', e.g. the sectors of automobiles, telecommunications, and services, China does not make more concessions than it did in the treaty with the United States. This seemed to reveal the influence of the Chinese 'infant industries' on decision making, whose interests are represented and communicated by some existing organisations within the central administrative institutions. Taking account of the fact that the EU has been the late investor in services sectors and the important role played by services in promoting investments in manufacturing sectors, China's initial issuing of a few certificates to permit the European insurance sector to enter China beforehand can be regarded as a positive arrangement contributing to obtaining the support for this deal on each side and to promoting the approval of this treaty both by EU institutions and by member states. The outcome of the negotiation concerning market access to China's 'infant industries' appeared to be a result of 'two-level' games. China partially satisfies the demands of the EU, in the meantime it also seeks to provide some protection of the interests of its infant industries. However, concerning trade defence instruments, the EU managed to maintain its specific procedures for dealing with cases of alleged dumping by Chinese exporters available for up to fifteen years after China enters the WTO, and the China-specific safeguard provision will be available for up to twelve years after China's accession. And a further sector specific mechanism provides added protection in the textile field until 2008.³²⁷ Such derogations from the WTO rules might further protect European industrial sectors from the expectable adverse impacts after China's accession. Thus, in a period after China's accession to the WTO, it will

³²⁷ For a relatively detailed content of this treaty, see 'Proposal for a Council Decision Establishing the Community Position within the Ministerial Conference Set up by the Agreement establishing the WTO on the Accession of the PRC to the WTO', COM (2001) 517, final, 19.9.2001.

be still implicitly treated by the EU as a 'non-market economy' concerning some issues in the bilateral trade.

VI. General Conclusion

As the title indicates, this dissertation provides an analysis of the evolution of the relations between China and the EC/EU from the mid-1970s down to the present. Though the two parties began their contacts with fundamentally different goals in mind, the pursuit of maximum benefits has always been the primary goal in the extending and deepening interdependence, so much so that they are now beginning to build a new bilateral relationship framework to facilitate co-operation in more extensive areas of mutual interest and common concern.

Through a description of the policy practices, analysis of the policy goals and isolation of the principal factors behind the policy changes in different external and domestic contexts, it can be concluded – despite the fact that China’s original idea in establishing official relations with the EC had nothing to do with the European reality – that the launch of market-oriented economic reforms and the Open Policy set new goals for and changed the direction of the development of bilateral relations. In three different periods and different Chinese domestic contexts, the relations with the EC/EU had different implications, but the pursuit of maximum economic benefits has always been one of the principal policy goals. In order to attain this unchanging objective, new areas of co-operation were opened. Increased demands emerging in the course of deepening interdependence not only provided the principal dynamics for policy evolution and the broadening of policy scope, but also gave new meaning to the bilateral relations. In this context, the relations with the EC/EU took on new implications, but such new implications have mainly been related to China’s domestic developments.

The successful operation of China’s new foreign policies, which are mainly designed to suit the changing Chinese domestic demands and are concentrated on both export promotion and attracting foreign investments, has changed China’s relative position in the bilateral relations and increasingly influenced the interests of EU subsystemic actors, in particular those of economic interest groups. Consequently, the EU as one of China’s principal economic partners has to adjust its policies and broaden its policy scopes both as European reactions to the changing external economic policies of China and as responses to the increasing demands in Europe and developments in China at a time when Europeans are becoming so deeply involved in this country. In other words, although the primary dynamics for this change came from China, the new demands came mainly from Europe, in particular from economic interest groups there. Demands arise from the continually deepening and extending interdependence, in which the line of foreign and domestic policies are blurred. The EC/EU

began to play a more active role in Chinese developments in the 1990s, mainly in terms of facilitating the pursuit of long-term goals conducive to European economic interests in particular. The policies of each partner towards the other not only respond to own internal demands but also relate increasingly to the internal socio-economic policies of the other. As a result of this, the two parties have to set new goals, redefine the concrete contents of the bilateral relations and build new mechanisms in order to expedite the reciprocal effects and ensure mutual interests. The completion of the Single Market and the shift from a Community to a Union created new institutional mechanisms facilitating policy adjustments, goal incorporation, and a broadening of policy scopes. Co-operation and pursuit of mutual benefits are the main tendency in the bilateral relations. The positive outcomes from co-operation between the two sides are striking, as indicated by the analysis in the previous chapters.

The first part of this dissertation shows the causes leading to China's perplexing policy practice towards the EC in the 1970s in a specific domestic and external context. It was an unexpectedly positive attitude towards an unknown partner (the EC) due to a misinterpretation of the implications of European integration in China's international policy strategic thinking. It also analyses the new external and domestic contexts that led to the EC shifting from a potential political ally to a principal economic partner in the new Chinese foreign policy strategy, which in the post-Mao period has mainly aimed at the attainment of domestic goals. The analysis reveals that, in a specific external and internal situation, a combination of ideological bias, inadequate information, misperception of European integration and an extremely high concentration of decision-making power in a single individual, as well as factional conflicts led to such a perplexing phenomenon that the relations with the EC were related to the ensuring of China's external security and its ambition to oppose hegemony. It was in this specific Chinese context that a European preference was created in China's external relations. It is also argued that new domestic demands in the post-Mao period drove China's principal external policy goals and redefined the actual importance of the EC in China's external relations. The second part reveals the connections between the changes in China's general external economic policies and its policy practices towards the EC/EU, with an effort being made to fully engage the European factor under the general Open Policy with the principal purpose of contributing to domestic developments. When the emphasis of the Open Policy began to shift from export promotion to the pursuit of more extensive socio-economic objectives in the transition period and the attainment of sustainable economic development, the EU's importance in China's new

development strategy was boosted accordingly. The third part describes how the EC/EU sought to strike a balance in selecting appropriate policy measures to attain two principal goals in different European and Chinese contexts and in different periods of the bilateral relations: promoting and protecting European economic interests in China, and creating a better environment for promoting the bilateral relations by playing an increasingly important role in helping China to accelerate its integration into the world economy and to alleviate difficulties in the transition period through constructive engagements.

The evolution of the bilateral relationship demonstrates its specific features in the external relations of each of the parties. The fundamental divergence between the objectives pursued by the two parties when they began their contacts – China was explicitly looking for a political ally and the EC for a trade partner – meant that each needed to find new areas of broad-based shared interest in order to develop the bilateral relations. Mao's hope of creating a multipolar world system through the emergence of a third force, and his idea of an integrated Europe as a potential counterforce against hegemony brought a European preference in China's external relations. Currently, his idea might still be of some importance, but it has nothing to do with the principal areas of issue in which the two parties have the largest shared interests. The Chinese leadership in the post-Mao period has had to distinguish between strategic considerations for the future and concrete policies designed to secure actual maximum benefits in the present. As the domestic context and the main policy goals changed – the pursuit of economic growth edging out consideration of coping with the hegemony and the establishment of economic interdependence edging out the making of political alliances – So China found areas in which it has long-term interests and identified new approaches in pursuit of them. The status of the EC/EU in China's external relations thus shifted from being a counterforce against hegemony to being a principal economic partner, facilitating the attainment of various domestic goals. In short, the European preference in China's external relations has been retained, but its actual significance for Chinese external relations has varied in different domestic contexts and in different periods. Generally, its importance in promoting China's economic growth has not decreased but become increasingly significant.

At a time when foreign economic policies have become one of the principal means of solving domestic socio-economic issues, the pursuit of maximum economic benefits has furnished the primary dynamics for China to adjust its policies towards the EC/EU. Liberalisation of trade and investment regimes is the tendency, but the pace and extent of compliance with international regimes are mainly driven by changing domestic factors. Domestic rather than

external constraints have become the primary factors affecting the setting of policy goals and policy implementation towards the EC/EU.

Faced with increasing adverse factors affecting social stability and economic growth in the radical socio-economic transition period, the Chinese government has to concentrate most of its resources on coping with the domestic socio-economic issues, while making every effort to maintain high economic growth in order to alleviate arising difficulties. As indicated for the past two decades, it has sought to limit its involvement in international issues to those directly related to its internal developments, sovereignty and territorial integrity. Thus, on most issues of the EU's current concern falling within its Common Foreign and Security Policy, cooperation between the two parties mainly relies on whether and to what extent the issues are of common concern. Despite the fact that China has always supported a European role in some international issues, with the implicit goal of weakening American dominance and facilitating the emergence of a multipolar international system after the end of the Cold War and the collapse of the former Soviet Union, its actual policies towards the EU will continue to be subject to attainment of the principal goal of pursuing high economic growth, i.e. it will continue to rely on current policies promoting trade with and attracting investments from Europe; however, the policies and their implementation will be more transparent and more compliant with WTO rules after China's accession.³²⁸

In contrast to China, the EC/EU has a permanent primary policy goal – the pursuit of maximum economic benefits through a variety of policy instruments on a European scale within the framework of the Common Commercial Policy. It overestimated the potential of the Chinese market and underestimated the difficulties in gaining access to this market. Moreover, it did not foresee various new problems in the bilateral relations posed by the developments in China during the 1980s and the 1990s. To develop relations with China is for the EU both an opportunity and a challenge. China has some special features. It is one of the markets with the greatest potential for European products, an important partner on some important international issues, but at the same time a potential economic competitor. It is in a difficult transition period and various adverse domestic factors affecting the social stability and economic growth might impede its process of integration into the world economy. European economic interests can be promoted and protected only on condition of maintaining

³²⁸ The principal objective of this dissertation is to make a systematic study of the evolution of the relations between China and the EC/EU from the mid-1970s down to China's accession to the WTO in 2002. The material for this study relates to policies China and the EC/EU pursued in this period. Many of the laws and regulations will be abandoned or revised after China's accession to the WTO if they are non-compliant with the WTO norms and rules. Indeed, the Chinese central government and local governments have begun this work. By the end of 2002 the State Council had abolished 150 laws and regulations, while the central administrative organisations had abolished or revised 1100 regulations.

China's internal stability and high economic growth. While promoting China's further integration into the world economy, the EU has to avoid confrontations with China on some sensitive issues. Thus, the EU seeks to appropriately incorporate some policy goals, such as environmental protection, human rights, etc, into the framework of its trade and development policies towards China.

The evolution of its policies towards China indicates that it has always endeavoured to preserve a delicate balance between two principal goals in its relations with China: promoting and protecting various European economic interests by encouraging Chinese economic liberalisation and establishing a WTO rule-based bilateral economic relationship on the one hand, and on the other seeking to maintain friendly relations with this increasingly important partner through constructive engagements in China's internal developments, thereby helping the Chinese government to alleviate various difficulties in the transition period. While playing double roles of liberal and of protectionist on some trade issues, the EU has to play an other role as co-operative constructor in China's transition period.

The incorporation of multiple goals into the EU's applicable policy instruments and constructive engagements may be helpful in meeting various interest demands and obtaining extensive support in Europe for its China policy. Its constructive engagements in this aspect in fact expand the Community's competence in an increasing number of grey areas. The policy adjustments and policy-scope broadening indicate that the EU's trade policies towards China generally tended towards liberalisation while strengthening disciplining measures; moreover, the approaches and extent of its engagements in the CFSP domains were mainly defined by economic interests. Consequently, whereas in other cases the EU's economic policies became increasingly politicised, in the case of China they appeared to become more 'commercialised', or at least less politicised than in other cases. Such a commercialisation of the EU's policies towards China seems an appropriate choice in the two-level games, both to suit the specific features in the case of China and to meet various interest demands by the actors at sub-European levels.

As analysed in the previous chapters, despite the fact that the two parties have identified areas of common interests so that cooperation in these areas is the main tendency, the policy goals and approaches of each party in developing the bilateral relations are not always harmonious. China has shifted from being a recipient to a potential competitor. Domestic constraints determined both the policy goals and approaches. On the one hand, China's foreign economic institutions are still caught between mercantilism and liberalisation in the transition period, for all that the general tendency is towards liberalisation. On the other hand, faced with China's

export-promoting policies the EU's trade policy towards China is caught between liberalisation and protectionism.

China strongly demands its major trade partners remove all discriminatory commercial defence measures against its exports when it is certain that it has gone far enough in the market-oriented reforms and market opening. Undoubtedly, with regard to reduction of various trade barriers, in particular the reduction of import tariffs, China has undoubtedly made substantial progress. Despite various restrictions, its preferential policies towards foreign investments have been attractive. It is also a potential market for foreign products. Nevertheless, the evolution of China's external economic policies has demonstrated that without its accession to the WTO, it is questionable whether the long-term interests of its foreign economic partners can be ensured and whether China will actually become one of the major markets for European products. This is not completely determined by China's economic growth, even though it is the primary precondition.

As one of China's main economic partners, the EU, faced with China's efficient export-promoting and foreign-investment policies, has had to strengthen some commercial defence measures, such as anti-dumping, against Chinese manufactures, despite the fact that it has made substantial progress in reducing quantitative restrictions on imports from China. This has had adverse impacts on Chinese efforts to restructure domestic industries, particularly in relation to certain sectors characterised both by production over-capacity and by international competitiveness. Undoubtedly, such protectionist policy behaviour cannot enhance the EU's profile in China. Therefore, placing the bilateral economic exchanges under WTO governance seems the sole appropriate option for ensuring mutual economic interests, given that both parties want to realise real market access in a more transparent and conducive WTO rule-based framework.

After China's accession to the WTO, a large part of the bilateral economic exchanges will be placed under WTO governance. China will obtain better conditions for promotion of its exports and is obliged, in return, to provide WTO rule-based conditions for foreign investments. Some European products will be able to enter China more easily due to a substantial reduction in tariffs and some non-tariff barriers, and the interests of European investors will be better protected under a relatively more transparent and uniformed legal framework with regard to foreign investments. It is also possible that some Chinese enterprises with international competitiveness will be encouraged to invest in Europe, particularly after the East enlargement. However, the WTO regime cannot cover all domains of bilateral economic exchanges. It is still evolving, and the efficiency of its mechanisms for

solving trade disputes as well as other issues in the bilateral economic relations has yet to be tested. Moreover, the building of a more transparent legal framework is also a process of learning. Foreign constructive engagements might shorten this process and facilitate solving some problems arising in the bilateral relations.

In addition to the issues in bilateral trade, at least two problems are currently emerging in the bilateral relations. On the one hand, after the EC has transformed to the EU, i.e. it is in the transition from an economic power to a mixed entity of economic power/civil constructor/potential political power, its role in the world will largely be defined by its relations with other important international actors, among them China. More concretely, its role in the world will largely rely on its pursuit of common understandings with other major international actors in some areas of issue involving shared interests. On the other hand, the importance of the bilateral relationship might actually be 'degraded' in China's external policy strategy, for most of the contents of current bilateral relations, which are concentrated on economic exchanges, will be confined to the WTO mechanisms. In addition, in the process of market-oriented economic institutional reforms and in the aftermath of China's accession to the WTO, some central administrative organisations currently handling the relations with the EU might be disorganised. Without any doubt, as two emerging important actors on the world stage, the EU and China need to strengthen their contacts and co-operation. But the existing Community-China relationship framework seems inappropriate to this end. More concretely, what is called for is an additional framework for developing the bilateral relations, a framework between the 'Union' and China, in parallel to that between the 'Community' and China – in other words, a new relationship framework between the 'Union-Community' and China. Such a new framework would promote co-operation to be expanded into more areas with a view to resolving the existing and emerging issues, strengthening bilateral contacts, promoting mutual understanding and providing a new dynamic in developing bilateral relations. So how is this new framework of the bilateral relations shaping up, given that it must help resolve the existing issues, strengthen co-operation and facilitate future developments in the bilateral relations?

The policy strategy of building a comprehensive partnership with China, as formulated by the Commission in 1998, can be regarded as signalling the beginning of efforts in this direction through European initiatives. Its primary goal is to find a new way to develop the bilateral relations in the transformed Chinese and European contexts.³²⁹ The core of this strategy is to accelerate China's integration into the world economy and facilitate its smooth transition in

³²⁹ COM (1998) 181. final, *Building a Comprehensive Partnership with China*.

such a way as to promote its continuing economic liberalisation. This is the essential precondition for ensuring permanent European economic interests. According to this strategy, the EU's 'comprehensive engagements' in China's domestic developments has two mutually complementary parts: to strengthen constructive engagements in China's domestic developments and to promote the bilateral relations by quantitatively and qualitatively changing interactions and communications between them. The approaches include institutionalisation of the EU-China political dialogue by the annual summits ranging from the head of state/government level to the expert level. Concerning some sensitive issues with divergent or even conflicting positions, such as human rights, the EU seeks to deal with them by a 'positive approach', namely that goals be acceptable by China (supporting China's transition to an open society based on the rule of law and respect for human rights) and that engagement be limited to technical assistance (a combination of EU-China human rights dialogue without any pre-conditions and specific co-operation projects). Such a strategy of co-operation rather than confrontation can be more easily accepted by China and yet win extensive support in Europe. The continual broadening of dialogues between the two parties at various levels, in particular the institutionalised dialogues between the highest leaders of the parties, will facilitate the solving of existing issues in the bilateral relations, even as it deepens mutual understanding and promotes the possibility of cooperation on some important international issues of common concern. Through constructive engagement, the EU seeks to play a positive and active role in China transition process. Such positive European approaches can deepen mutual understanding and promote the pursuit of cooperation between the two parties.

This new strategy and the new institutional arrangements governing the bilateral relations appear to show that the EU has formulated a three-track strategy in developing its relations with China: a WTO rule-based bilateral economic exchange framework, European constructive engagement in the developments in China, and political dialogues at various levels of both sides. It seems to have been concluded that a comprehensive partnership also means a comprehensive involvement by various actors on both sides in the bilateral relations. Undoubtedly, it is a forward-looking policy strategy and its concrete details and emphases can vary with the passing of time and be influenced to different extent by various international and domestic factors, but it seems to indicate the beginning of a new period of the bilateral relations – the beginning of building a new and more structured relationship framework.

Some positive developments have appeared in this new bilateral relationship framework. In the annual EU-China summit, the highest leaders of the two parties directly exchange their

views on some important international issues concerning international security and regional stability, such as issues in the Middle East, the Indian-Pakistan conflicts, the process of reconciliation on the Korean peninsula, etc. The functional leaders seek to enlarge cooperation in more areas of shared interest and to facilitate resolving some issues in this new framework. These new developments seem to provide an optimistic perspective for the development of the bilateral relations.

VII Tables:

Table 3.1 *China's Foreign Trade, 1978-2001 (US\$ billions)*

Year	Exports	Imports	Total	Balance
1978	9.75	10.89	20.64	-1.14
1979	13.66	15.68	29.34	-2.02
1980	18.12	20.02	38.14	-1.90
1981	22.01	22.02	44.03	-0.10
1982	22.32	19.29	41.61	+3.03
1983	22.23	21.39	43.62	+0.84
1984	26.14	27.41	53.55	-1.27
1985	27.35	42.25	69.60	-14.90
1986	30.94	42.91	73.85	-11.97
1987	39.44	43.21	82.65	-3.77
1988	47.54	55.25	102.79	-7.71
1989	52.54	59.14	111.68	-6.60
1990	62.09	53.35	115.44	+8.75
1991	71.84	63.79	135.63	+8.05
1992	85.00	80.61	165.61	+4.39
1993	91.74	103.96	195.70	-12.22
1994	121.01	115.61	236.62	+4.40
1995	148.78	132.08	280.86	+16.70
1996	151.05	138.83	289.88	+12.22
1997	182.70	142.36	325.06	+40.34
1998	183.80	140.20	324.00	+43.60
1999	194.90	165.80	360.70	+29.10
2000	249.20	225.09	474.30	+24.11
2001	266.15	243.61	509.76	+22.54

Sources: For the years 1978 to 1992, MOFTEC, *Zhongguo Duiwai Jingji Maoyi Nianjian (Yearbook of China's Foreign Economy and Trade, various years)*. For the years 1998 and 1999, the author collected data from the annual publication of Chinese economic and social development issued by the State Statistical Administration. For the years 2000 and 2001, <http://www.moftec.gov.cn>

Table 3.2 *China's export Composition, 1980-1997*

Year	Value of primary products (US\$billion)	Value of manufactured industrial products (US\$ billion)	Value of export (US\$ billion)
1980	9.114	9.005	18.119
1985	13.828	13.522	27.350
1986	11.272	19.670	30.942
1987	13.231	26.206	39.437
1988	14.406	33.110	47.516
1989	15.078	37.460	52.538
1990	15.886	46.205	62.091
1991	16.145	55.698	71.843
1992	17.050	67.948	84.998
1993	16.666	75.078	91.744
1994	19.708	101.298	121.006
1995	21.485	127.295	148.780
1996	21.925	129.123	151.048
1997	23.930	158.767	182.687

Sources: MOFTEC, *Yearbook for Chinese Foreign Economy and Trade* (various years)

Table 3.3 *Foreign Direct Investments in China, 1979—2001, utilised capital (US \$ billion)*

79-82	83	84	85	86	87	88	89	90	91	92
1.77	0.92	1.42	1.96	2.25	2.65	3.74	3.77	3.41	4.73	11.00
93	94	95	96	97	98	99	2000	2001		
27.52	33.79	37.70	24.56	42.28	45.58	40.40	40.77	38.82	Total: 371.68	

Sources: *Yearbook of Chinese Statistics*, (various years).

Table 4.1 *EC/EU Trade with China, 1981-2001 (bn Ecu)*

Export	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
	1.9	2.0	2.8	3.5	6.5	6.5	5.5	6.2	6.8	5.8	6.3
	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	
	7.6	12.4	14.0	14.7	14.8	16.5	17.4	19.4	25.42	29.78	
Import	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
	2.3	2.3	2.7	3.2	3.8	4.2	5.2	7.5	9.8	11.4	16.0
	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	
	18.0	21.1	24.6	26.3	30.0	37.5	41.7	49.6	69.7	75.34	

Balance	198	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991
	-0.4	-0.3	0.1	0.3	2.7	2.3	0.3	-1.3	-3.0	-5.6	-9.7
	199	1993	1994	1995	1996	1997	1998	1999	2000	2001	
	-	-8.8	-10.6	-11.7	-15.3	-21.0	-24.4	-30.2	-44.3	-49.5	

Sources: Eurostat, *Yearbook* 1996, 2000 and 2002

Table 4.2 *Trade between China and the EC/EU in Manufactured Products, 1987-97*

% of the total extra-EU

	1987	88	89	90	91	92	93	94	95	96	97
China's export to the	2.2	2.6	2.9	3.6	4.7	5.4	6.0	6.3	6.3	6.9	7.4
EC/EU exports to China	1.8	1.9	1.8	1.5	1.6	2.0	2.9	2.8	2.7	2.5	2.4

Sources: Eurostat, *Yearbook* 1998/99, data from the year 1987-97

Table 4.3 *EC/EU Imports from China (bn Ecu)*

	1987	88	89	90	91	92	93	94	95	96	97
Machinery and transport equipment	0.4	0.6	1.1	1.7	2.3	2.9	3.9	5.1	6.3	7.6	10.0
Manufactured articles	2.4	2.8	3.2	3.1	3.3	3.2	3.1	3.3	3.6	3.8	4.5
Chemical products	0.4	0.6	0.7	0.7	0.8	0.8	0.9	1.1	1.5	1.5	1.8

Source: Eurostat, *Yearbook* 1998/99

Table 4.4 *Foreign Direct Investment from the EC/EU, Japan and the USA, 1986-1999, utilised capital, value: bn US\$*

	86	87	88	89	90	91	92	93	94	95	96	97	98	99
EC/EU	0.2	0.1	0.2	0.2	0.1	0.2	0.2	0.7	1.5	2.1	2.74	4.17	4.30	4.47
Japan	0.3	0.2	0.5	0.4	0.5	0.5	0.7	1.3	2.1	3.1	3.68	4.33	3.16	3.0
USA	0.3	0.3	0.2	0.3	0.5	0.3	0.5	2.1	2.5	3.1	3.44	3.24	3.91	4.39

Source: MOFTEC

Table 5.1 *EC/EU Anti-dumping Proceedings Initiated against Imports from China, 1979-2000*

Year	1979	80	81	82	83	84	85	86	87	88	89
Number of	2	1	2	4	2	2	1	2	0	7	5
Year	90	91	92	93	94	95	96	97	98	99	2000
Number of	4	4	6	2	1	3	0	7	5	12	6

Sources: The statistics from 1979 to 1992 are from Xiao pp. 87-88, those for the period from 1993 to 2000 are made by the author according to the *Official Journal* 1993-2001. This figure includes proceedings initiated and reviewed by the EC.

Table 5.2 *Categories of Commodities Involved in EC/EU Anti-dumping Proceedings, 1979-1999*

	1979-92	1993-8.99	Total
Chemical products	19	8	27
Mineral products	7	3	10
Machinery products	7	7	14
Textile and light industry products	3	7	10
Agricultural products	2		2
Electronic products	2	5	7
Medical products	2		2

Sources: The statistics for 1979-1992 are from Xiao Zhi Yue, p. 88. The statistics for 1993-99 are compiled by the author from the *Official Journal* 1993-1999.

Table 5.3 *Programmes Initiated by the EC/EU in the 1990s*

Education

EU-China Higher Education Programme,
EU-China Junior Managers Training Programme,
Euro-Asian Business Internship Programme,
EU-China Programme for the Development of Vocational Training,
EU-China Legal and Judicial Co-operation Programme,
EU-China Scholarship 2000 Programme,
EU-China Basic Education Co-operation Programme,
China-Europe Public Administration Programme

Environment

EU-China Liaoning Integrated Environmental Programme,
EU-China Honghe Environment Protection Programme,
EU-China Environmental Management Co-operation Programme

Agriculture

EU-China Technical and Commercial Co-operation with the Dairy Sector,
EU-China Qinghai Livestock Development Programme,
EU-China Qinghai Potato Development Programme,
EU-China Ningxia Hui Land Reclamation Programme,
EU-China Water Buffalo Development Programme,
EU-China Co-operation in Agriculture,
EU-China Panam Integrated Rural Development Programme
Social and Economic Reform
EU-China Statistical Co-operation Programme,
EU-China Public Procurement Co-operation Programme,
EU-China Local Authorities Linking Programme,
EU-China Training Programme on STD AIDS,
EU-China Training Programme on Village Governance,
EU-China Support Programme for Accession to WTO,
Asia-Invest Programme,
EU-China Intellectual Property Rights Co-operation Programme

Source: European Commission Delegation in China, <http://www.ecd.org.cn/co>

VIII Abbreviations

ABM	Anti-Ballistic Missile
ATC	Agreement on Textiles and Clothing
CCP	the Chinese Communist Party
CEEC	Central and Eastern European Countries
CFASLG	Central Foreign Affairs Small Leading Group
CFSP	Common Foreign and Security Policy
CMEA	Council of Mutual Economic Assistance
DG	Directorate General
EC	the European Community
EEC	the European Economic Community
EFTA	European Free Trade Association
EU	the European Union
FEER	Far Eastern Economic Review
FYP	Five-Year Plan
IMF	International Monetary Foundation
GATT	General Agreement on Tariffs and Trade
GSP	General System Preference
MFA	Multifibre Arrangement
MFN	Most Favoured Nation
MOFTEC	Ministry of Foreign Trade and Economic Co-operation
NATO	North Atlantic Treaty Organisation
NCNA	New China News Agency
NGOs	Non-Government Organisations
NICs	New Industrial Countries
PRC	People's Republic of China
QR	Quantitative Restriction
RMB	Renmin Bi (People's Currency)
RMRB	Renmin Ribao (People's Daily)
SALT	Strategic Arms Limitation Talks
SDPC	State Development Planning Commission
SETC	State Economic and Trade Commission
SEZ	Special Economic Zone
TEU	Treaty on European Union
USA	United States of America
WTO	World Trade Organisation

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