2016: The Year of China's Market Economy Status?

With the expiration of China's Protocol of Accession to the WTO taking place in December, its market economy status will become an important debate in 2016.

In 2001, the World Trade Organisation (WTO) successfully concluded negotiations on China's terms of membership. At the time, the WTO's Director-General, Mike Moore, said: "With China's membership, the WTO will take a major step towards becoming a truly world organisation. The near-universal acceptance of its rules-based system will serve a pivotal role in underpinning global economic cooperation." However, China was not granted the full rights of WTO membership.

As a result of the negotiations, formalised in the Protocol of Accession, China agreed to undertake a series of important commitments to open and liberalise its economy for goods and services. This agreement originally foresaw this transitionary period ending after 15 years, with the consolidation of China's status as a market economy being scheduled for 12 December 2016. This Protocol has allowed China to be treated as a non-market economy and for WTO members to take protective measures against Chinese exports that go beyond WTO general disciplines, without giving China the power to seek Special and Differential Treatment, as other developing country members have.

To be considered a fully-fledged "market economy" under WTO rules, five considerations need to be satisfied. A country must have a floating exchange rate, a free market, a non-intrusive government, effective business accounting standards and a clear definition of property rights and bankruptcy laws. However, in the most recent comprehensive assessment conducted by the European Commission in 2011, China was deemed to only have met the necessary criteria for one of these areas.

Many stakeholders in Europe have expressed their concerns about the potential harmful implications of granting market economy status to China, which they fear could limit the EU's ability to impose duties and apply higher anti-dumping rates. This rose to particular prominence in 2013, when the European Commission imposed anti-dumping duties on imports of solar panels from China, following an investigation which found that these were being sold at far below their normal market value. More recently, crisis in the steel sector made headlines across Europe, with ministers stressing the need to make the full use of the EU's trade policy instruments. Last year, the European Commission launched five new trade defence investigations against China.

In September 2015, a study by the Washington-based Economic Policy Institute argued that granting China market economy status could put up to 3.5 million jobs at risk, as Chinese companies could "undercut domestic production by flooding the EU with cheap goods." AEGIS Europe, a group of European industry organisations, has been particularly vocal in its concerns, and has continuously criticised what is calls China's state-sponsored dumping and export subsidies. The European Trade Union Confederation (ETUC) has also argued that China has yet to meet the criteria to become a market economy, saying that granting this would "deprive Europe of the ability to defend itself against Chinese imports."

However, there could also be benefits for the European economy deriving from cheaper imports, meaning that a range of effects could be felt by economic operators, including retailers, importers, third-party users and consumers. Indeed, a study recently conducted by the European Parliament argued that the economic implications of granting China market economy status "may be positive for certain sectors of the economy and negative for others." Furthermore, some analysts have argued that it would be "bad politics" to deny China market economy status, which should be integrated into the world economy according to a rules-based approach.

With trade becoming the exclusive competence of the EU since the Treaty of Lisbon, which entered into force in 2009, it is clear that the issue of China's market economy status will become increasingly prominent in 2016 and could well define the EU's relationship with China for years to come.

China's Position

Since 2003, obtaining market economy status has been one of the China's major foreign policy objectives. It has repeatedly argued that, according to its Accession Protocol, the non-market economy methodology expires after 11 December 2016, resulting in a legal obligation to grant market economy status to China after that date.

China has often criticised the EU's persistent refusal to recognise the country as a full-fledged market economy, as it considers this issue to be a serious obstacle to the development of closer commercial relations with Europe. Indeed, in a paper produced by the European Commission's Directorate-General for External Policies (DG EXPO), this was described as "one of the

Yang Yanyi, China's Ambassador to the EU

country's principal points of contention" with the EU. While some analysts in have argued that the EU may not be obliged to abandon its market economy status methodology for China in December 2016, Beijing disputes this and expects the members to automatically repeal the rules as of this date. China is therefore likely to bring the EU before the WTO dispute settlement body if importing countries still object to market economy status for China after December 2016.

This view was reaffirmed by Yang Yanyi, China's Ambassador to the EU, when she spoke to the European Parliament in April 2015. She called for both sides to "stand against protectionism" in accordance with WTO rules, while insisting that China has met the necessary requirements to be granted market economy status. However, as recently as 2014, the WTO itself argued that "China [still] applies price controls to commodities and services deemed to have a direct impact on the national economy and people's livelihoods."

China is also pushing the EU to complete the negotiations on the Bilateral Investment Treaty (BIT), which were started in early 2014, and will include rules on investment protection, market access and other elements further facilitating investment. It hopes that this will support its efforts in also having a deep and comprehensive free-trade agreement in the future. However, if China continues to be considered a non-market economy by the EU, it will remain hampered in its ability to further enhance its trading relationship with Europe.

The EU's Position

The European Commission, meanwhile, has made it clear that it does not see China's accession to market economy status as automatic in December 2016. It instead argues that this decision should be made on a country-by-country basis and based on individual technical assessments. Cecilia Malmström, the EU's Commissioner for Trade, has explained that the European Commission is currently undertaking an in-depth analysis of China's economy to this end, which is expected to be completed in early 2016.


Cecilia Malmström, EU Trade Commissioner

While several countries have granted early recognition of market economy status to China, mainly via the conclusion of provisions within Memoranda of Understanding, the United States has also made it clear that it will not automatically revoke its restrictive measures against China. This has lent support to the Commission's position that it is ultimately up to the EU to decide when its non-market status for China is revoked.

According to the most recent comprehensive assessment made by Commission's Directorate-General for Trade (DG TRADE), four out of the five fundamental criteria for measuring a market economy had still not been met. The exception, the report stated, was the "absence of barter trade and absence of state-induced distortions in the operations of enterprises linked to privatisation." At the time, this view was shared by the European Parliament, which expressed its concerns in a document entitled "EU and China: Unbalanced Trade?", and more recently stressed the importance of "market reform in China and of the implementation of market economy principles and the elimination of discrimination and unjustified restrictions".

Granting market economy status to China would lead to several changes in the EU's legal framework for Trade Defence Instruments (TDIs), which are tools used to oppose unfair trade practices by requiring a level playing field. Specifically, it would involve an amendment to the Basic Anti-Dumping Regulation, which listed China alongside other countries as a non-market economy, entitling the Commission to use a methodology that is not based on a strict comparison with domestic prices and costs in China. While the review of this, along with the Basic Anti-Subsidy Regulation, is currently facing severe disagreement in the Council, it is hoped by some that the upcoming WTO deadline will force the Council to act in the coming months.

As of November 30 2015, 53 anti-dumping and measures were in place against China. EU trade officials say that other safeguards, notably the anti-subsidy measures, could continue to be used even if China were to be granted market economy status. However, stakeholders have noted that the burden of proof for these is far higher than for anti-dumping cases. It has recently been reported that the Netherlands, which currently holds the Presidency of the Council, is now likely to wait for the Commission's position on China's market economy status before taking any further steps.

Conclusion

It is clear that the issue of China's market economy status will continue to gain prominence in 2016, particularly after the European Commission publishes its eagerly anticipated assessment. The ensuing debate is likely to divide opinions, both in the Council and the European Parliament, who should have an equal say on the Commission's upcoming proposal under the ordinary legislative procedure.

This decision will not only have important consequences for the EU's relationship with China, but could also have a significant impact on the international trading system as a whole.

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