

# The Heritage Foundation **Backgrounder**

214 Massachusetts Avenue, N.E. Washington, D.C. 20002-4999 (202) 546-4400

5/9/91

Number 160

**UPDATE**

## THE CASE FOR RENEWING CHINA'S TRADE STATUS

(Updating Asian Studies Center *Backgrounder* No.104, "Washington's Agonizing Decision: To Extend or Revoke China's Most-Favored-Nation Status," May 8, 1990.)

The Washington-Beijing relationship is beset by problems. The People's Republic of China's 1990 trade surplus with the United States was \$10.4 billion, up \$4.2 billion from 1989, and could leap to \$15 billion by the end of this year. This would make the U.S. deficit with China greater than with any country except Japan. The trouble with the mushrooming trade deficit with China is that there is a growing feeling that it is caused in part by Beijing's refusal to open China's markets fully to American goods. To make matters worse, the Chinese refuse to protect U.S. patents and copyrights, and apparently use prison labor to lower the price of their exports. Then there is significant evidence that the Chinese are peddling missiles and nuclear technology to Algeria, Pakistan and other Third World customers in defiance of multilateral efforts to ban such sales. And Beijing has yet to make a full accounting of what has happened to the pro-democracy demonstrators arrested after the 1989 Tiananmen Square massacre.

It is in this environment that George Bush will be challenged to decide by June 3 whether to renew China's most-favored-nation (MFN) trading status. Such status, granted to China in 1980 and approved annually since then, gives Chinese goods exported to the U.S. the same tariff treatment as that received by the some 180 other nations to which Washington accords MFN status, including Iraq and Syria and a host of other unpleasant regimes.

**Equal Treatment.** Although the expression "most-favored-nation" suggests that a country is accorded special trading privileges, the term actually means something quite different. Specifically, a country that receives MFN status merely is entitled to those trade benefits and concessions granted to any other MFN country. MFN thus confers no special trading status; it simply treats all MFN recipients equally.

Generally, MFN is a permanent status. The only exceptions are communist countries which, under the Trade Act of 1974, either annually or semi-annually must seek renewal. Specifically, Title 4 of the Act, known as the Jackson-Vanik Amendment, named after the late Senator Henry M. Jackson of Washington and former Representative Charles A. Vanik of Ohio, both Democrats, states that MFN status can be given to "non-market economies" if their countries permit substantially free emigration of their citizens. The law works like this: If the President wants to extend MFN status he must either certify to Congress that the country under consideration is not in violation of the Amendment's human rights criteria or waive the criteria for the country involved on an annual basis because such a move would "substantially promote the objectives" of Jackson-Vanik. Once George Bush certifies that China over the past year has allowed free emigration, Congress effectively has ninety days to approve or disapprove China's MFN status. Their vote is then subject to presidential veto.



America's problems with China thus fall into two categories — the economic and the political. Washington should deal with them accordingly: economic problems should be addressed with economic mechanisms; political problems with political ones.

**Trade Retaliation.** If Beijing refuses to assure copyright, patent and trademark protection to American business, for instance, then China should be identified under the 1988 Omnibus Trade and Competitiveness Act as a so-called "priority" country that has established "systematic" barriers to U.S. exports. This law sets procedures for dealing with unfair "priority" foreign trade practices through trade retaliation. The Bush Administration, in fact, on April 26 cited China as a "priority" nation for pirating U.S. copyrights and patents.

Conversely, the current political problems in the Sino-American relationship should be addressed through political mechanisms. China's continuing human rights abuses in Tibet, its likely use of some prison labor to manufacture goods for export and its sales of advanced weapons to dangerous nations should elicit vigorous condemnation from the highest levels of the U.S. government. Under Secretary Robert Kimmitt, the State Department's third-ranking official, traveled to China this week to convey U.S. dismay over Beijing's trade practices and human rights violations. Even tougher American political and diplomatic actions against China may be warranted by Beijing's transgressions.

What is not warranted is mixing the economic and political issues. China no more should be punished economically for its unacceptable political actions than Japan should be exempted for political reasons from economic punishment for its unacceptable economic actions against American products.

If Beijing violates the Jackson-Vanik amendment's "freedom-of-emigration" provision, then China's MFN status should be revoked. Otherwise, the issue should be subject to the same considerations by which Washington has deemed it proper to extend MFN to 180 other nations.

Other factors also argue against ending China's MFN status. To do so would:

- ◆ Dramatically raise duties on Chinese exports to America and thus hike the prices that working class and other Americans pay for these goods. Products from China now account for one-third of the American toy market, 10 percent of the American footwear market and 15 percent of the imported American apparel market.
- ◆ Cost the export industries of South China up to two million jobs. It is this area in which the free market and pro-democratic forces are strongest. Ending MFN thus would penalize those Chinese whom American policy ostensibly seeks to help.
- ◆ Reduce China's access to hard currency, further squeezing Beijing's ability to service its \$45.8 billion international debt.
- ◆ Close Chinese markets to American exporters. Last year, U.S. exports to China totaled \$4.8 billion. Among the biggest American losers would be wheat growers, whose 1990 sales approached \$1 billion; commercial aircraft manufacturers, for whom China has become a dependable \$500 million a year market; and phosphate fertilizer manufacturers, who consistently sell one-sixth of their entire annual output to China.
- ◆ Create enormous new problems for Hong Kong at a time when the colony can least afford anything that undermines confidence in its future. Some 70 percent of American imports from China are shipped through Hong Kong. As Hong Kong's largest foreign market and one of its principal investors, U.S. interests lie in a politically assured and economically healthy



Hong Kong. Uncertain about their future, 60,000 Hong Kong citizens leave the territory each year. Denying China MFN status may well speed the exodus.

- ◆ Increase Beijing's dependence on arms sales for cash. Cutting off American markets to Chinese goods could force Beijing to rely even more on the international weapons market for hard currency.
- ◆ Threaten to abandon the China market to the Japanese, the Europeans and others who automatically give China MFN status.

Almost two years after the violence in Beijing, Washington policy makers confront a recalcitrant, unapologetic and defiant China. A long and potent list of U.S. grievances daily increases. In such light, it is emotionally easy to make a case for punishing Beijing. If so, then appropriate punishment should be sought, and inflicted. Yet ending China's MFN status is not appropriate. If it is, then Washington must review the domestic political behavior of scores of other countries and prepare to revoke their U.S. MFN status. To end MFN for mainland China, moreover, barely will pinch Beijing's aging leaders who are the authors of the repression. Instead, it will hurt reformers in China, consumers in America and deal a heavy blow to Hong Kong.

Washington should recognize this. It should separate the economic and political issues at stake. And then it should conclude that there are no grounds for revoking U.S. MFN trade status for China.

Andrew B. Brick  
Policy Analyst

