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China Trade Strategy:  
FTAs, Mega-Regionals, and the WTO

Longyue Zhao



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**Robert Schuman Centre for Advanced Studies**  
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RSCAS Policy Paper 2015/11

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## **Abstract**

In light of the stalemate in the Doha Round of trade negotiations of the WTO, various regional and mega-regional free trade agreements are becoming the norm. Free trade areas advocated by major economies such as the U.S., China, and the EU have become the focus of attention in the field of international economics and trade. Compared to the free trade agreements of the U.S. and the EU, China's free trade agreement strategies are unique in their approach and philosophy. This essay analyzes and envisions China's FTA strategies, mega-regionals, and the WTO.

## **Keywords**

Free trade agreement; mega-regionals; the WTO.





## **Introduction\***

Behind the trend of economic globalization and regional economic integration, realizing the complementary advantages and the efficient allocation of intra-regional resources, as well as strengthening the ability to avert risks and increasing competitiveness internationally have become the key objectives of countries around the world. In recent years, the United States has been active in implementing a series of new initiatives in foreign trade. Through its leadership roles in mega-regional trade agreements such as the Trans-Pacific Partnership (TPP), the Transatlantic Trade and Investment Partnership (TTIP), and the Trade in Services Agreement (TISA), the U.S. is establishing a new set of rules in global trade and investment, in the process challenging the role of the WTO. The economies of the countries and regions involved in the TTP and the TTIP account for 60% of the world economy. These initiatives, together with their focus on removing barriers to entry in areas such as finance, investment, telecommunications, digital trade, e-commerce and the internet provide China, a nation currently undergoing further economic transition, a new set of challenges.

In response to TPP, TTIP, TISA and other threats of being marginalized in the world economy, China has rolled out a new set of strategies. Domestically, China is pursuing three types of measures to adapt to new international rules governing global economic integration: (i) political reforms; (ii) strengthening the rule of law; and (iii) establishing a new system of further opening up the economy through the construction of domestic pilot free trade zones. Internationally, China seeks to accelerate the negotiation processes in the Regional Comprehensive Economic Partnership (RCEP), move forward on a Free Trade Area of the Asia-Pacific (FTAAP), conclude bilateral free trade agreements, and support the leading role of the WTO in the multilateral trade system. China has also developed the “Silk Road Economic Belt” and the “21st Century Maritime Silk Road” initiatives to enhance the level of connectivity and bolster economic cooperation and with participating countries. These two programs taken together are called the “One Belt, One Road” initiative.

## **I. Strategies of China’s Free Trade Policy**

China officially made free trade policy an element of its national strategy following the 17th National Congress of the Chinese Communist Party (CCP) in 2007. In the 18th National Congress of the CCP in 2012, it was emphasized that China should speed up FTA negotiations with neighboring countries. At the 3rd Plenary Session of the 18th Central Committee of the CCP, General Secretary Xi Jinping announced the goal of “utilizing the surrounding areas as the foundation to accelerate the implementation of FTA strategies, and developing a high-standard international free trade network.”

In December 2014, the Politburo of the CCP Central Committee engaged in a collective learning session on China’s FTA strategies. At the meeting, Xi stated that standing at a new starting point in history, in order to achieve the “Chinese Dream” of realizing the revival of the Chinese race, China must adapt to the new trend of economic globalization, determine accurately the changes in the international situation, and grasp the needs for domestic reforms in order to push for higher levels of opening up, accelerate the implementation of its free trade area strategies, speed up the construction of a new economic system of opening up, and in doing so, gain the initiative in economic development and international competitiveness. There are three important pillars:

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### **A. Free Trade Agreements**

Currently China has concluded 14 FTA and is negotiating seven more. Together these span 32 countries and regions. The 14 FTAs that are in force or soon will be involve 22 countries and regions, and include agreements with ASEAN, Singapore, Pakistan, New Zealand, Chile, Peru, Costa Rica, Iceland, Switzerland, South Korea, and Australia, the Closer Economic Partnership Arrangement (CEPA) with Hong Kong and Macau, and the Economic Cooperation Framework Agreement (ECFA) with Taiwan. All these agreements are in effect except for the FTAs with South Korea and Australia, which are expected to go into effect by the end of 2015 or early of 2016.

Seven FTAs, involving 22 countries, are currently under negotiation. They include agreements with the Gulf Cooperation Council (GCC), Sri Lanka, Norway, the China-Japan-South Korea Free Trade Agreement, the Regional Comprehensive Economic Partnership (RCEP), an upgraded version of the ASEAN-China Free Trade Agreement (10+1), and the a second round of negotiation with Pakistan to expand the China-Pakistan Free Trade Agreement. In addition, China has completed joint research with India regarding the China-India Regional Trade Arrangement (RTA) and is currently exploring the potential for establishing FTAs with Columbia, the Maldives, Georgia, and Moldova. Furthermore, China is also a member nation of the First Agreement on Trade Negotiations among Developing Member Countries of the UN Economic and Social Commission for Asia and the Pacific (also known as the Bangkok Agreement).

In June 2015, China's FTA negotiations achieved significant progresses in two areas. First, the China-South Korea FTA was signed on June 1st. The agreement has 22 chapters and covers 17 areas, including trade in goods, trade in services, as well as foreign investment. In 2014, the volume of bilateral trade between China and South Korea was US\$300 billion, and is expected to surpass \$400 billion within five years. Second, after ten years of negotiation, the China-Australia FTA was finally signed on June 17th. Of the other FTAs signed by China, the China-Australia FTA has the highest level of liberalization in trade and investment. Australia is also the first country to adopt a "negative list" approach to trade in services with China.

During the State Visit of President Xi Jinping to the United Kingdom, China and the UK issued a Joint Declaration, and committed to building a global comprehensive strategic partnership for the 21st century. Both sides support the early conclusion of an ambitious and comprehensive China-EU Investment Agreement, and call for the swift launch of joint feasibility study for a China-EU Free Trade Agreement, and to build a deep and comprehensive FTA once the conditions are right. The European Union is the largest trade partner of China. In 2014, China-EU trade volume exceeded \$610 billion, of which China's export to the EU was \$370 billion and imports from the EU was \$240 billion. In recent years, the EU has signed FTAs with South Korea, Singapore, and Canada, and negotiations with the U.S. regarding the TTIP and with Japan regarding the Economic Partnership Agreement (EPA) are ongoing. The EU is also engaging in FTA talks with Malaysia, Thailand, and Vietnam, and is exploring the possibilities of signing a FTA with ASEAN. However, the likelihood of China negotiating a FTA with the EU is still uncertain. At the 17th China-EU Summit, held on June 19th, the two sides issued a joint communiqué, agreeing to reach a high level and comprehensive investment agreement as soon as possible, covering areas such as investment protection, market access, investment facilitation, and other elements.

### **B. Pilot Free Trade Zones**

Establishing pilot free trade zones is another major strategic move in China's push for a new round of opening up. The China (Shanghai) Pilot Free Trade Zone—the first of the kind—was established in 2013. Covering 28 square kilometers upon establishment, the Pilot Free Trade Zone was expanded to 120 square kilometers in 2014. After two years of experiment, China established another three more pilot free trade zones in Guangdong, Tianjin, and Fujian respectively, in 2015.

Generally speaking, the goal of establishing pilot free trade zones is to explore new ways of deepening domestic policy reform and expanding openness, building a system of institutional innovation and converge with international trade and investment rules in order to form new advantages of investment facilitation, effective government regulation, and rule of law in international competition.

However, each pilot free trade zone is different in terms of focus. The Shanghai Pilot Free Trade Zone emphasizes the innovation of institutional governance, the Guangdong Pilot Free Trade Zone focuses on deepening levels of cooperation between the mainland and Hong Kong and Macau, the Tianjin Pilot Free Trade Zone emphasizes the promotion of the cooperative development of the Beijing-Tianjin-Hebei region, and lastly, the Fujian Pilot Free Trade Zone focuses on deepening the cross-Straits economic cooperation.

### ***C. The “One Belt and One Road” Initiative***

Another grand strategy behind China’s construction of an updated opening economic system is the “One Belt and One Road” initiative. Chinese President Xi Jinping unveiled the initiative during his visits to Central Asia and ASEAN in 2013, during which he called for the construction of the “Silk Road Economic Belt” and the “21st Century Maritime Silk Road” using innovative models of cooperation. The initiative received positive responses from neighboring countries. In March 2015, China’s National Development and Reform Commission, Ministry of Foreign Affairs, and Ministry of Commerce issued jointly an action plan titled “Vision and proposed actions outlined on jointly building Silk Road Economic Belt and 21st-Century Maritime Silk Road.” The core of the “One Belt and One Road” initiative is to explore a new approach to regional cooperation and participation in global economy. The general idea of the initiative is to go from small into big and gradually forming a model of large regional cooperation, and as such promote “policy coordination, infrastructure connectivity, trade facilitation, financial integration, and people-to-people understanding.” The “One Belt and One Road” initiative has the following four characteristics:

First, the “One Belt and One Road” initiative extends through a vast region; there is no starting point or end point in the concept. It runs through Central Asia, Western Asia, Southeastern Asia, and South Asia, and is the link that connects the Asia-Pacific, Europe, Africa, and Latin America. The “One Belt and One Road” initiative engages over 60 countries and regions and over 4 billion people, which will account for 60% of the world population and 30% of the world economy. Since most of the countries concerned with the initiative are developing countries, the “One Belt and One Road” initiative provides these countries with a broad new opportunity for development.

Second, the “One Belt and One Road” initiative calls for a comprehensive cooperation among participating countries, not only in socio-economic areas such as economics and trade, investment, transportation, and the humanities, but also include international political and security areas such as promoting levels of friendship and cooperation, fighting terrorism, cooperation in non-traditional security areas, etc.

Third, the “One Belt and One Road” initiative promotes the development and internationalization of Western China and paves two different paths for China’s new round of opening up. On the one hand, it further advances the levels of openness of the coastal regions in East China. On the other hand, it paves the way for the opening up of Western China, helping the region transform from being marginalized in China’s policy of opening up to becoming the frontier of the policy.

Fourth, the “One Belt and One Road” initiative is different from conventional FTAs. There are no barriers to entry, no preconditions to join; instead, it is open and inclusive, focuses on the operation of the market that is mutually beneficial to all countries, and calls for a brand new model of international cooperation.

## II. Mega-Regional Trade Agreements

In light of the stalemate in the Doha Round of trade negotiations of the WTO, regional and mega-regional free trade agreements are becoming the norm, and mega-regional free trade agreements such as the Trans-Pacific Partnership (TPP), the Transatlantic Trade and Investment Partnership (TTIP), and the Trade in Services Agreement (TISA) led by the U.S. and the EU have become the focus of attention in the field of international economics and trade.

These agreements are significant in several aspects. The first aspect is the scope of participation of these agreements. There are 39 countries and regions participating in the talks for the TPP and the TTIP, which taken together account for over 50% of global trade volume and 60% of the world economy. The second aspect is the scope of the issues discussed, which include trade in goods, trade in services, intellectual property rights, domestic regulations, government procurement, competition policy, environmental cooperation, and labor cooperation, etc. The third aspect is the high level of focus of these arrangements on areas such as finance, investment, communication, and e-commerce that are central to global trade and investment today, further challenging the multilateral trade system led by the WTO.

Compared to the mega-regional free trade agreements led by the U.S. and the EU, China's free trade agreements are unique in their goals, emphases, and subjects. First, China's FTAs are mainly focused on the needs of domestic economic development. Major objectives include the promotion of the transition from a major trade country to a strong trade country; to adjust China's trade structure and to consolidate the traditional advantages of foreign trade while accelerating the development of new competitive advantages; and to ensure a stable and sustainable development path for China's foreign trade.

Second, the construction of China's free trade agreements is still in the stage of reciprocal arrangements, in which market opening is the focus of attention. The scope of the agreements is rather limited. Of the FTAs signed, most countries involved are developing countries, and both sides focus on arrangements such as the reduction and elimination of tariffs, market opening, and the facilitation of trade and investment. The main component of the FTAs focuses on traditional trading, and the legal text is relatively straightforward. The fundamental underlying principles are: simple first, complex later; easy first, difficult later; and sign first, improve later. The most typical example is the China-ASEAN FTA. First signed in 2003, the Framework Agreement on Comprehensive Economic Cooperation Between ASEAN and the People's Republic of China consists of less than 20 pages in text only, but was followed by the Trade in Goods Agreement and the Trade in Services Agreement, and an upgraded version of the China-ASEAN FTA is currently being negotiated.

Third, compared to the mega-regional FTAs led by the U.S. and the EU, China's FTAs are lacking in the attention given to innovation and redesigning of the rules governing economic cooperation and trade. As a developing country, in most cases, China considers first the interests of other developing countries and focuses on creating mutual-beneficial opportunities for all. In its participation in Asia-Pacific regional cooperation and the push for the Regional Comprehensive Economic Partnership (RCEP) negotiations, China is not taking on a leadership role, but focuses instead on helping to maintain the core position of ASEAN. The main reason behind this stance is to avoid the negative effects for regional cooperation resulting from competition between major powers, as well as to avoid the potential negative impact on small countries of China's building of its sphere of influence.

As the only hegemon in the international system today, the U.S. is not only the leader in various international organizations, but also dominates the negotiations of mega-regional FTAs. On the other hand, FTAs advocated by China focus mostly on developing countries, and are intra-regional, not trans-regional. That said, FTAs and more generally economic cooperation advocated by China are also changing. The "One Belt and One Road" initiative is an important example, with China attempting to construct a "mega-regional" strategic framework that encompasses the needs of all parties involved and in which China takes on the leadership role.

In the recently signed China-South Korea FTA and the China-Australia FTA, China is also starting to pay attention to the innovation of rules in international economics and trade. Encompassing contemporary issues such as e-commerce, competition policy, and the environment, and introducing for the first time language on local economic cooperation, the China-South Korea FTA has been referred to as the FTA with the “highest standard and broad content.” China and South Korea are planning to pursue a second round of negotiations to expand coverage of the agreement within two years of the effective date of implementation of the FTA, employing pre-establishment national treatment and negative list approaches.

The China-Australia FTA encompasses over ten areas, including goods, services, and investment, realizing the goals of comprehensiveness, high quality, and balance of interests, including investor-State dispute settlement provisions, and has the highest level of liberalization in trade and investment among the all FTAs signed by China. Australia eventually agreed to open up its service sector by way of a negative list, while China, on the basis of its WTO commitments, agreed to open up its service sector by way of a positive list, and promised to engage in trade in services negotiations with Australia in the future using a negative list approach. The China-South Korea FTA and the China-Australia FTA not only set the examples for the construction of free trade areas in the Asia-Pacific, but also provide new driving forces for the economic development of the region.

### **III. Prospects for China’s Free Trade Strategies**

Generally speaking, FTAs advocated by China are similar in their economic objectives to those advocated by the U.S. and the EU, but differ in their political appeal. Other than primarily pursuing market access and economic benefits, the FTAs advocated by the U.S. and the EU focus on establishing new sets of rules governing international commerce. FTAs advocated by China, on the other hand, emphasize to a large extent domestic economic development and the need for involvement in global economic cooperation, and are in part a strategic response to the mega-regional FTAs of the U.S. and the EU. In this respect, the U.S. and the EU are active players in global economy, and emerging countries such as China are in the passive position and striving to win the initiative. In other words, the strategic focus of the U.S. and the EU is to maintain their leadership roles in international politics and the global economy, and the strategic focuses of emerging countries such as China are to maintain their own interests, seek to participate in international economic cooperation, and seek to participate in the establishment of the rules governing international economics.

But from the perspective of long-term development, China’s free trade strategy is also changing. Developing countries remain the foundation of China’s foreign relations, as maintaining the common interests of these countries helps China build a more favorable international environment. China will become more active in speeding up the implementation of its free trade zone strategies in order to participate in establishing the rules governing international commerce as well as to increase trade and investment. Moreover, the multilateral trade system provides a forum for China to enhance its ability to participate in international rulemaking. Engagement in the WTO and implementation of the different elements of China’s free trade strategy will allow more Chinese voice on the reconstruction and innovation of the rules governing international commerce, and as such, promote the balanced development of the international economy.

With the Asia-Pacific region as the basis, and focusing on surrounding countries, China will steadily push for the negotiation processes of the Asia-Pacific free trade area and the RCEP, and begin the FTA negotiations with other partners of economics and trade in a timely manner. China’s development cannot be separated from the Asia-Pacific, and China’s development is an opportunity for development for other countries in the region. In promoting the construction of free trade zones, China will pay special attention at the integration of the advantages of various countries in the Asia-Pacific. At a recent ministerial-level meeting of the RCEP at Kuala Lumpur, capital of Malaysia, ministers from various countries discussed pressing issues such as trade in goods, trade in services,

and investment, hoping to conclude the negotiations by the end of 2015. With the formation of the ASEAN economic community, the RCEP may not remain at the initial stage of preferential trade arrangements, but develop more in-depth in the future.

At the same time, China is actively promoting the construction of an Asia-Pacific free trade area. This is reflected in the three grand objectives aimed at constructing a future-facing Asia-Pacific partnership and forging an open Asia-Pacific economic pattern established at the 2014 APEC Beijing summit: first, start the process of Asia-Pacific free trade area construction, taking Asia-Pacific cooperation into a new direction; second, formulate a consensus in the growth, reform, and the innovative development of the economy, exploring new impetus for the Asia-Pacific; and, third, focus on joint-development, building a new pattern of comprehensive, multi-faceted, and complex exchange system in the Asia-Pacific.

The final element of China's free trade strategy is the implementation of the "One Belt and One Road" initiative, accelerate the joint construction of a free trade area with surrounding countries in China's periphery and along the "One Belt and One Road," and forging a high standard free trade network. As the economic cooperation zone that is the longest in length in the world and has the most potential for development, the "One Belt and One Road" initiative is aimed at further fusing countries in East Asia, Central Asia, and Southeast Asia, forming a new basis for regional development. China adheres to the path of peaceful development, pursues a mutual-beneficial strategy of development, and practices the diplomatic philosophies of intimacy, honesty, kindness, and capacity in order to gradually deepen the cooperation with neighboring countries. Through the construction of "One Belt and One Road," China hopes to better promote the friendly exchanges between the peoples of different countries and advance the harmonious relationship between peoples of different races, different religions, and different cultures.

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