

## ARTICLE

# WTO's Special and Differentiated Treatment (S&DT) Principle and Solutions of the US-China Conflict



Kyoungseo Hong<sup>1</sup>, Jeong Ho Yoo<sup>2</sup>, Inkyo Cheong<sup>3,\*</sup>

<sup>1</sup>Department of Political Science, Graduate School, New York University, New York, NY, USA

<sup>2</sup>Division of International Commerce, Pukyong National University, Busan, Korea

<sup>3</sup>Department of International Trade, Inha University, Incheon, Korea

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\*Corresponding author: Inkyo Cheong  
Department of International Trade, Inha  
University, Incheon, Korea  
Tel: +82-32-860-7785  
E-mail: inkyo@inha.ac.kr

**Abstract** As the US-China conflict intensifies, the United States is pursuing a ‘decoupling’ strategy to build a new world trade order, arguing that the current World Trade Organization (WTO) system does not properly regulate China's non-market economic system. The WTO provides special and differentiated treatment (S&DT) for developing countries. The United States argues that China should give up its developing country (DC) status. Sufficient research on the DC status and S&DT has not been conducted as a means of resolving the US-China conflict. Decoupling means the collapse of the global supply chain (GSC), which will bring substantial shock to the global economy and a catastrophe for China. This paper examines the re-classification of DC status and S&DT in the context of US-China conflict and seeks an approach for China to avoid decoupling and coexist with the United States. It would be an optimal way for China to revive the WTO first and to improve its economic system through negotiations under the WTO.

**Keywords** Decoupling, Developing country status, Special and differentiated treatment (S&DT), Global value chain (GVC), World Trade Organization (WTO)

## 1. Introduction

During the Trump administration (January 2017–January 2021), the view of the United States toward China was fundamentally changed, although the two countries signed the Phase one agreement in January 2020. The Trump administration considered China's accession to the World Trade Organization (WTO) as “a mistake” (Donnan 2018), and it was understood that the US' establishment of ‘Normalizing Trade Relations with China’ in 2000 was also “a mistake” (Salam 2018). The current Biden administration continues to maintain the nation's China policy established from the Trump administration, and even has intensified the level of its pressure.

Such atmosphere between the United States and China is described as ‘a new cold war’. The United States analyzes that China has been expanding an ‘unorthodox economic regime’, meaning a non-market economy that is focused on its state-owned enterprises, rather than integrating itself into the global economy as a WTO member through the system of market economy (Rodrik 2019). In particular, the United States has deep concerns about how ‘China's socialist market economic system (China's System)’, which has been promoted by President Xi Jinping so far, and the policies related to China's System diverge from the principles of traditional market economy.

In April 2018, President Trump pointed out that China should not be classified as a developing country (DC) in the WTO and must stop enjoying special and differentiated treatment (S&DT), which is summarized in WTO (2018). He voiced that the WTO regulations including the S&DT should be fixed appropriately considering today's trade environment. Accordingly, a discussion on S&DT was revived within the WTO. China took a direct action toward the United States' request, arguing that the WTO reform should include pursuing S&DT and that the decision-making must be done unanimously (WTO, 2019). As the United States officially suggested the WTO to reform S&DT in February 2019, China submitted a document, which refutes the United States' argument, to the WTO (2019).

Special treatment toward DCs is a traditional practice in the multilateral trading system since the General Agreement on Tariffs and Trade (GATT), and it is determined through self-declaration. It is difficult for DCs, that are relatively disadvantaged

in competition compared to developed countries, to abandon S&DT. Since the WTO pursues a decision-making process by unanimous approval, the United States is aware that the WTO reform would not be easy. Accordingly, approaching the task in multi-dimensions, the United States decided to re-classify the DC status by itself in July 2019. Having mentioned its WTO withdrawal, the United States facilitated a strategy that let the WTO to be left on its own and to ultimately fade away, in other words, *an incapacitating strategy*. To avoid any blame for its WTO withdrawal, the United States chose to take a detour of blocking the function of the Appellate Body, making the WTO nominal. In this way, the United States certainly let the world know that ending the life of the WTO whenever it desires to was not a simple bluff.

China did not have to accept the United States' request to abandon the WTO DC status. However, the WTO has been collapsing followed by the American-led incapacitating strategy, and considering a situation where the United States constructs a new trading system that excludes China, what should be China's optimum response? The Washington Examiner (2019) reported that the United States was 'preparing for clash of civilizations with China' (Gehrke 2019). There could arise various opinions on the clash of civilizations (He and Chen 2019); the United States kept a more serious conflict in mind than what China had expected (Pastreich 2019).

Not to mention the United States and China, the collapse of the WTO could be a loss to all countries around the globe. Nevertheless, the reason why the United States had sought to facilitate the incapacitating strategy might have been based on its judgment that it cannot coexist with the present China. While demanding the S&DT reform and re-classification of DCs to the WTO, the United States could be accumulating justification for 'decoupling' toward China and establishing the post-WTO trading system.

Despite the abundant research on S&DT, there has not been a paper that analyzes the S&DT and DC status from the viewpoint of the US-China relation. As the global economy and the international trade order face new challenges on top of the great power competition between the world's two largest economies, it is especially critical to study an optimal strategy for all, not to mention the United States and China themselves. This paper seeks ways to resolve the US-China conflict based on the S&DT reform and re-classification of DC status.

## 2. Literature review on development of multilateral trading system and special and differentiated treatment (S&DT) institution

One of the challenges confronted in the process of developing the multilateral trading system was to accept DCs as well as the least developed countries (LDCs) as members and to lead them to adopt an active approach toward trade liberalization. Although they could expect economic benefits through international trade, it is difficult for those DCs, that have weak international competitiveness due to the pressure of domestic industry's restructuring, to readily adopt an open-door policy. At the time of signing the GATT in 1947, the 23 member countries were all developed countries, except Cuba.<sup>1</sup> Despite the fact that a very small fraction of DCs, such as Brazil, India, Pakistan and etc., had participated in 1948, the number of member countries during the Kennedy Round in 1964 was a maximum of 38 countries. Afterwards, the Tokyo Round (1973–1979) recorded 102 countries of participation, and the Uruguay Round (1986–1994) recorded 123 countries. In terms of a customs territory, the present number of the WTO members is 164; among them, 31 countries are developed countries, and the rest of 133 countries are DCs.<sup>2</sup>

S&DT is a concept that was established during the time of the GATT. Yet, DCs and the LDCs of the 1950s and 1960s did not realize the value of S&DT due to the import substitution strategy, and in the 1970s, some DCs such as South Korea sought to actively utilize S&DT in order to access the export market as making a transition toward a strategy of export-oriented growth (Messerlin 2006). Specifically, as the Generalized System of Preferences (GSP) was established under the GATT system in 1979, preferential approach of DCs (DCs include LDCs, hereafter) toward markets of developed countries was first legally defined.

S&DT institution greatly influenced the expansion of members of DCs (Whalley 1990). To construct a structure where developed countries and DCs with different stages of industrial development all together participate in the multilateral trading system, special consideration for DCs, which is the S&DT, had been necessary from the early days of the GATT. As the scope

<sup>1</sup>Since Cuba was a country directly involved in the Havana Charter, it was a member during the establishment of the GATT.

<sup>2</sup>Excluding the United States, Canada, Australia, New Zealand and Japan, developed countries in the WTO are the European countries. For more details, refer to the WTO website ([https://docs.wto.org/dol2fe/Pages/FE\\_Search/FE\\_S\\_S009-DP.aspx?CatalogueIdList=254127&CurrentCatalogueIdIndex=0](https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S009-DP.aspx?CatalogueIdList=254127&CurrentCatalogueIdIndex=0)).

of liberalization and binding trade rules expanded, the discussion on S&DT also became more vigorous to induce participation of more DCs. To lessen the pressure of trade liberalization and implementation of the GATT/WTO obligations along with a privilege of flexibility, and to secure export markets for industrial development, DCs felt the need to engage in the multilateral trading system (Keck and Low 2006).

## 2.1 Different perspective on special and differentiated treatment (S&DT)

S&DT is not regulated as an obligation of developed countries, but has been implemented through bilateral agreements between DCs and developed countries themselves as donors based on national interests (Michalopoulos 1990). Although a form of privilege for DCs was needed for development of multilateral trading system and expansion of members, developed countries expected contribution of DCs in trade liberalization. Developed countries had expected a process where the DCs perform the principle of reciprocity through trade liberalization after a certain period of time, though lessening the burden of their obligations in the beginning of their participation in the multilateral trading system. Moreover, developed countries wanted some DCs eventually to end their DC status ('graduation' in strict terms), while those countries anticipated to maintain special treatment permanently (Messerlin 2006).

The proliferating controversy of S&DT after the Uruguay Round (UR) and the Doha Development Agenda (DDA) resulted from the divergent positions on the large-scale negotiation that developed countries and DCs were engaged in. Despite the numerous arguments that S&DT contributed to advancement of DCs, there also existed opposite views by Whalley (1990), Michalopoulos (1990), Garcia (2004) and Hoekman (2005) that S&DT spurred protectionism of DCs rather than to expedite trade liberalization, which facilitated the S&DT controversy further. Hoekman (2005) asserted that the S&DT provided 'an excuse for avoiding trade liberalization'. Özden and Reinhardt (2003) also argued that those countries who had adopted an open-door policy instead of maintaining S&DT demonstrated greater growth. Analogous quantitative results were drawn from the research by Conconi and Perroni (2015) and Ornelas (2016). In specific, the former research displayed that those DCs that enjoy S&DT but also embrace reciprocity are likely to record higher trade liberalization and trade growth.

The S&DT issue has been converted into a discussion on 'policy space' since the 1999 WTO Ministerial Conference (MC) in Seattle where the topic of anti-globalization came up (Messerlin 2006). The idea arguing for special consideration toward DCs to earn benefits of economic growth through trade rather than developed countries' demand for DCs' globalization was globally expanded. Then such argument was developed into a logic of the policy space of DCs for economic development.<sup>3</sup> The reason why the first WTO negotiation on multilateral trade liberalization in 2001 became the Doha 'Development Agenda' was also reflected on the atmosphere of the international society in supporting 'development' of DCs.

There is so much literature for the argument of special consideration for the LDCs which was persistently raised with common interests (Conconi and Perroni 2015, Fukasaku 2000; Garcia 2004; Messerlin 2006; Michalopoulos 1990; Stevens 2002). Most of these studies emphasize the need for vibrant S&DT toward the LDCs. Further, Garcia (2004), Mah (2011) and Stevens (2002), suggest a more adequate form of S&DT for economic development of DCs.

However, there has been the need for a discussion on a new form of S&DT for DCs under the new trade environment. Specifically, as emerging DCs, such as China, India, Brazil and more, distinguished themselves in international trade, the view of developed countries on S&DT began to change. Keck and Low (2006) classify the major contents of S&DT that were negotiated from the beginning of the GATT to the DDA negotiation into 4 phases; they conclude that the S&DT remains unchanged while the trade environment changes.

Moreover, Stevens (2002) discusses that although S&DT was contrived to induce DCs to participate in the multilateral trading system, it did not operate in practice, arguing that instead of 'trying one size to fit all', designing S&DT in an appropriate form of which the domestic economic situation is pertinent for other DCs should take place. Nevertheless, there are voices arguing S&DT should circumvent away from 'a convenient negotiating slogan' (Whalley 1990), but should be improved into an effective system suitable for the spirit of the times (Pangestu 2000) and be enhanced to ignite 'development aspirations of DCs' (Hart and Dymond 2003). As the coverage of the Washington Consensus widens, the United States pursues new rules in the DDA (Rodrik 2019). The United States expressed concerns over how DCs may not engage in negotiating the new rules with the justification of S&DT. There could be multiple factors why the DDA negotiation was ceased in 2008 (Martin and Messerlin 2007), yet no country could explicitly express their complaints in spite of the numerous complaints from developed

<sup>3</sup>The policy space refers to trade and non-trade policies in favor of DCs so that DCs can actually benefit from the participation of the WTO system.

countries. After 10 years passed, the global trade environment has changed immensely. Although S&DT did not earn much attention within the multilateral trading system, it has become a global issue as the United States recently suggests the WTO to re-classify DC status. In fact, the US targets China, and China could not help, but to identify this issue as critical in establishing coping strategies for its trade conflict with the United States.

## 2.2 Special and differentiated treatment (S&DT) for DCs

During the time of the GATT, there was a practice of preferential treatment such as the GSP. By then, DCs were understood as ‘countries that still largely depend on exportation of raw materials though their standard of living has been improved’. At the 1979 Tokyo Round, countries agreed that DCs must also comply to the GATT rules when their economies gradually develop, by adopting a concept of ‘graduation’ of DCs. Following a rapid increase in participation of DCs in international trade after the 1980s, a discussion on the issue of the advanced DCs’ graduation of DC status took place more actively.

By adopting S&DT provisions at the 2001 WTO MC in Doha, Qatar, the rule of special consideration towards DCs under the WTO system was strengthened. This was due to the need for special consideration toward DCs to participate in the DDA negotiation. Although developed countries could adopt a wide scope of trade liberalization in negotiations, DCs could be convinced even without a large burden when they utilize the privileges of S&DT. Accordingly, the DDA negotiation could be launched, but it was not successful.

The UR adopted 155 S&DT provisions for DCs in the WTO. The areas of special treatment include tariffs, trade of agricultural products, subsidies, safeguard, Trade-Related Intellectual Property Rights (TRIPs) and others (WTO 2018). These areas are the issues that were currently subject to the US-China trade conflict. In general, DCs get to have less obligations than developed countries under the system. For example, while developed countries were obligated to reduce 36% of tariffs for 6 years, DCs were to reduce them by two-thirds of those for developed countries over 10 years.

At the 2001 MC, developed countries discussed the rule of graduation of DCs, then agreed to review any rules relevant to S&DT (Keck and Low 2006), yet DCs argued that due to limitations in ability and technical capacity, they were faced with difficulties in implementing the WTO agreements that were adopted at the UR. In addition, since the tariff gap between developed countries and DCs was drastically decreased due to continuous reduction of tariffs under the GATT and the WTO, DCs counter-argued that S&DT was more urgently needed. However, developed countries viewed the issue in the opposite direction (McCook 2015). In particular, the United States has been reluctant in giving S&DT privileges to emerging economies. Nevertheless, the WTO does not have a clear definition about emerging economies.

## 3. Re-classification of DC status in the WTO

In 2018, the United States claimed that China must not continue to enjoy the privileges of DC status under the WTO system and undertook the so-called ‘reform of developing-country status in the WTO’. China argued for a continuous practice of S&DT privileges and a return to the spirit of the WTO. Based on the present trade rules, China’s position is correct, since the United States is taking an issue with China’s economic system with its own yardstick, not with the WTO rules. Furthermore, since the WTO uses the system of self-declaration for DC status, China can declare itself to be a DC and does not violate the WTO rules, as Yu (2020) claims. Gao and Zhou (2019) argue that China does not enjoy considerable benefits as a DC in the WTO. If Gao and Zhou (2019) are true, it is possible for China to give up the status without substantial burden.

If the United States had been able to legally argue that China violated the WTO rules, it could have taken a measure to bring a dispute to the Dispute Settlement Body (DSB) of the WTO. Since taking such action was not feasible, the United States employed a combination of strategies to enervate, decouple and withdraw from the WTO in preparation of a bloc competition. The United States’ suggestion for re-classification of DCs can be seen as the groundwork that exerts pressure on China to abandon DC status using its own logic that China cannot be acknowledged as a DC. If China gives up its DC status, the United States would rush to revise the WTO rules targeting China’s non-market economy, then let China to carry out roles at the level of developed countries within the WTO.

The United States had not announced the reform strategy explicitly before, but in February 2019, it suggested 4 criteria for re-classification of DCs in the WTO, as can be seen in Table 1. Since the United States could not target and only pressure China to abandon its DC status, it officially raised the need for objective criteria of categorizing DCs to the WTO General Assembly. After 5 months -on 26 July 2019- President Trump, in the Presidential Memoranda, claimed that many WTO member countries are abusing DC status and that they must give up their DC status within 3 months in order to re-establish the WTO trade order. Further, if those developing economies fail to do so, they will be punished by the U.S. law, which is regarded as unilateralism.

**Table 1. Classification of DCs by the United States**

	OECD membership (7)	G20 membership (10)	High income (22)	Trade share* (17)
4 criteria	South Korea	South Korea	South Korea	South Korea
3 criteria	Turkey, Mexico	Turkey, Mexico	Saudi Arabia	Turkey, Mexico
2 criteria	Chile, Israel	China, India, Brazil, Indonesia, Argentina, South Africa	Chile, Israel, Argentina, Singapore, others	China, India, Brazil, Indonesia, others
1 criterion	Columbia, Costa Rica	-	13 economies such as Uruguay	4 economies such as Vietnam and Malaysia

Note: \* Higher than 0.5% in the global trade volume.

OECD, Organization for Economic Cooperation and Development.

Source: Classification base on the USTR (2021).

In particular, the Memo precisely proposed that China must not receive any further special treatment (White House 2019). By 2019, 6 countries, including Brazil, Taiwan, South Korea and etc., abandoned their DC status. The threat of the United States certainly worked.

Although there are no internationally objective criteria in categorizing developing and developed countries, the United States suggested 4 criteria, and argued that if a country satisfies at least one criterion, it cannot be treated as a DC. It is sensitive to judge whether one is a DC or not, since it is linked with the obligations in international institutions. Therefore, international organizations mostly assess by applying different criteria following their needs and defer to make a clear definition. In general, the most widely used criterion is per capita income. For instance, the Development Assistance Committee (DAC) of Organization for Economic Cooperation and Development (OECD), the United Nations (UN) and International Bank for Reconstruction and Development (IBRD) categorize those countries that have less than a certain level of per capita income to be underdeveloped countries. The International Monetary Fund (IMF) or the GATT evaluate by comprehensively considering the economic conditions or by the country's voluntary intent, not with explicit criteria.

### 3.1 Incapacitating the WTO

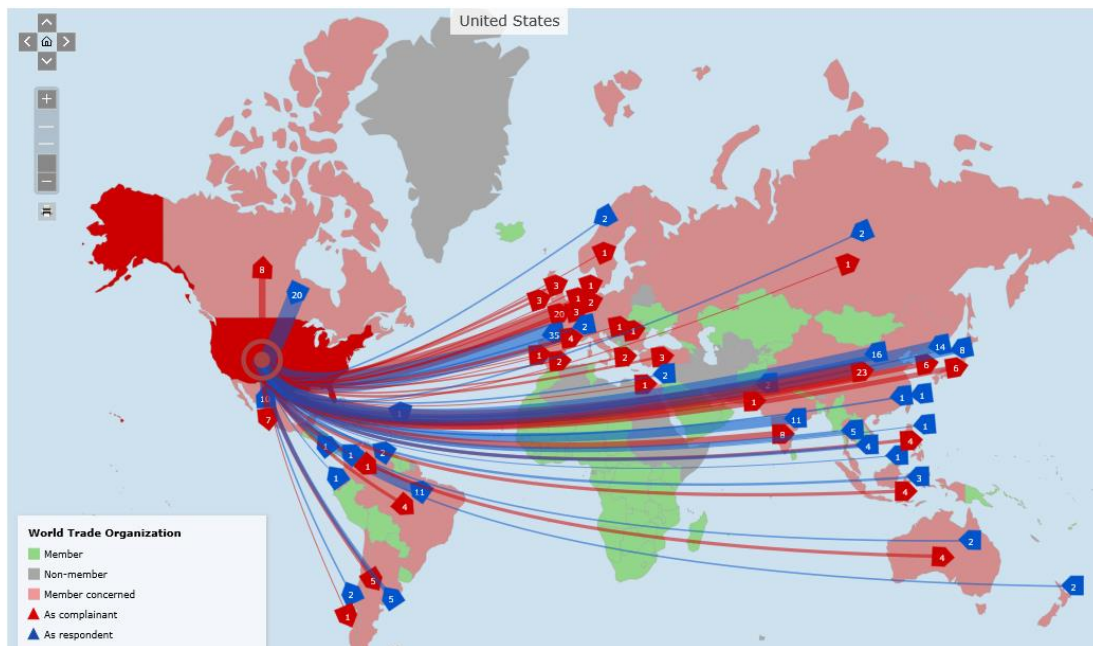
The United States most frequently applied the anti-dumping and countervailing duties to major exporters in the world. Although such practices are more relaxed towards DCs, the United States' trade sanctions on China have rapidly increased since before and after 2014 when China emerged to be the world's top trading partner. By January 2020, China was filed 44 cases by others, and China filed 21 cases of the WTO trade disputes. Among China's total of 65 cases (complaint, respondent), 39 cases were associated with the United States (Figure 1).

The United States viewed that not to mention the current WTO system, its domestic law would also be ineffective in regulating China's exports. Thus, the United States decided to regulate other exporters along with China by revising its own laws in spite of violation of the WTO rules. Adverse Facts Available (AFA), which was to increase the penalty on dumping and subsidies intentionally, can be an example. By applying the AFA aggressively, the United States imposed the anti-dumping duties on China by hundreds of percentages for the first time in under the GATT and the WTO. For this, China filed a dispute against the United States to the WTO DSB (Case of DS 471) in December 2013, and the Appellate Body stood on the side of China in May 2017.

When the law based on the US domestic law was judged to be illegal, the United States explicitly expressed its complaint regarding the current WTO rules. As found in the points made in Swan (2018), the loss of the 2017 lawsuit in the WTO has become the background for the United States to facilitate the incapacitating strategy of the WTO by blocking the appointment of new Appellate Body judges. Imposing high levels of tariffs with the justification of security based on Section 232 of the Trade Expansion Act was likely to violate the WTO rules, but the US has become not too concerned with the violation anymore since it ceased the judging system itself from functioning.<sup>4</sup> It can be said that the United States stopped the functioning of the DSB since it regulated the country's unilateralism.

When President Trump mentioned the possibility of the US withdrawal from the WTO during his presidential campaign in 2016, the world regarded it as a campaign promise that the American president cannot mention. After World War II, the United

<sup>4</sup>See Miles (2018), Schott and Jung (2019) and Swan (2018) for Trump's strategy on the WTO.



**Figure 1. Map of China's WTO trade dispute.**

Note: The figure may be transformed according to the guidelines.

Source: WTO (2021) DSU Image (assessed May 24, 2021).

States established the Bretton Woods system, then took leadership in creating the GATT to expand international trade. It is a clear historical fact that the United States took a critical role in establishing the current WTO system over the UR back in the early 1990s. President Trump's view on the WTO became even worse than it had been during his presidential campaign. The WTO reform may be a strategic offer of the United States, as it may have thought that buck-passing to other members who fail to agree upon the reform is politically more advantageous than withdrawing from the WTO and being condemned by the international society. At this time, the United States deemed China as an 'alien' and approached its conflict with China as the 'clash of civilizations'. As a point made in Washington Post (2019), the clash of civilizations could be 'the worst justification' (Taylor 2019), but it certainly was indisputable that the United States under the Trump administration, in multi-dimensional approaches, was in the process of creating a logic for the decoupling strategy against China and exclusion of China from the international trade order.

In fact, how the United States shook and even weakened the WTO began from the Obama administration. Originally, although the WTO was to acknowledge China as a market economy from 2016 (the Protocol for China's accession to WTO in 2001), developed states, such as the United States, the European Union (EU), Japan and more, refused to grant market economy status to China, raising issues with its factors of non-market economy, such as the Chinese government's support for its SOEs. While maintaining China as a non-market economy, it could impose duties of high rates against dumping and subsidies. Moreover, the United States blocked the appointment of new judges to the WTO Appellate Body by condemning the WTO in dealing with global trade issues. It is regulated that a judge can be appointed when all members agree, thus the United States ultimately ceased the functioning of the WTO Appellate Body as its original plan.

The United States expressed its criticism toward the WTO and facilitated a discussion on the WTO reform with the EU and Japan since 2018. The EU led the discussion on the WTO reform by presenting a 'concept paper' of the WTO reform, trying to reflect the US' position and the change of political economy and technology. According to the CSIS (2020), the 'concept paper' of the EU includes strengthening transparency, reporting payment of subsidies, relaxing investment barriers, banning enforced transfer of technology and more, yet the major topic is to intensify regulations on the SOEs and subsidies of market distortion. Also, the paper contains increasing the number of the Appellate Body judges from 7 to 9, changing part-time system to full-time, and augmenting the budget and organization of the Appellate Body.<sup>5</sup> The United States rejected the EU's suggestion

<sup>5</sup>Although the United States rejected the EU's suggestion regarding the Appellate Body, it would result in an "enervating strategy" unless the WTO rules are revised as a whole.

regarding the Appellate Body, and this seems to be due to the United States' desire for the incapacitating strategy toward the WTO by blocking the DSB from functioning.

As the WTO reform began to be discussed based on the paper by the EU, China also disclosed its position in November 2018. The Chinese government's position is that although the WTO reform is necessary, DCs including China itself must not become damaged from it. WTO (2019) of China has suggested 3 fundamental principles for the WTO reform: keeping the core value of the multilateral trading system, supporting development of DCs, and sticking to the integrated decision-making process of consensus. These principles displayed a huge gap with the United States' position that views China as a non-market economy and that China's SOE system should be fixed into the one fitting to the market order.

On December 11<sup>th</sup>, 2019, the Appellate Body of the WTO remained with one judge only, rendering it useless for future trials. If the Appellate Body does not operate, the WTO DSB also fails to function (WTO 2019). The Appellate Body functions as the supreme court of the world trade. The DSB is the last resort to enforce countries to comply with the WTO rules. Schott and Jung (2019) warn that the loss of the DSB may threaten the existence of the WTO itself. Joseph Stiglitz said the Trump administration's blocking of the process of appointing new Appellate Body judges would incapacitate the WTO during the interview with the CNBC (Chandran and Soong 2018). The United States also reviewed a way to speed up the collapse of the WTO.<sup>6</sup> In this sense, the United States' proposal for the WTO reform inevitably became a pressure for other member countries. Furthermore, although China was aware that collapse of the WTO will be an immense shock on its economy, which is the world's top trading partner, its position remains to be that it cannot accept the change of rules based on what the United States wants as it would impair China's benefits from the multilateral trading system (Zhang 2018; Zhu 2019).

When the DSB will be normalized would determine the destiny of the WTO. The WTO will fade away if other member countries do not put efforts into the reform. Then, the United States would emphasize both internationally and domestically how it did not explicitly destroy the WTO.

### 3.2 The US-China conflict and bloc competition

The more forcefully the United States calls for the WTO reform, the more robust the argument for the WTO's uselessness becomes. Despite the rapid change of the trade environment, the WTO rules have not changed conspicuously.<sup>7</sup> As China rises, the United States and the EU problematize China's non-market economy. After President Trump took office, the China containment policy has been even more bolstered. Further, the United States' desire to withdraw from the WTO is based on its argument that China enjoys special treatment by abusing its DC status. The United States promoted the decoupling strategy against China by applying its domestic laws and forming international alliance with the EU and Japan. Moreover, the United States inserted a clause that implicitly targeted China in the US-Mexico-Canada Agreement (USMCA), preventing Canada and Mexico from signing any trade agreement with a non-market economy, which indicates China (Lawder 2018).

The scenarios of how the US-China conflict will unfold can be divided into an optimistic view and a pessimistic one. As the Phase one negotiation out of 4 phases was settled at the end of 2019, the optimists would accentuate the possibility that the United States and China can resolve their conflict over a negotiation. At the first round of negotiation, China promised to expand imports of the American agricultural products and improved the trading system of intellectual property rights and more. Then, for this, the tariffs that the United States had forewarned were to be postponed with some reduction of the existing tariffs.<sup>8</sup> On the other hand, the pessimists would be concerned that there still exist challenges on major components, such as the non-market economy, subsidy, the dominant role of the Chinese SOEs, digital trade (e-commerce), the implementation of the Phase one agreement, and etc.

In the midst of the rocky situation with China, the United States is expanding its allies. In other words, the United States has entered into a bloc competition against China. China, too, has been strengthening its diplomatic power with many countries as France, Italy and more, but it seems to be beyond its capacity when compared to the United States. Developed countries, such

<sup>6</sup>“To put the nail in the Appellate Body coffin, US officials now are seeking to sharply reduce funding for it and threatening to block the WTO budget for 2020 if other members don't accept US demands” (Schott and Lee 2019, p. 4).

<sup>7</sup>The WTO had sought to upgrade the organization through the 2001 DDA negotiation, but it was, as a matter of fact, ceased. The Trade Facilitation Agreement (TFA) is the first new agreement that the WTO took into effect since the organization's establishment. There are optimistic evaluations on the TFA which entered into force in February 2017 (ADB 2019; USAID 2017), but it may have a more symbolic meaning than the WTO still functions rather than economic effects. Although not all members agree, a fraction of the members, in other words, the 'like-minded countries', facilitated 4 plurilateral agreements such as Government Procurement Agreement (GPA).

<sup>8</sup>The United States' 25% additional tariff on Chinese exports of \$ 250 billion will remain the same, but the 15% tariff on \$ 120 billion will be reduced to 7.5%.



as the EU, Japan and Canada, appear to have agreed on the decoupling strategy of the Trump administration, though tacitly minding China. In September 2018, the representatives of these countries met in New York to discuss the international trade order and the WTO reform, then decided to take collective actions on the issues of policies and practices of non-market economic policies, the SOEs/unfair subsidies, and enforcement of technology transfer at the trilateral meeting, based on the guidelines by the USTR (2018)<sup>9</sup>. The statement did not explicitly indicate China, but it was interpreted as constructing the U.S.-EU-Japan trilateral cooperation system. In spite of the importance of economic cooperation with China, which soon will become the world's biggest economy, the EU and Japan have decided to share the same position as the United States, hoping that the United States would not leave the WTO and not impose further tariffs on their exports based on Section 232.<sup>10</sup>

Further, the EU and Japan may have taken such position to cope with the Chinese state capitalism.<sup>11</sup> These countries are well aware that the core of the Xi administration's 'Made in China 2025' includes substantial government subsidies and the roles of the SOEs, but also worry about how the WTO is unable to regulate any of them. In other words, the developed countries commonly share the idea that they are in a helpless situation where China facilitates a national development strategy in its manufacturing industry while fully receiving special treatment granted to DCs. In this sense, those countries may have shared the same position on the WTO reform plan which the United States suggested.

There are already clear indications that the new Biden administration aims to unite the American allies in an effort to "contain China's territorial claims across the Indo-Pacific" (Lendon 2021). On March 12<sup>th</sup>, 2021, the Biden administration took a bigger step forward to that goal by bringing together a virtual gathering for leaders of the Quad, which is "the loose alliance of the United States, Japan, India, and Australia that Beijing has called emblematic of a "poisonous" Cold War mentality" (Lendon 2021). Although the Quad is not a formal military alliance like the North Atlantic Treaty Organization (NATO), it is understood by some as "a potential counterweight to growing Chinese influence and alleged aggression in Asia-Pacific" (Lendon 2021).

### 3.3 The ways for China

Chatham House assessed that although President Trump intimidated that it could withdraw from the WTO, it would not be easy due to political economic pressures against disintegrating the current international economic system and trade order that led the American hegemony (Schneider-Petsinger, 2019). However, even within the American politicians, an atmosphere of advocating the trade policy against China seemed to be dominant.<sup>12</sup> The US Congressional Research Service (2019) reviewed the issues of the WTO reform and assessed the position of DCs in setting new trade rules regulating non-market economic policies and practices of China. It also pointed out that the 2017 WTO MC did not take any actions on the WTO reform and called for the need to upgrade the WTO system to the one compatible with the present global trade environment. Considering the level of Trump's criticisms at the UN speech in September 2019, it seems reasonable that decoupling with China would be merely a question of time.

Even though the threat of the WTO withdrawal can end as a mere threat, President Trump has proved that a threat can become a reality several times over the course of his presidency, thus the world does not regard such threat as a mere bluff. Although the recent G20 summits (Buenos Aires in November 2018; Osaka in June 2019) called for the WTO reform, a plan that could embrace both China's state capitalism and the Western market-economy system was not founded (Financial Times, 2019). The American policymakers came to see that the WTO's adoption of the China containment policy in the present system is unlikely. Not to mention the WTO itself, but even its member countries do not conceive that the WTO is functioning properly. The current WTO is in a difficult situation to overcome an existential crisis and its uselessness. Since the collapse of the WTO would result in the deterioration of the global trading environment, President Trump's argument on the U.S. withdrawal from

<sup>9</sup>The Joint Statement released by the USTR(2018) says that "they directed their staff to further their discussion on various elements or indications that signal that non-market oriented policies and practices exist for businesses and industries, to enhance information sharing on non-market-oriented policies and practices of third countries, to engage with other trading partners on identifying means to maintain market-oriented conditions, and to deepen discussions on enforcement and rule-making as tools to address these problems."

<sup>10</sup>In 2018, the United States imposed a 25% tariff on imported steel and aluminum for national security (Section 232) and is currently planning to a Section 232 tariff on imported cars. The EU and Japan have been exempted from additional tariffs on steel and aluminum through some agreement with the United States.

<sup>11</sup>Followed by the trilateral meeting between the US, EU and Japan in September 2018, Canada invited trade representative of 13 countries, the US, EU, Japan, Australia, South Korea, Brazil and more, to Ottawa to discuss the WTO reform, and announced a joint statement similar to the trilateral meeting in the same year.

<sup>12</sup>In terms of the trade war with China, farmers and distribution industries are complaining, but President Trump describes the trade war, which he has been facilitating, as a patriotic act and promises to promote agricultural industry. Then, he attenuates the opposition of the damaged groups and is competent in a propaganda war toward his own people.



the WTO carried too many risks to be simply regarded as his bluffing.

Considering the United States' strategy, the WTO might soon reach the end of its life as an international organization. In some aspects, several measures could be done to shorten the lifespan of the WTO (Schott and Jung 2019). Preserving and reforming the WTO are critical to the world economy (González 2019). Unless China improves or reforms major parts of the Chinese characteristics and socialist factors from China's System, the United States seeks to build a new multilateral trading system. The clash of civilizations and decoupling mean that the United States does not intend to go with China. Surely, the current US-China conflict is completely different from the US-Japan trade conflict in the 1980s. Since the Chinese domestic market size is huge, China certainly can live through even if it is isolated; however, its share of trade is 38% of the country's gross domestic products (2018). The cost that China has to pay when it has to be reliant on the imported energy would be considerable. China itself would be the country that would be damaged the most from collapse of the WTO. Although it may be humiliating to be caught up in the U.S.' strategy, it would be wise to adopt a more practical foreign policy. Furthermore, China's position in the international trading system would gradually be weakened due to the bloc competition with the U.S. and the decoupling strategy.

The strategies that China can adopt in the current US-China conflict can broadly include 3 approaches: (1) direct confrontation, (2) negotiation and compensation, and (3) leadership strategy. Since the end of 2018, it is understood that China abandoned the strategy of direct confrontation. China lacked practical measures to directly confront the asymmetrical action of the Trump administration in the impositions of additional tariffs. As a result, China currently is performing the second strategy of negotiation and compensation and unwillingly continuing disadvantageous negotiations, as seen in the Phase one agreement.

Considering the many sensitive issues between the United States and China, the 4 phases of full-scale negotiation that President Trump mentioned would take a long time, and in the meantime, the WTO can be disintegrated. Even if China exerts diplomatic efforts based on its enormous purchasing power, its position in the international society will be weakened. One should address if China can persistently maintain its position with unsustainable economic growth. Further, if China becomes excluded in the new international trade order established by the US, its industrial development will be critically damaged. Above all, adoption of advanced technology would be difficult, and there would be a gap between China's technical regulations and global standards, which would result in China's risk especially in new technology. Over time, China will suffer a big loss in international competitiveness due to technical barriers to trade.

In this sense, the third strategy of leadership would be more applicable to China. This includes abandoning of DC status and participation in the WTO reform, then eventually normalizing the function of the WTO and keeping some of the major benefits for itself through containing the United States' unilateralism. The international society is concerned of the United States' unilateralism, yet also views that the WTO S&DT cannot rationalize non-market economic factors included in China's socialist market economy. Maintaining the Chinese version of economic system, China needs to be aware that the economic growth and creation of jobs using the current WTO system are not permitted by the international society.

#### 4. Conclusion

As the United States turns to protectionism, there exists an empty space in the WTO leadership. In the past, the United States and the EU led the multilateral trading system by first reaching an agreement among themselves then persuading other countries. However, China cannot exert leadership, since the world knows that the United States is pushing the decoupling strategy against China. The multilateral trading system is a system to prevent the transgression of the great powers and is advantageous to the weak and smaller economies. The United States weakens the WTO to impose trade sanctions on China that go beyond the WTO norms. China, a G2 nation, is by no means a small country, but can be considered relatively weak in the current U.S.-China relations. Therefore, it would be wiser to revive the multilateral trade system first, and to improve the domestic economic system through negotiations in the multilateral trade system.

De Mars (2019) views that if the WTO reform takes place, the United States would introduce a new rule for China's state-owned enterprises (SOEs) to rationalize the US' trade sanctions on China. Moreover, it is expected that the rules for subsidies will be modified to contain the Chinese government's support for the SOEs and to include a clause on rationalizing the 'Trump tariffs' with the justification of security. China is concerned of the burden on its shoulders followed by the range and contents of the reform (He and Chen, 2019; WTO, 2019; Xinhua, 2018; Zhang, 2018).

About 80% of the world's trade is related to the activities of multi-national companies based on the global supply chain (GSC) (Taglioni and Winkler 2016), and China is the core country of the GSC. Today, the GSC is based on the WTO framework and globalization. The collapse of the WTO will lead to a reversal of globalization, and the resulting contraction of trade will

outpace the 1929 Great Depression. To avoid this, the United States seeks to establish a new multilateral trading system that excludes China. When the WTO is disintegrated and a new trading system is introduced, China, the world's biggest trader, will be shocked the most. China should be aware of the possible damage it has to bear.

It should be recognized that the American policy toward China will continue regardless of Trump's term, since the United States is sure that the WTO cannot coexist with the current China's System. In fact, President Biden's China policy continues to maintain the nation's China policy established from the Trump administration, and even has intensified the level of its pressure. It should be kept in mind that non-market economic factors that cannot be internationally recognized are hard to be sustained. Several countries like Brazil, gave up their DC status, and the United States will push other countries, such as Turkey, Mexico, India and more, to abandon their DC status. It will not only exert pressure on China, but also become an agenda in the US-China negotiation.

It will also be more advantageous for China to negotiate the WTO reforms in the context of the organization as a whole rather than through a bilateral negotiation with the United States. Nevertheless, since the advisors to the American presidents are well aware of the failures resulted from the numerous time-wasting negotiations of the past, it is advised that China does not adopt the leadership strategy in an aim of time-wasting and ultimately flipping the situation. Further, China should understand that expansion of market economy improves the Chinese economy in strengthening the structural improvement and competitiveness.

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