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China's Trade Relations with the United States in Perspective

Dong Wang

Abstract: China's trade relations with the United States over the past four decades is a topic that has not been fully dealt with in scholarly works. This paper charts the course of US-China economic relations since 1971, explains the principal forces stimulating growth and encouraging change and, finally, discusses how these two economic giants fit into an interlocking Asian and world economy. In reaction to the post-2008 financial downturn, advocates for a new world economic order have suggested a rebalancing of global demand, which will arguably become a major, politically charged issue in the US and in China in the years to come. Growing economic interdependence has quickly presented new challenges and opportunities, with issues such as human rights, Most-Favoured-Nation status, the Taiwan and Tibet question, and the huge American trade deficit threatening to cloud the relationship at times. With China's emergence as a major power and America's hegemonic ambitions tested in successive wars, the contradiction between a booming commercial relationship and conflict associated with geopolitical and ideological differences will continue to constitute a serious challenge. The long-term goal for each side will be to forge economic ties strong enough to create a stable political relationship, rather than to be held hostage by geopolitical constraints.

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Dr. Dong Wang is Professor of Contemporary Chinese History and Director of the Centre for East Asian Studies at the University of Turku in Finland. In this capacity, she also manages the Graduate School of Contemporary Asian Studies and the National University Network for Asian Studies. Professor Wang's research interest centres upon the interaction between China and the outside world, as exhibited in the areas of politics, international organizations, nationalism, treaties, international law, charities, the environment, urban development, disaster management, state and society, heritage, religion, art, higher education, the economy, and US-China relations.
E-mail: <dong.wang@utu.fi>

1971 and 2009, "The China Puzzle" and "The China Price" – Turning Sino-American Commerce on Its Head

On February 25, 1971, President Richard Nixon made headlines when he told Congress that the continuing animosity between the US and the People's Republic of China was an "unresolved problem, serious indeed in view of the fact that it determines our relationship with 750 million talented and energetic people" (MacFarquhar 1972: 251-253).[1] Nixon announced his intention to open dialogue with Beijing and bring China back into the world community.

For Americans in the early 1970s, as far as the economy was concerned, Nixon might just as well have announced a trip to the moon. As a *New York Times* reporter wrote, "The news of President Nixon's coming trip to Communist China, sensational as it is politically, produced virtually no effect on the stock market" (Silk 1971: 45, 48). China was a "puzzle" to be pieced together, as an important fiscal development would soon illustrate. On August 15, 1971, in an attempt to redress inflation and unemployment, the Nixon administration devalued the US dollar by 8 per cent by imposing a system of wage and price controls and fixing the exchange rates for American currency. As a result, "one country after another began to float its currency against the dollar" (Walton and Rockoff 1998: 650). A few days later, James Reston filed this report for the *New York Times* from Shanghai:

> The "dollar crisis" was no crisis in China. Even here in this commercial capital of the People's Republic there was no public evidence that anybody was paying the slightest attention to Washington's "new economic policy." […] Two days after President Nixon devalued the old greenback and sent a hiccup through all the banks and stock exchanges of Europe, I cashed $500 worth of American travelers [sic] checks at the old exchange rate in Peking. No problem. No questions asked. And even a day later, the banks here in Shanghai were still paying out on cabled dollars from New York as if nothing had happened (Reston 1971: 33).

1 Acknowledgement of assistance and encouragement is due to Mark Selden, Paul Sorrell, Susan McEachern, Xiaoyan Zhang, Junxin Jiang, Kari Lehti, Flemming Christiansen, Petra Brandt, and anonymous reviewers.

Reston's report provides a glimpse of China's almost total insulation from the outside world in 1971. Yet, 36 years later, on Tuesday, February 27, 2007, Wall Street tumbled in the wake of a massive 9 per cent slide on the Shanghai stock market, equivalent to a 1,100-point drop in the Dow Jones industrial average. On the same day, the Chinese sell-off set off falling stock prices around the world: The Shenzhen Stock Exchange (China) fell 9.3 per cent, the Hang Seng Index dropped 1.76 per cent, the Nikkei went down 0.5 per cent, share prices in London, Frankfurt and Paris plummeted 2-3 per cent, and the New York Stock Exchange closed down 3.29 per cent – the worst day on Wall Street since 2001 (Barboza 2007; Norris and Peters 2007; *The New York Times* 2007; O'Rourke 2007).

The transformation of the commercial relationship between the two countries has indeed been profound. As of January 2009, China is the third-largest buyer of US goods and services whereas the US is China's second-largest export market, according to American statistics (The US-China Business Council 2009: 8). The Chinese side figures put China as the fourth-largest buyer of American products and the US as China's largest export destination (People's Republic of China General Administration of Customs 2009). According to 2006 US statistics, the trade volume between the two nations had risen to 285.3 billion USD (of which 201.7 billion USD was a trade deficit run by the US) – more than 60,702 times the level of trade between the two countries in 1971 (Harding 1992: 99; The US-China Business Council 2007b; China Business 2006; Cheng 2006; Lieberthal 2006).[2]

US-China economic relations over the past four decades is a topic that has not been examined fully in scholarly works. This paper charts the course of China's trade relations with the United States since 1971, explains the principal forces stimulating growth and encouraging change and, finally, discusses how these two economic giants fit into an interlocking Asian and world economy. An examination of trade in different geo-strategic contexts reveals five themes inherent in the economic character of the relationship.

First, sustained growth in both economies has benefited both nations through the mutual stimulus to exports and imports. In nearly 40

2 This estimate is based on figures in Harding 1992: 99 (setting the 1971 figure at 4.7 million USD) and Tao 2004: 339, zero. The increase in bilateral trade volumes from 1979-2006 was 116-fold, although a number of sources point to an increase of 80 times.

years, extraordinary increases have taken place in the volume, value and complexity of economic exchange – trade, investment, and technological transfer – between the US and China, making them among each other's largest and most important trade partners (Frisbie and Overmyer 2006).

Second, the development and growth of business ties were driven by interdependent geopolitical and economic factors including a common US and Chinese interest in isolating the former Soviet Union; Cold War and post-Cold War geopolitics; the drive for profits; China's economic reforms; and the rise of the Asian economy on the world stage.

Third, since the rapprochement, the US has often had the upper hand in the relationship while China has mostly found itself on the defensive (Wang 2007: 10-22).[3] As the relationship deepened, the Chinese, nevertheless, gained increased leverage and bargaining power. Most significantly, China, along with India, was the driving force of the robust economic recovery in Asia in 2009. China has helped shield the US from the effects of its own economic mismanagement. Over the period 2000-2004, spanning a global recession, the growth in imports to China occurred side by side with China's own export boom. This was "a key factor in ensuring that the impact of the global recession on the United States and other economies was not as severe as it might have been" (The China Business Forum 2006: 2). By the end of 2009 China's foreign exchange reserves reached a record of just under 2.4 trillion USD (The US-China Business Council 2010). Since 2006, China has been instrumental in propping up the American dollar by its purchase of 247.6 billion USD of US Treasury Bonds (Leonard 2006). China has become America's banker, holding a 585 billion USD American government debt, as one analysis sees it (The US-China Business Council 2009: 8; BBC World News America 2008). To put it another way, "China is funding American profligacy", allowing Americans to consume far more than they produce (Leonard 2006).

Fourth, China's economic surge was far from being limited to US-China relations. The Chinese hedged their bets and diversified their economic cooperation with Japan, Korea, and with certain Southeast Asian, European, South American and African countries.

The fifth theme is the heightened contrast between booming economic ties and the political relationship that notoriously blows hot and

3 In China's eyes, Chinese diplomacy from 1977 to 2007 had been dominated by China's reactions to a myriad of issues and criticisms initiated by the US.

cold. Although both governments since 1972 have broadly promoted the policy of engagement, constant swings testify to the absence of durable political foundations for the relationship, particularly notable in the post-Cold War era.[4] Some crucial questions remain unanswered: While business links have expanded on a massive scale, will commercial relations bring the two nations closer politically and ideologically? Will their volatile political relationship be stabilized by the construction of an entrenched economic platform?

The First Ten Years, 1971-1980: Historic Beginnings

As the US and China emerged from a long political freeze, the first steps towards renewing direct contact were taken in 1971. These ten years saw historic and institutional changes in the economic realm that were unprecedented in terms of scale and rapidity.

Already by 1971-1972 China's international trade and its trade with the US were increasing by levels of 20 per cent per year, which would be sustained over the coming four decades. In March 1971, the State Department eased restrictions on US citizens visiting China and the following month American table tennis players toured the country in what became known as the "ping-pong diplomacy". On April 14, the Nixon administration announced five measures aimed at removing restrictions on commerce and travel between the US and China. Under this initiative, the United States would expedite visas for visitors from the People's Republic. US currency controls were to be relaxed, allowing American citizens to remit money to Chinese citizens or organizations without prior Treasury approval. There was also limited liberalization of commercial activity. Restrictions were to be lifted on:

> American oil companies providing fuel to ships or aircraft proceeding to and from China except on Chinese-owned or Chinese-chartered carriers bound to or from North Vietnam, North Korea, or Cuba (MacFarquhar 1972: 254).

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4 On the American side, David M. Lampton writes that "US presidents as different from one another as Richard Nixon and Jimmy Carter, and Bill Clinton and George H. W. Bush and George W. Bush, not to mention Ronald Reagan and Gerald Ford, have all ended up pursuing a broadly consistent China policy, even though they came to office with quite divergent inclinations and domestic contexts" (Lampton 2007: 745-749).

The *New York Times* reported that:

> A list of "non-strategic" goods will be drafted and U.S. companies will be allowed to export these items directly to mainland China without prior government permission. Selected direct imports from there will be authorized in the future. […] American carriers will be allowed to haul Chinese cargo between non-Chinese ports (Keatley 1971: 2).

Then on June 10, following these carefully calibrated measures, President Nixon officially ended the trade embargo, sweeping aside the legal barriers which had hindered significant economic ties between the US and China since 1950. In October, United Nations General Assembly Resolution 2758 brought China onto the Security Council in place of the Republic of China in Taiwan. China had assumed a position as a leading power after a quarter of a century of marginalization that was chiefly promoted by the US.

While taking note of the geopolitical sea change, the American media remained wary of the prospects for bilateral trade. Some newspapers characterized the China market as illusory, given that China, a nation with a population five times greater than the US, had a GNP only about 7 per cent of that of the US. A headline in the *Wall Street Journal* could hardly have been more explicit: "Illusory Market: Trade with China, Long a Dream of Americans, Remains Only a Mirage". Its author made no attempt to conceal his sarcasm:

> Since the U.S. embargo on China trade was lifted last June, trade has totaled about $5 million; all of this has been through third parties because the Chinese still refuse to deal directly with American firms. From this tiny level, trade has nowhere to go but up (Galeota 1972: 1).

A more temperate assessment by a *New York Times* journalist expressed a widely held view: "In straight economic terms, it is difficult to see United States trade with Communist China amounting to a great deal for years to come" (*The New York Times* 1971: 34). An editorial in the same paper commented that

> in the short run, there are fairly narrow constraints on how much trade can take place bilaterally between China and the United States. Chinese economic capacities are extremely limited – per capita income is about $120 a year. Total Chinese exports are only about one-tenth those of Japan. […] There are many goods China would like to import from the United States, such as locomotives, industrial chemicals, fertilizers, construction equipment, steel mills, machine tools, wheat – which this country can produce in abundance. But China's

> ability to pay is tightly bound by her narrow export list. […] Since June [1971] when trade with China was opened, total American imports from that country have amounted to a mere $5 million (*The New York Times* 1972: 38).

Many Americans believed that China would be unable to "finance any great increase of imports until it can begin to earn enough foreign exchange by increasing its own exports" (Jones 1971: F1). Hence, the growth of Sino-American economic relations would likely depend on US "willingness to extend export credits or other forms of aid to China" (*The New York Times* 1972: 38).

Little business had been transacted by 1972 when President Nixon visited China. In spite of the general success of Nixon's mission, the diplomatic relationship between the two nations was not normalized until January 1, 1979 – lagging behind around 100 other countries that already recognized the PRC (Martellaro 1982). The "quiet" years in US-China relations between 1972 and 1978 were the product of US-Soviet détente and China's consequential weak bargaining position, political opposition within mainland China, the Watergate scandal, and the death of Chinese leaders Mao Zedong and Zhou Enlai – all of which had a bearing on the shape and timing of the strategic triangle formed between the three great powers. However, in 1977 the Soviet invasion of Afghanistan and the appearance of Soviet combat troops in Cuba undermined US-Soviet cooperation. "As the Soviet Union came to appear more ominous, China grew more valuable to the United States as a strategic ally" (Ross 1986). Efforts and adjustments by both the American and Chinese governments led to the establishment of diplomatic relations in 1979.

By the 1970s, international trends also validated the cementing of official diplomatic relations between the US and China. The other major developed countries had already renewed business with the PRC, in keeping with their early diplomatic recognition of the country in 1950 (Sweden, Denmark, Finland), 1954 (Norway), 1964 (France), 1970 (Canada, Italy), 1972 (UK, Japan, Germany, Australia, New Zealand), and 1973 (Spain). In January 1978, China signed a treaty with France for the exchange of science and technology, followed in February by an eight-year, 20 billion USD trade pact with Japan. Japan, France, West Germany, Canada and the United Kingdom became China's chief creditors and suppliers of scientific and technological expertise. Japan, China's leading trading partner, accounted for 25 per cent of total Chinese imports and exports in 1977-1978 (Szuprowicz 1979). Mindful of the above international rivalry, as well as 1784 when Americans made their first voyage to China as latecomers to the China market, a China specialist in the US warned that "the United States is daily missing opportunities by its procrastination on normalization" (Totten 1978: C5).

With full diplomatic relations established, the United States and Chinese governments set out to clear the remaining legislative and administrative hurdles and move trade relations forward. On May 11, 1979, US Treasury Secretary Michael Blumenthal and Chinese Finance Minister Zhang Jinfu reached a settlement on the 280 million USD worth of claims and assets resulting from the reciprocal confiscation of assets and property that had followed the outbreak of the Korean War in 1950 (Devane 1978; Martellaro 1982). The next twelve months saw a wide range of developments encouraging the full normalization of trade relations including a bilateral trade agreement; the opening of the first American law firm (Coudert Brothers of New York City) in mainland China since 1950; US assistance with Chinese hydroelectric power development, consumer goods manufacturing, and petroleum production and transportation; export-import bank credits; approval for expanded arms sales to China; and a Chinese commitment to exporting scarce strategic materials.

Most importantly, on 24 January 1980 Congress passed a trade agreement conferring Most Favoured Nation (MFN) status on China. This measure exempted Chinese exports to the United States from the high tariff rates stipulated by the Smoot-Hawley Act of June 1930. Enacted at the start of the Great Depression, this piece of legislation epitomized American protectionism and was subsequently used to distinguish friends from foes among its trading partners (US Department of State n.y.). Despite this move, China's MFN trade status (which was not granted permanently) created new legal and political impediments to Sino-American trade relations which were not removed until 2001. Under US law, the normalizing of trade relations placed the People's Republic within the purview of the Jackson-Vanik Amendment contained in Title IV of the 1974 Trade Act. Regarded as the most important human rights legislation ever passed by the US Congress, the Jackson-Vanik Amendment links trade benefits with the human rights policies of communist (or former communist) countries and was originally directed at Russian restrictions on Jewish emigration to the United States. Not only does it deny preferential trade relations to offending nations, but

> such a country shall not participate in any program of the Government of the United States which extends credits or credit guarantees or investment guarantees, directly or indirectly (U.S. Code Online 2007).

Viewing the amendment as a major barrier to membership in the World Trade Organization (WTO), Russia has long urged the United States to repeal this measure, a move which would require legislation by Congress. The US president has the authority to waive the application of the Jackson-Vanik Amendment to a particular country, and Congress must review the president's semi-annual reports on that country's continued compliance in upholding rights to freedom of emigration. Therefore, the Jackson-Vanik Amendment provided the legal grounds for the annual Congressional renewal of China's MFN status until 2001 when China joined the WTO, whose rules prohibit members from imposing such trade restrictions on other members.

Tables 1 and 2, compiled from US and Chinese sources respectively, present data for the first decade of renewed commercial activity between the two countries. Both tables show continued growth, but at quite low levels, with a hiccup from 1975 to 1977 with respect to US exports to China. Nevertheless, with the exception of 1979 and 1980, the two sets of figures rarely correspond. Especially noteworthy is the fact that, during this period, America's trade with China never amounted to more than 1 per cent of total US trade worldwide – a situation very similar to US trade relations with China in the 18^{th} and 19^{th} centuries. Overall, during this period the US sold more than it bought from China. By the end of the decade, however, the total business conducted between the two nations was doubling each year, from 1.1 billion USD in 1978 (US figures; Chinese statistics recorded 991.7 million USD), to 2.3 billion USD in 1979 (Chinese figures: 2.4 billion USD), to 4.8 billion USD in 1980 (Chinese figures were almost the same).

Table 1: Sino-American Trade, 1971-1980 (US Figures)

Year	US Imports from PRC	US Exports to PRC	Total Bilateral Trade	US Trade Balance	Per cent of Total US Trade	Per cent of Total PRC Trade
1971	4.7	0.0	4.7	-4.7	0.0	–
1972	32.2	60.2	92.4	28.0	0.1	–
1973	63.5	689.1	752.6	625.6	0.5	–
1974	114.4	806.9	921.2	692.5	0.4	–
1975	157.9	303.6	461.6	145.7	0.2	–
1976	201.5	134.4	335.9	-67.1	0.1	–
1977	200.7	171.3	372.1	-29.4	0.1	2.5
1978	324.0	820.7	1,144.6	496.7	0.3	5.4
1979	592.3	1,724.0	2,316.3	1,131.7	0.6	7.9
1980	1,058.3	3,754.4	4,812.7	2,696.1	1.0	12.7

Note: In millions of current US dollars (in the American system, 1 billion = 1,000 million, 1 trillion = 1,000 billion).

Source: Harding 1992: 364.

Table 2: Sino-American Trade, 1971-1980 (Chinese Figures)

Year	PRC Exports to US	PRC Imports from US	Total Bilateral Trade	China Trade Balance
1971	–	–	–	
1972	9.6	3.30	12.90	6.30
1973	39.72	220.66	260.38	-180.94
1974	102.86	372.85	475.71	-269.99
1975	128.88	341.83	470.71	-212.95
1976	156.04	160.64	316.68	-4.60
1977	179.63	114.62	294.25	65.01
1978	270.60	721.10	991.70	-450.50
1979	595.01	1,856.59	2,451.60	-1,261.58
1980	981.06	3,830.21	4,811.27	-2,849.15

Note: In millions of current US dollars.

Source: Tao 2004: 339 and own calculation.

From the late 1970s, when China embarked on the "Four Modernizations" – of agriculture, industry, science and technology, and the military

– raw materials such as iron and steel (rather than technology and industrial equipment) formed the bulk of China's imports. In 1977 China spent 22 per cent of its foreign exchange on iron and steel, followed by foodstuffs (17 per cent), chemicals (12 per cent), transport equipment (9 per cent), and textile fibers (7 per cent) (Szuprowicz 1979: 11). US exports reflected this: In 1978 the US sold China cereals, raw textile fibers and waste, machinery, fertilizers, and vegetable oils and fats, while the chief items exported by China were feathers, cotton fabrics, basketwork, fireworks, pig bristles, and various kinds of mats and matting screens (Varg 1980). It needs to be said that this situation also reflected continued American restrictions on exports of technology and equipment.

The excitement of these historic developments as well as the lure of the China market generated considerable enthusiasm in America:

> Within weeks of diplomatic recognition, seminars and conferences on trade with China proliferated throughout the country (U.S.), playing to packed houses of several hundred business executives at a time. U.S. Department of Commerce officials reported an average 350 calls a day and a flood of inquiries in the mail. Teng Hsiao-ping's [Deng Xiaoping's] pointed interest in automobiles, petroleum equipment, and aircraft manufacturing plants gave an additional impetus to the snowballing interest in Chinese markets (Szuprowicz 1979: 9).

The Second Decade, 1981-1990: Rapid Economic Expansion and the Barriers to Success

Throughout the 1980s, the normalization of political relations and China's nascent economic reforms paved the way for an acceleration in the exchange of goods, values, ideas, personnel, and technology. This two-way trade was mutually beneficial; although, from the US point of view, the China trade was still small beer. Nevertheless, by 1984 the US had become China's third-largest trading partner, trailing only Japan and Hong Kong, then still a British colony. As America's fourteenth-largest trade partner, on the other hand, China accounted for a paltry 1.7 per cent of total American foreign trade in 1988 and 2.2 per cent in 1990 (Shi 1985; Harding 1992: 145-154). While these developments represented a strengthening of the web of mutual relations, they also planted the seeds for new issues and conflicts that subsequently caused fierce debate in the 1990s. In the 1980s, the commodities traded between the two countries were complementary rather than competitive. The two nations, however, differed on the extent of China's exports and the trade imbalance, despite the fact that statistical discrepancies hadn't yet become a major issue.

During this period, both the United States and China recognized that, in the words of the former US Consul General in Hong Kong,

> we are not each other's adversary, that we share important common security interests globally, and in Asia, and that our cooperation is crucial to peace and stability in East Asia (Williams 1989).

In addition, this decade witnessed the initial phase of Chinese economic reform. In 1979, China took its first steps towards reforming the planned economy that had been built on the Soviet model. This "second revolution", led by Deng Xiaoping and Zhao Ziyang, made China a serious competitor in the world economy and brought prosperity to more Chinese than at any time since the founding of the People's Republic in 1949. Changes in rural land ownership and the introduction of private farming and a decentralized pricing regime spearheaded the steady advance of the Four Modernizations. With growing market access, peasants farming contracted land under the household responsibility system had real incentives to work hard and seek new avenues of profitability. The household contract system led to a surge in grain output in the years 1978-1984, strengthening China's ability to feed 22 per cent of the world's population on only 7 per cent of its arable land. The new policies encouraged the proliferation of village and township enterprises, which set the stage for further market-led reforms. In the industrial sector, the central government gradually loosened its control over state-owned enterprises (20 per cent of which recorded losses in 1986 (Gamer 2003)), while permitting dynamic rural industries and joint stock companies to diversify their industrial production as well as to expand market outlets. As competition increased, profitability criteria began to extend to state-run industries. Managers were given greater freedom in hiring and firing (Naughton 2007: chapter 4).

The restructuring of the domestic economy coincided with China's opening up to the outside world. Here, the position of Hong Kong as an entrepôt linking East with West proved crucial. The first step in connecting China to global trade involved harnessing Hong Kong's trading power in world markets by encouraging Hong Kong firms to sign export-processing contracts with businesses in the newly established Special Economic Zones in the provinces of Guangdong and Fujian. Direct international trade grew apace as well. By the mid-1980s the number of companies engaged in direct export and import had increased dramatically, and the central government relaxed controls over local agencies and prioritized revenue-creation. The government also offered tax incentives to both domestic and foreign investors, which virtually turned China's entire littoral into a lucrative export-processing zone (Naughton 2007: chapter 16). These dual trade reforms resulted in the annual growth of around 10 per cent in China's GNP from 1983 to 1987 and a 15.8 per cent annual expansion in international trade (Harding 1992: 145-154). China's foreign trade almost tripled from 20.6 billion USD in 1978 to 60.2 billion USD in 1985 (Lee and Lo 1988). The acceleration of China's international trade was reflected in its trade with the US – but here the growth was sevenfold, from about 1 billion USD to over 7 billion USD during the same period.

One noteworthy change facilitating US-China economic relations was the steady liberalizing of controls over American exports of advanced technology. In 1980, such exports to China were reassigned from category Y (the Warsaw Treaty countries) to category P (new US trading partners), and then, in May 1983 under the Reagan administration, to category V (American allies). A three-tiered system of export licences further streamlined the licencing process, placing 75 per cent of export licence applications in a "green zone" under the sole control of the US Department of Commerce.

In contrast to the heavy emphasis on iron and steel in the 1970s, in the 1980s Chinese imports from the US diversified to include grain (699 million USD in 1988), chemicals and industrial raw materials (596 million USD), fertilizer (379 million USD), instruments and communications and transportation equipment (905 million USD), wood products, and chemical fibers. In the second half of the decade, finished manufactures and technologically advanced products began to enter the Chinese market. Among American imports from China, textiles and clothing accounted for more than 40 per cent of the total value of Chinese exports to the United States (Shi 1985). After Hong Kong and Macau, the United States was the largest investor in China, with about 3 billion USD in assets by 1985.

Following the Chinese economic reforms of the 1980s, US companies manufacturing consumer goods were increasingly drawn to the Chinese market. American companies entered the country by forming joint ventures with a Chinese company or government agency. Early participants included H. J. Heinz; R. J. Reynolds Tobacco; Coca-Cola; American Express; American Motors; AMF, Inc.; General Foods; Beatrice; Gillette; Pepsi-Cola; Eastman Kodak; AT&T; Nabisco; and Bell South. By 1985, four Coke bottling plants were operating in Beijing, Guangzhou, Xiamen, and Zhuhai, and by 2000 Coca-Cola had invested 1.2 billion USD in 23 plants, accounting for 70 per cent of China's domestic soft drink market. In spring 1985, the Great Wall Sheraton Hotel in Beijing became the first internationally managed concern in China to accept American Express (Eatlack and Lucker 1986).

The Road to Conflict: The Problem of Re-traded Goods

While US-China trade advanced at breakneck pace, the two nations differed on the extent of trade and the trade imbalance, which eventually fuelled the wrangling over statistics that began after the Cold War came to an end and that continue to this day. The most striking discrepancies in American and Chinese trade statistics, as illustrated in Tables 3 and 4, centred on disagreements over the extent of China's exports. In 1984, for example, the *Los Angeles Times* reported that the bilateral trade figure had hit a record 6.1 billion USD, 50.6 per cent higher than in 1983. The Chinese claim of a deficit here was disputed by American data, with US officials

> insisting that two-way trade balanced at 3 billion for each side, whereas China claimed a 1.5 billion trade deficit. Washington concluded that the numbers were concocted by the Chinese in order to extract concessions from the U.S. in talks on textiles and other trade negotiations (*Los Angeles Times* 1985: OC-C2).

And while official US estimates of Chinese exports varied to some degree, the figures were relatively consistent on American exports to China (Lampton 2001: 382).[5] US statistics show that 1986 was a turning point, with a 1.67 billion USD trade deficit against the US which not only made the previous year's 9.9 million USD deficit look paltry, but also kicked off a deep 20-year trade deficit with the People's Republic. In stark contrast, the Chinese figures for 1986 show a more than 1 billion USD deficit against the PRC – one point on the long curve of a trade deficit stretching from 1973 through 1992.

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5 The figures adopted by David Lampton differ from those quoted above from Harry Harding. According to Lampton, e.g., Chinese exports to the US from 1981 to 1990 were valued at 2,062 million USD; 2,502; 2,477; 3,381; 4,224; 5,241; 6,910; 9,261; 12,901; and 16,296 million USD respectively.

Table 3: Sino-American Trade, 1981-1990 (American Figures)

Year	US Imports from PRC	US Exports to PRC	Total Bilate-ral Trade	US Trade Balance	Per cent of Total US Trade	Per cent of Total PRC Trade
1981	1,865.3	3,602.7	5,468.0	1,737.4	1.1	12.7
1982	2,283.7	2,912.1	5,195.8	628.4	1.1	12.7
1983	2,244.1	2,176.1	4,420.2	-68.0	0.9	10.2
1984	3,064.8	3,004.0	6,068.8	-60.8	1.1	11.8
1985	3,861.7	3,851.7	7,713.4	-9.9	1.4	10.9
1986	4,770.9	3,105.4	7,876.3	-1,665.5	1.3	10.5
1987	6,293.5	3,488.4	9,781.8	-2,805.1	1.4	11.8
1988	8,512.2	5,022.9	13,535.1	-3,489.3	1.7	13.2
1989	11,988.5	5,807.4	17,795.9	-6,181.1	2.1	16.1
1990	15,223.9	4,807.3	20,031.2	-10,416.6	2.2	17.6

Note: In millions of current US dollar.
Source: Harding 1992: 364.

Table 4: Sino-American Trade, 1981-1990 (Chinese Figures)

Year	PRC Exports to US	PRC Imports from US	Total Bilateral Trade	China Trade Balance
1981	1,505.79	4,382.53	5,888.32	-2,876.74
1982	1,619.25	3,716.75	5,336.00	-2,097.50
1983	1,720.17	2,321.67	4,041.84	-601.50
1984	2,299.71	3,663.38	5,963.09	-1,363.67
1985	2,651.60	4,373.36	7,024.96	-1,721.76
1986	2,466.43	3,527.09	5,993.25	-1,060.66
1987	2,962.66	3,809.36	6,772.02	-846.70
1988	3,209.96	5,651.93	8,261.89	-2,441.97
1989	4,410.00	7,860.00	12,270.00	-3,450.00
1990	6,580.00	5,190.00	11,770.00	-1,390.00

Note: In millions of current US dollar.
Source: Based on Tao 2004: 339-340; figures adjusted by the author.

The above statistical differences, in hindsight, had paved the road to escalated frictions later on. Nevertheless, both sides in the 1980s recognized the rapid growth that had taken place in their commercial relationship since the establishment of diplomatic relations in 1979 – an annual average growth rate of 44 per cent (Shi 1985). The controversy over the bilateral trade imbalance calls for an analysis of a complex array of local, regional and international factors. The disagreements over the size and causes of the deficit originated in a number of areas: the two sides' different accounting approaches to re-exports to and from China via Hong Kong; US policy constraints on exports to China; the role of foreign firms in China; the multinational trade in commercial services; and global outsourcing and capital flows in the increasingly interdependent East Asian and world economy. Here, we will focus on one of these disputed areas – whether American exports and imports channelled through Hong Kong should be considered part of US-China trade.

In the 1980s, Hong Kong's intermediary role in connecting China with the world was vital to the national economy. In the mid-1980s, over 30 per cent of China's foreign exchange passed through Hong Kong. The United States was the largest foreign investor in Hong Kong with 54 per cent of the total, followed by Japan (21 per cent) and the United Kingdom (7 per cent) (Mun and Chan 1986). In 1984 the US was the leading export market for Hong Kong with about 7.8 billion USD worth of exports, and was the colony's second-largest re-export market, handling trade worth approximately 1.5 billion USD. In 1984, China provided 25 per cent of Hong Kong's imports (and 45 per cent of its food imports), overtaking Japan as the territory's leading supplier. In the same year, American exports channelled through Hong Kong to China amounted to 375.9 million USD, while China in turn exported over 1,125 million USD worth of goods through Hong Kong to the US (Mun and Chan 1986). The Chinese insisted that these Hong Kong re-exports accounted for 50 per cent of China's total exports to the US that year (almost one third in the US statistics).

According to Chinese trade figures, 60 per cent of Chinese exports to the United States were initially consigned to buyers in Hong Kong who resold them to a third party, who then shipped them to the US. On top of this, a further 20 per cent of Chinese exports to the US were re-exported via a third country (Tao 2004: 340; Tong 2005). Although the Chinese accepted that such goods had originated in China, they argued that the 40 per cent to 100 per cent appreciation accrued through re-export markups should not be computed as China's direct imports to the US. They argued, for example, that the added value of re-exports to the US in 1992 and 1993, amounting to 5.23 billion USD and 6.3 billion

USD respectively, should be deducted from Chinese export figures for those years.

Although US trade statistics did not record goods traded to China via Hong Kong, they did trace the countries of origins of all imports, including re-exported goods. Similarly, prior to 1993 the Chinese authorities did not keep an account of the final destinations of goods exported through Hong Kong – figures which might have compromised the value and volume of Chinese exports to the American market. The differences in accounting practices suggest that "the discrepancies between official trade figures may be brought down by as much as three-quarters when adjustments are made" (Tong 2005).

Economic Relations in Perspective

One way of putting the 1980s in perspective is to ask how important the Sino-American business relationship was to each side. A balanced answer to this question involves a close look at the multifaceted relationship.

First, in the closing years of the 1980s, economic factors had assumed a weight that both sides could no longer discount. As we have seen, initially Sino-American rapprochement was based primarily on geopolitical considerations, driven by US-Soviet and Chinese-Soviet rivalries during the Cold War and with no immediate impact on their respective economies. Within a decade, things had changed markedly. At the beginning of the Bush administration in 1989, American direct investment in China stood at 284 million USD, and an estimated 100,000 American jobs were dependent on exports to China (not including "service" exports). China had also begun to play a role in the US Treasury notes and bond market (Lampton 2001: 113).

Second, in the 1980s, the growing involvement of Congress and political lobby groups in making China policy reduced the power of the executive branch and its ability to engage in the kind of clandestine diplomacy that had led to the thawing of relations in the early 1970s. The annual renewal of China's MFN status was a continuing irritant for the Chinese until China's accession to the WTO in 2001. By law, members of Congress were at liberty to raise any concerns about China, especially human rights issues, and the president was obliged to respond. The heated debate over China made an annual spectacle on Capitol Hill, particularly after 1989, as Congress, the president, the Chinese and other interest groups wrangled over the issues. The result was that the business relationship of the two nations became embroiled in complex and potentially destabilizing issues of foreign policy, trade, ideology, technology, domestic politics and the economy. Looking back, in 2005 James McGregor, former China bureau chief of the *Wall Street Journal* and corporate executive, offered his rule of thumb on the relationship between trade and politics:

> Technology companies doing business in China require significant investments in proactive government relations in Washington. The mission isn't only to make friends, but to educate officials (McGregor 2005: 186).

Otherwise, such firms "could find their business short-circuited by political storms" (McGregor 2005: 188). This lesson was as important then as now.

Third, the problems experienced by both sides were largely a natural consequence of the rapid advances in communication between two vastly different societies. For example, in 1979, the first Chinese Joint Venture Law came into effect, representing a step forward in opening China to foreign investment. In the following three years, a long list of new organizations and regulations were created, intended to attract and channel foreign funds. However, in the first half of the 1980s, the much anticipated "floodgate" failed to eventuate as far as investment from the US was concerned. A sampling of American concerns over the commercial environment in China published in a US business journal in 1983 supplies some reasons for this:

- China is seen as a potentially large but statistically under-defined market.
- As a centrally planned economy, sales are based largely on contracts rather than autonomous purchasing decisions.
- Investment support can be costly, including office expenses in China and the considerable requirement for top executive time, travel and attention.
- Unknown relationships between, and unproven control over, future material costs, labour rates and other factors of production make productivity increases and profits difficult to project.
- The evolving legal and regulatory structure is sufficiently new – and experience with its operational interpretation is sufficiently lacking – that faith rather than precedent must be the basis of a potential investor's analysis of risk (Ruggles 1983).

Chinese concerns were similar. From their perspective, potential problems

> can be attributed to the mutual lack of experience and inadequate understanding of each country's laws, accounting systems, markets, pricing policies, management systems, fund-raising methods and the financial situations of the enterprise concerned (Ruggles 1983).

Rapid commercial growth sometimes resulted in a major backlash. As more and more Chinese textile products entered the American market, China provoked the ire of the American textile industry and its powerful political supporters, triggering surging protectionism in the US. In reaction to its escalating global trade deficit and increasing pressure from the manufacturing sector in the 1980s, the US Congress moved to create legal barriers to Chinese textile imports. Under the Multifiber Agreement and the Agreement on Textiles and Clothing (ATC) that governed the international trade in textiles and apparel from 1974 through 2004, developed countries could unilaterally impose quotas on the quantities and categories of textile imports from developing countries to prevent disruption to existing markets. During the seven years from the signing of the first Sino-American agreement on textiles in 1980 to the third accord in 1987, the categories of Chinese textiles restricted by quotas grew from 8 to 87, and over 85 per cent of Chinese exports were put under the quota system. From 1987 through 1991, the period covered by the third agreement, the permitted annual growth rate for Chinese textile exports was 3 per cent, dropping from 19 per cent in previous years.

The fourth major element in the economic developments of the late 1980s was the surging American anxiety over the trade deficit with China – just one aspect (but an important one) of the growing international debt accrued by the US, rising from 26 billion USD in the late 1970s to 126 billion USD in 1988. The China trade imbalance, like that with Japan and Taiwan, led to domestic demands in the US for counter-protectionist measures as well as calls for the further opening up of the Chinese market and increasing the transparency of trade rules (Chang Bloch 1997).

As China's economic reforms took root and gradually lifted millions out of poverty, the lure of China as a potentially sophisticated consumer market became a reality for the first time. Beginning in 1992, as it emerged from the shadow of the Tiananmen Square events, China embarked on a second phase of economic reforms. American corporations began to see the People's Republic as more than a processing centre with low labour costs for them to produce goods intended largely for their own domestic markets.

Despite the four significant areas of change identified here, the importance of bilateral trade in this period should be kept in perspective. It would be fanciful to subscribe to the notion that both sides were critical to each other's economies and polity. Taiwan provides a useful reality check: With a population of slightly more than 22 million, Taiwan's area is only 32,260 square kilometers; it's smaller than Maryland and Delaware combined. Nevertheless, with 82 billion USD in foreign exchange reserves – the largest in the world in 1992 – and a per capita income of 10,000 USD a year, in the 1980s Taiwan ranked sixth among America's trade partners, while the US was Taiwan's leading foreign trader (Bernkopf Tucker 1994: 168).

The "grand bargain" concluded by Richard Nixon, Mao Zedong, Jimmy Carter, and Deng Xiaoping had helped stabilize Sino-American relations since 1972 (Lampton 2001: 2). As the 1980s drew to a close, the American business relationship with the People's Republic of China was stronger than ever. Nevertheless, a decade of sustained improvement in Sino-American relations suffered a serious setback sparked by the Beijing crisis in 1989. In June 1989, in defiance of mounting domestic and international pressures, the Chinese government called in troops to bring student protests in Beijing's main public square to a violent end. In the months that followed, American political and economic sanctions and the Chinese government's continuing crackdowns on political dissidents undermined the framework of collaboration built up by both sides since 1972. The strains that resulted from the events in Tiananmen Square in 1989, along with the end of the Russian-American standoff during the Cold War, ultimately led to the end of "a decade-long strategic alliance" between the US and China (Yan 2002).

1990-2009: Economic Advances and Political Frictions in the Wake of the Cold War

Sino-American economic relations following the collapse of the Soviet Union fall into two phases, 1990-2001 and 2002-2009. These phases can be marked by certain geo-economic and geopolitical watersheds: China's rejuvenated economic reforms and accession to the World Trade Organization; a series of political conflicts; the world economic downturn; and the events of 9/11. The destruction of the Berlin Wall in 1989 presaged the collapse of communist regimes in Eastern Europe and the dissolution of the Soviet Union over the ensuing two years. As the common threat of the Soviet Union dissipated, China and the United States drifted into an uneasy relationship in which their steadily developing economic ties belied the uncertainties of the volatile geopolitical domain. Trade and investment relations weathered a steady flow of political crises. By 1993, China had attracted 27 billion USD in foreign direct investment, second only to the United States that had accrued 32 billion USD in investment from foreign sources in that year. After Hong Kong and Taiwan, the United States became the biggest investor in China (Yang 1995). However, despite the increased flow of information and ideas, political irritations continued to disturb relations between the two countries. The level of economic activity was out of step with the strategic relationship.

Overall Trade Performance

The figures in Tables 5 and 6 reveal a number of significant economic trends. First, China is on course to become the second-largest economy in the world after the US. According to US foreign trade statistics, China overtook Mexico as its second-largest trading partner in 2005 and 2006. The total value of Sino-American trade for these two years was 285.3 billion USD and 343 billion USD respectively – behind the figures of 499.29 USD and 533.67 billion USD contracted for the same period with Canada, the United States' largest trading partner (U.S. Census Bureau various years a).

The second economic trend revealed by Tables 5 and 6 is that US exports to China were headed by a mix of raw materials and sophisticated technology – electrical machinery and equipment, power-generation equipment, aircraft and spacecraft, optics and medical equipment, oil seeds and oleaginous fruits, plastics and plasticware, inorganic and organic chemicals, iron and steel, and cotton. China in turn supplied the US not only with toys and games, furniture, apparel, footwear and footwear parts, iron and steel, plastics and plastic goods, leather and travel goods, but also with electrical machinery and equipment, power-generation equipment, and vehicles and vehicle parts.

Third, since joining the WTO in 2001, China's international exports have increased more rapidly than its exports to the US. Thus, [China's] fastest growth these days lies in Europe, Africa, the Middle East, South America and elsewhere in Asia – in other words, practically anywhere other than the United States (Bradsher 2007).

Table 5: Sino-American Trade, 1991-2009 (American Figures)

Year	US Imports from PRC / World*	US Exports to PRC / World	Total US-China / U.S.-World Trade	US-China / U.S.-World Trade Balance	Per cent of Total U.S. Trade
1991	19.0 / 488.2	6.3 / 421.9	25.6 / 910.1	-12.7 / -66.3	2.8
1992	25.7 / 532.7	7.4 / 448.2	33.1 / 980.9	-18.3 / 84.5	3.4
1993	31.5 / 580.7	8.8 / 465.1	40.3 / 1,045.8	-22.8 / -115.6	3.9
1994	38.8 / 663.3	9.3 / 512.6	48.1 / 1,175.9	-29.5 / -150.6	4.1
1995	45.6 / 743.5	11.8 / 584.7	57.4 / 1,328.2	-33.8 / -158.8	4.3
1996	51.5 / 795.3	12.0 / 625.1	63.5 / 1,420.4	-39.5 / -170.2	4.5
1997	62.6 / 869.7	12.8 / 689.2	75.4 / 1,558.9	-49.8 / -180.5	4.8
1998	71.2 / 911.9	14.3 / 682.1	85.8 / 1,594	-56.9 / -229.8	5.4
1999	81.8 / 1,024.6	13.1 / 695.8	94.9 / 1,719.6	-68.7 / -328.8	5.5
2000	100.0 / 1,218.0	16.3 / 781.9	116.3 / 1,999.9	-83.7 / -436.1	5.8
2001	102.3 / 1,141	19.2 / 729.1	121.5 / 1,870.1	-83.0 / -411.9	6.5
2002	125.2 / 1,161.4	22.1 / 693.1	147.3 / 1,854.5	-103.1 / -468.3	7.9
2003	152.4 / 1,257.1	28.4 / 724.8	180.8 / 1,981.9	-124.0 / -532.4	9.1
2004	196.7 / 1,469.7	34.7 / 818.8	231.4 / 2,288.5	-162.0 / -650.9	10.1
2005	243.5 / 1,673.5	41.8 / 906	285.3 / 2,579.5	-201.6 / -767.5	11.1
2006	287.8 / 1,854	55.2 / 1,037	343 / 2,891	-232.5 / -817.3	11.9
2007	321.5 / 1,957	65.2 / 1,148.2	386.7 / 3,105.2	-256.3 / -808.7	12.5
2008	337.8 / 2,103.6	71.5 / 1,287.4	409.2 / 3,391	-266.3 / -816.2	12.1
2009	296.4 / 1,558.1	69.6 / 1,056.9	366.0 / 2,615	-226.8 / -501.3	14.0

Note: in billions of current US dollar, 1 billion = 1,000 million, 1 trillion = 1,000 billion.

* American world trade figures are based on data from U.S. Census Bureau (various years c). These figures were rounded and calculated by the author.

Source: 1991-1994 figures are based on U.S. Census Bureau (various years b); 1995-2009 figures are drawn from The US-China Business Council 2007b (20 December 2007 and 17 April 2010).

Table 6: Sino-American Trade, 1991-2009 (Chinese Figures)

Year	PRC Exports to U.S. / World	PRC Imports from U.S. / World	Total China-U.S. / China World Trade	China Trade Balance with U.S. / World	Per Cent of Total PRC Trade
1991	6.2 / 71.9	8.0 / 63.8	14.2 / 135.7	-1.8 / 8.1	10.5
1992	8.6 / 84.9	8.9 / 80.6	17.5 / 165.5	-0.3 / 4.4	10.6
1993	17.0 / 91.7	10.7 / 104.0	27.7 / 195.7	6.28 / -12.2	14.2
1994	21.5 / 121.0	14.0 / 115.6	35.4 / 236.6	7.5 / 5.4	15.0
1995	24.7 / 148.8	16.1 / 132.1	40.8 / 280.9	8.6 / 16.7	14.5
1996	26.7 / 151.1	16.2 / 138.8	42.9 / 289.9	10.5 / 12.3	14.8
1997	32.7 / 182.7	16.3 / 142.4	49.0 / 325.2	16.4 / 40.4	15.1
1998	38.0 / 183.7	17.0 / 140.2	55.0 / 323.9	21.0 / 43.5	17.0
1999	41.9 / 194.9	19.5 / 165.7	61.4 / 360.6	22.4 / 29.2	17.0
2000	52.1 / 249.2	22.4 / 225.1	74.5 / 474.3	29.7 / 24.1	15.7
2001	54.3 / 266.2	26.2 / 243.6	80.5 / 509.8	28.1 / 22.6	15.8
2002	69.9 / 325.6	27.2 / 295.2	97.2 / 620.8	42.7 / 30.4	15.7
2003	92.5 / 438.2	33.9 / 412.8	126.3 / 851.0	58.6 / 25.4	14.8
2004	125.0 / 593.3	44.7 / 561.2	169.6 / 1,154.6	80.3 / 32.1	14.7
2005	162.9 / 762.0	48.6 / 660.0	211.5 / 1,422	114.3 / 102.0	14.8
2006	203.4 / 969.0	59.2 / 791.5	262.7 / 1,760.4	144.2 / 177.5	14.9
2007	232.7 / 1,218.0	69.4 / 955.8	302.1 / 2,173.8	163.3 / 262.2	13.9
2008	248.4 / 1,428.6	81.1 / 1,133.1	329.5 / 2,561.7	167.3 / 295.5	12.9
2009	220.8 / 1,201.7	77.4 / 1,005.6	298.2 / 2,207.3	143.4 / 196.1	13.5

Note: in billions of current US dollar, 1 billion = 1,000 million, 1 trillion = 1,000 billion.

Source: Statistics for 1991-2000 are drawn from Tao 2004: 339-340 with adjustments by the author. For statistics on China's trade with the US for 2001-2006 and with the world for 1978-2006 respectively, see National Bureau of Statistics of China 2001-2007. The 2007-2009 figures are from *Caijing* 2008; the Ministry of Commerce of the People's Republic of China 2008, 2009, 2010; and the US-China Business Council 2007b.

From 2002 to 2009, China's international exports rose respectively by 22.3 per cent, 34.6 per cent, 35.4 per cent, 28.4 per cent, 27.2 per cent, 25.7 per cent, 17.2 per cent, with an exceptional decrease of 16 per cent in 2009 resulting from the global financial crisis. The corresponding figures in international imports were increases of 21.2 per cent, 39.9 per cent, 36 per cent, 17.6 per cent, 20 per cent, 20.8 per cent, 18.5 per cent, and a decrease of 11.2 per cent in 2009. During the same period, China's exports to the US increased by 22.4 per cent, 21.7 per cent, 29.1 per cent, 23.8 per cent, 18.2 per cent, 11.7 per cent, and 5.1 per cent, but reduced by 12.3 per cent in 2009. The fluctuation in imports from the US was 15.1 per cent, 28.5 per cent, 22.2 per cent, 20.6 per cent, 32.1 per cent, 18.1 per cent, 9.5 per cent, and -2.6 per cent. This trend, in part, reflects China's outward-oriented growth path noted above (Kaplinsky and Messner 2008), but on the other hand, it underscores China's avoidance of dependence on the US market, which it has achieved by diversifying its partnerships as a hedge against future uncertainty.

Fourth, throughout the 1990s and the first nine years of the 21st century, China was the fastest-growing export market for American firms. American exports to China rose from 6.3 billion USD in 1991 to 55.2 billion USD in 2006 – a massive increase of approximately 776 per cent – as opposed to a 146 per cent increase in the United States' total foreign exports from 421.9 billion USD in 1991 to 1,037 billion USD in 2006. For the period 2000-2006, American exports to China rose around 238 per cent while its international exports increased by only 32.6 per cent. In 2006 China was the United States' fourth-largest export market after Canada, Mexico, and Japan.

Fifth, according to the American figures, from 1995 to 2009 the US ran a trade deficit with China, which snowballed from 33.8 billion USD in 1995 to 266.3 USD in 2008 – an almost eight-fold increase over thirteen years. However, the American statistics also reveal a degree of instability in the economic relationship. For instance, between a 10.9 per cent growth in exports to China in 1998 and a 24.4 per cent increase in 2000, US exports fell by 8 per cent in 1999; and sandwiched between a 22.3 per cent increase in US imports from China in 2000 and a 22.4 per cent increase in 2002, a figure of only 2.2 per cent was recorded in 2001.

Sixth, transcending the frequent swings in the political relationship (if not completely immune to them), economic factors have played an important role in both countries, appropriate to the level of bilateral trade and investment (Jian 1994: 73). At the beginning of the 1990s, the total volume of bilateral trade was less than 3 per cent of total US trade; it would grow to nearly 14 per cent by 2009. Since 1980, China's trade with the US has varied between 10 per cent and 18 per cent of its total international trade volume. Clearly, both countries have benefited from expanded commercial links.

Major Developments in Economic Relations

From George H. W. Bush's time in office (1989-1993) through the Clinton years (1993-2001), and well into Barack Obama's presidency in 2009, the two powers weathered a number of critical developments that set their relationship on a new course. First, the "Beijing Spring" of 1989 has had serious repercussions, particularly for policymaking and mutual perceptions, right up to the present. The second development was the decoupling in 1994 of human rights issues from trade with China and the general use of economic issues as a political tool in the post-Cold War era. Third, this period saw China's accession to the World Trade Organization in December 2001 and continued business cooperation within the post-9/11 strategic framework. Fourth, early in the George W. Bush administration (up to 9/11), China became the main target of leading neoconservatives who asserted the "righteousness" of American power, disdained diplomacy, and championed American military operations overseas. The "neocons" continue to view China as "both a growing military threat and an ongoing moral challenge" (Pan 2006; Story and Laurie 2008: 163-165; Marshall 2003). Fifth, China's trade relations with the United States are being tested again in 2010 by a myriad of issues including the Chinese CNY currency, US arms sales to Taiwan, and President Obama's meeting with the Dalai Lama.

The first grave challenge to relations originated in the Tiananmen student protests in Beijing in May/June 1989, "a global video event" (Schaller 2002: 201) that put China under an unprecedented media spotlight. The Beijing Spring of 1989 was the most gripping news story of its time. As one American study reveals:

> The evening news shows of the three major networks (ABC, CBS and NBC) totaled five hundred seventy-seven China stories in the first six months of 1989, by comparison with forty-four stories in all of 1988. There were three hundred ninety-seven stories in these shows in the month between May 14 and June 14, 1989, by comparison with three hundred forty-four stories in the ten years (1972-81) before China was opened to American television coverage (Berlin, Terrill, and Iriye 1991: 13).

Extensive coverage of the official crackdown on the student demonstrations fired American outrage against the Chinese government, but also exposed the division between the executive and legislative branches of the US government in regards to their respective approaches to China issues, particularly human rights. On June 5, 1989, in a reaction to the crackdown, President Bush announced sanctions against the Chinese government including the suspension of a host of bilateral agreements: the nuclear cooperation agreement; investment guarantees regulated by the Overseas Private Investment Corporation; the Trade Development Program; the liberalization of export controls; and satellite export permits. However, convinced of the value of the bilateral relationship and optimistic that economic growth would ultimately bring about political democratization in China, Bush refused to bow to mounting pressure for further sanctions from both democrats and republicans in Congress. Despite this, Congress passed two pieces of legislation, one that suspended export licences for police equipment and one that froze Eximbank loans to China, in addition to granting Chinese students and academics the right to stay and work permanently in the United States (Harding 1992: 232-234). Washington and Beijing worked to keep the lines of communication open and sought ways to improve political relations, yet restoration of normal relations proved challenging. The events of 1989 focused US Congressional attention on American policy toward China, so that economic issues – especially the annual renewal of China's MFN status – quickly became a vehicle for debates over human rights, tougher economic sanctions, and revocation of China's MFN position (Yuan and Yang 1997).

Always intimately linked to the vagaries of politics, economic issues provided a lever to obtain concessions from China in the sphere of human rights. In the immediate aftermath of the Tiananmen storm, some critics doubted American enthusiasm for doing business with China. A cover story in the October 1990 issue of *The Atlantic* reflected this pessimistic outlook: "American business in China in the eighties fell victim to the naïve optimism with which it contemplated the vast 'China market'" (Chu 1990). To others, the China market was a chimera:

> U.S.–China bilateral trade totaled $18 billion in 1989, scarcely half of U.S. trade with Taiwan, and today direct U.S. investment in China amounts to less than half of one percent of direct U.S. investment worldwide. And these days Eastern Europe would seem to provide business with far more fertile ground (Chu 1990).

Despite fears that relations would continue to deteriorate, fear gave way to optimism when the predicted political chaos failed to materialize in China. After a two-year setback (1989-1991), China's transition to a market-oriented economy rolled on, symbolized by Deng Xiaoping's 1992 "Southern Tour" of Shenzhen and other Special Economic Zones (SEZ) in South China. Deng's strong endorsement provided momentum for a new phase of economic reform. This second phase, led by Jiang Zemin and Zhu Rongji, rested on regulatory and administrative restructuring of the banking, taxation, and corporate governance systems, as well as further exposure to world markets through China's membership in the WTO. This strong commitment to reform yielded some significant outcomes, positive and negative – price stability replaced rising inflation; the number of state-owned enterprises (SOEs) dwindled while private firms increased in number, hiring twice as many workers as the SOEs by the end of 2004; and increased market competition sharpened pressure on employers and employees alike, generating massive layoffs and fuelling social inequity. The US-China economic relationship survived Tiananmen, although 1989 marked the end of an era of improving relations between the United States and China. Looking back, it is clear that during the nineteen years from 1990 to 2009, the two countries bonded through economic engagement while seeking new mechanisms that would allow them to live with each other. While the shadow of Tiananmen still hangs over the relationship, the "friend-or-foe" model of political relations was at odds with the rapid growth in bilateral trade from 1990 to 2009.

The second major development in this period was the de-linking of human rights issues from the annual extension of China's MFN trading status in spring 1994. Less than two weeks after his inauguration in January 1993, with Tiananmen and his campaign trail attacks on President Bush's "soft" stance on China consigned to the back burner, President Clinton appointed Winston Lord to head the Senior Steering Group (SSG) charged with advising him on China's MFN status. On 28 May 1993, Clinton bypassed Congress and issued Executive Order 128590, linking the renewal of China's MFN status to seven conditions tied to human rights issues – free emigration, cessation of exports manufactured by prison labour, observation of the UN Declaration of Human Rights, preservation of Tibetan indigenous religion and culture, access to prisons for international human rights organizations, the permitting of international radio and TV broadcasts, and the release of political and religious prisoners (Clinton 1993: 771). Clinton's intervention represented a sharp departure from President Bush's position that political democratization would occur as China's economic conditions improved. Nonetheless, a year later, on 26 May 1994, the Clinton administration reversed this strong stance and decoupled human rights issues from the MFN status.

The new approach had the support of the business community, who argued that the "only way to undermine the regime is to infiltrate it". Trade with China came to be seen as a "moral crusade" and business executives asserted that "missionaries and businessmen will work together to change China, unless Congress interferes" (Kahn 2000).

This striking policy turnaround had three major implications. First, Clinton's rapid reversal of his 1993 executive order raised questions about the way in which moral issues such as human rights violations should be addressed in American politics and foreign policy (Morris 2000). Second, the China question became a "political football" in the US (Tao 2004: 322). The intense debate over China policy during both terms of the Clinton presidency (1993-2001) involved a wide spectrum of interest groups. On the one hand, the debate highlighted the checks and balances operating in the presidential prerogative over foreign affairs and Congress's role in handling trade issues under the US constitution. On the other hand, it showed the extent to which Sino-American relations had expanded since 1972, explaining the intrusion of the China question into American politics.

Third, this vacillating emphasis on human rights and economic interests set the tone for the constant swings in political relations in the years to come. During the eight years from 1993 to 2001, the absence of an enduring strategic foundation ensured that the only certainty about the relationship was its uncertainty. Relations were undermined by numerous crises, including military tensions between Taiwan and mainland China in 1995/96 (Friedman 2006; Marsh and Teufel Dreyer 2003); the Cox Committee report on alleged technology leakage to the People's Republic; the allegations against former Los Alamos scientist Wen Ho Lee; the bombing of the Chinese embassy in Belgrade in May 1999; and the American spy-plane incident of 2001. Yet, despite these setbacks, economic relations between the two nations continued their rapid expansion throughout these years.

The third major development in Sino-American economic relations during this period was the formal acceptance of China by the 142 member governments of the World Trade Organization (WTO) on 11 December 2001. This again highlighted the continuing disparity between booming business ties and strained political relationships in the post-9/11 world.

Although the WTO came into being on 1 January 1995, its predecessor, the General Agreement on Tariffs and Trade (GATT), dates back to 1948. China was one of the original signatories of the GATT, but withdrew from the organization in 1949 when the nationalists lost the civil war to the communist party. In 1986, China formally applied to rejoin GATT. However, it would require 15 years for it to become the 143rd member of the WTO. Set up to regulate international trade in commodities, over the years GATT evolved through several rounds of negotiations aimed at settling trade disputes. The last and largest of these was the Uruguay Round from 1986 to 1994, which led to the birth of the WTO. Reflecting changes in world trade, the WTO extended its purview to trade in services and intellectual property (WTO no year). Legally, WTO agreements and other instruments constitute binding rules intended to help exporters and importers trade as efficiently as possible. Beginning in 2001 the WTO hosted a new round of trade negotiations, the Doha Development Round, which collapsed in July 2006.

Joining the WTO prompted China to implement a new round of economic reforms aimed at increased prosperity, liberalization of trade, and integration into the global community. The financial sector was liberalized by allowing foreign banks to compete on the domestic market. China's WTO commitments included lower tariffs and non-discriminatory trading rights for both domestic and foreign private firms. The average tariff rate was reduced from 43 per cent in 1992 to 17 per cent in 1999 and to under 10 per cent by 2004. China also lowered average agricultural tariffs to 15 per cent. Many imports are now exempt from tariffs, and in fact many goods enter the country duty-free. As a result, in 2006 actual tariffs levied relative to the value of imports were only 2 per cent (Lardy 2007; Naughton 2007: 389-391).

Membership in the WTO has contributed to major growth in international trade and investment, matched by the widening scope and increasing sophistication of commercial operations both in China and overseas. In the space of 30 years, China has emerged from relative insignificance to become, in 2005, the world's third-largest trading nation after the United States and Germany (Naughton 2007: 377). In 1978, the total value of China's trade was 20 billion USD and in 2005 this figure had rocketed to 1.4 trillion USD. American exports to China increased by 81 per cent in the three years after China joined the WTO, compared with 34 per cent in the three previous years. Similarly, American imports from China rose by 92 per cent in the three years after China's WTO entry, but by just 46 per cent – exactly half this figure – in the three previous years (Frisbie and Overmyer 2006: 243-246).

As the business environment improved, American entrepreneurs spared no time in exploring new opportunities. Elite sports proved to be a promising area:

> Boosted by the popularity of Chinese center Yao Ming of the Houston Rockets, the NBA's China business is growing by 30 percent each year. The league's China operations already include three offices with about 50 staff (*The Associated Press* 2006: 15).

During an interview in Guangzhou, NBA commissioner David Stern – the architect of the league's push into the international market – said "the China market is our most important and largest market outside the United States" (*The Associated Press* 2006: 15).

Another development involves the Chinese automobile sector, which many feared would collapse when foreign competitors swarmed in following China's WTO negotiations. To meet WTO requirements, China reduced its tariff on car imports from 200 per cent to 25 per cent, and scrapped the import quota on automobiles in 2005. Despite price cuts on imported cars, auto sales soared at home and China began to tap export markets. Some 43,000 Chinese-made vehicles were exported in 2003, an increase of 96 per cent from the previous year, and auto exports surged to 173,000 units in 2005 (Liu 2006). In July 2007, Chery Automobile Co. Ltd., the largest Chinese auto exporter, and the Chrysler Group, the third-largest car manufacturer in the US, signed a cooperation agreement in Beijing.

The attacks on 11 September 2001 and the response that followed redefined the relationship between the United States and the world's 1.4 billion Muslims (Singer 2006). These events also had consequences for US-China relations, resulting in shifts in American attitudes toward the PRC (Lewis 2001). Prior to the 9/11 attacks, a series of statements by President Bush and others were widely seen as targeting China as a major strategic rival, rather than a strategic partner – a stance different from that taken by the Clinton administration (Yan 2002; Wu 2004; Karen 2001; Yuan 2002: 14). The 2001 *Quadrennial Defense Review Report* – largely prepared before 11 September but released on 30 September – implicitly identified China as a potential "military competitor" in the Asia-Pacific and a future challenger to American interests in the region:

> Although the United States will not face a peer competitor in the near future, the potential exists for regional powers to develop sufficient capabilities to threaten stability in regions critical to U.S. interests. […] The possibility exists that a military competitor with a formidable re-

> source base will emerge in the region. The East Asian littoral – from the Bay of Bengal to the Sea of Japan – represents a particularly challenging area (U.S. Department of Defense 2001).

In the aftermath of the 9/11 attacks, however, President Bush quickly sought to reassure China: "Our ties are mature, respectful and important to both our nations and to the world" (The White House, Office of the Press Secretary 2002a). In spite of this, the "National Security Strategy of the United States of America", released in September 2002, sent a mixed message about bilateral relations. First and foremost, it makes clear that America "seeks a constructive relationship with China" and welcomes "the emergence of a strong, peaceful, and prosperous China". Secondly, the report places Sino-American trade relations within the new post-9/11 strategic coalition framework. However, in the list of US allies and friends in the war against terror, China ranked not only after Canada, the European countries, Japan and Australia, but also after Russia and India. Ominously, the report warns that

> in pursuing advanced military capabilities that can threaten its neighbors in the Asia–Pacific region, China is following an outdated path that, in the end, will hamper its own pursuit of national greatness (The White House, Office of the Press Secretary 2002b: 25-28).

Needless to say, the report did not find a warm reception in China.

> Although in recent years Beijing has refrained from identifying Washington as an adversary or criticizing its "hegemonism," […] many Chinese still view the United States as a major threat to their nation's security and domestic stability (Wang 2005).

The major developments from 1991 to 2009 suggest that economic relations between China and the United States have continued to expand and deepen despite the lack of a stable political foundation. "The China question" is still a real political issue in the United States, although it was not as volatile in the opening years of the 21st century as it was in the 1990s (*Reuters* 2010; Locke 2010).

Conclusion: Toward a Sustained Economic Relationship

In just two decades, Chinese goods have taken the US market by storm while American signature products such as Coca-Cola, McDonald's, Boeing, Microsoft, and Hollywood movies have became household names in China. Although the two countries are now more tightly linked than ever before, divergent national priorities and geo-strategic frictions, as well as changing regional and global economic and strategic realignments, continue to challenge a relationship that is vital to both nations and to world peace.

Five interrelated vectors have molded the development of Sino-American economic relations since the 1970s. These are: the profound changes experienced by both the American and Chinese economies, the expanding economic engagement of both nations with East Asia and the world economy, the parallel growth of Chinese imports and exports, the US edge in commercial services, and the controversial rebalancing of the global economy and US-China relations. Consideration of all five is necessary for a balanced assessment of the performance of bilateral trade over the four-decade period.

First and foremost are the profound changes in both the American and Chinese economies and their impact on foreign trade, a factor that helps explain the US trade deficit with China. Until the 1970s in the US, the gap between government spending and taxes, and the gap between imports and exports, were both small. In the 1970s and 1980s, however, the US federal budget deficit soared, savings regularly exceeded investment, and the foreign trade balance moved deeply into the red. Borrowing to service the growing national debt became the order of the day. Some Chinese economists believed

> that the large share of the national economy financed by debt and the large share of the government budget allocated to interest payments will eventually bankrupt the U.S. economic system (Hu 1988).

American economists, however, still dispute whether reducing the budget would have positive effects on investment, economic growth, and the foreign trade deficit. Two senior economists assert that "it is by no means clear that the foreign trade deficit owes its existence to the budget deficit" (Walton and Rockoff 1998: 733-735). Rather, they attribute it to higher levels of imports from Canada, Mexico, Asia, Latin America, Eastern Europe, and other US trading partners. Nevertheless, policymakers in the 1970s and 1980s were concerned about both the deficit in the federal budget and the trade deficit.

It is against this background that America's trade imbalance with China has sparked debate. As one Chinese economist puts it, the US trade deficit with China in 2005 and 2006 was "the largest deficit it has ever recorded with a single economy in history" (Hong 2006). Critics of

China attribute the deficit to a raft of factors, most of which related to job losses in the US manufacturing sector and obstacles to US exports to China. These include the low cost of Chinese goods and services, arbitrary devaluation of the currency (CNY), market-access barriers, poor handling of intellectual property rights, and a low level of government transparency (Frisbie and Overmyer 2006: 245-246; Frisbie 2009).

Since 2003, China's new generation of leaders, Hu Jintao and Wen Jiabao, have built on the gains achieved in earlier phases of market reform to deliver economic benefits to a larger slice of the population, particularly those living in rural areas. China's WTO accession has not only liberalized its foreign trade and investment regime, but also "institutionalized the process of China's domestic reform externally through the force of WTO obligations" (Qin 2007). The WTO commitment, for instance, has prodded the Chinese government into easing limits on foreign ownership of domestic financial institutions and loosening restrictions on foreign investment in certain areas. In April 2007 four branches of foreign-funded banks – HSBC Bank (China) Co. Ltd., Standard Chartered Bank (China) Ltd., Bank of East Asia (China) Ltd., and Citibank (China) Co. Ltd. – were duly incorporated and began trading CNY retail business (Lan 2007). To enhance the protection of intellectual property, China has also mandated the installation of licensed operating software on all computers manufactured in China prior to sale – although implementing these rules throughout the country remains a challenge. Some economists downplay the significance of the gap:

> Given today's globalized manufacturing network, in which most products are made in a multi-stage process distributed across several countries, the bilateral trade balance has lost much of its economic meaning (Hong 2006).

One Chinese commentator takes this argument to an extreme:

> The bilateral trade balance is a hot issue in official discussions and news media. However, to economists it is a non-issue. A country's total trade deficit reflects the excess of its national spending over its domestic savings, and bilateral trade balances reflect international comparative advantages and consumer preference. They are topics in different areas of economics. Mixing them is a common mistake. […] We have to ask ourselves whether it is total trade balance or bilateral trade balance that we care about. More basically, for an international-currency country such as the U.S., one needs to ask why we should care about either at all (Cheng 2001: 253).

The second major factor impacting US-China economic relations is the shifting role of East Asia in the world economy. Despite its rapid increase in trade, over the decade from 1997 to 2006, China's share of the US global trade deficit remained static in percentage terms, increasing from 27 per cent to 28 per cent (The US-China Business Council 2007a). During the same period, however, the share of the American global trade deficit held by all East Asian countries declined from 70 per cent to 45 per cent, while the US trade imbalance with the rest of the world increased from 30 per cent to 55 per cent. The sharp fall in trade surpluses with the United States experienced by other East Asian nations is explained by the change of destination in Asian manufacturing and direct investment from the US to China. In 2004, funds from Hong Kong, Japan, South Korea, Singapore, and Taiwan accounted for nearly 60 per cent of foreign direct investment in China. According to Swiss investment bank UBS AG and the US-China Business Council, although more than 50 per cent of PRC exports by value are products of foreign companies operating in China, most of these firms are based in Hong Kong, Taiwan and Korea.

Consider toys, footwear, and laptop computers. In the 1960s and 1970s, Hong Kong was the centre of world toy manufacturing – until the entire industry moved to the mainland shortly after China reopened its doors to the outside world. The same phenomenon transformed the shoe industry in the 1980s when Taiwanese manufacturers relocated to the mainland. Laptop production followed suit twenty years later (Leng 2005). For many years, Taiwanese companies had accounted for 80 per cent of global laptop assembly. But, beginning in 2001, within five years they had transferred all production lines to China to take advantage of the mainland market. By 2006, 80 per cent of global laptop was assembled in China (Lardy 2007).

The integration of the stronger East Asian economies is primarily a business-driven phenomenon, combining China's low-cost manufactures and efficient export arrangements with capital from its wealthy regional partners. Since 2000, Asian investors have opened 20,000 manufacturing facilities a year in China, amounting to a wholesale shift in their operations. In the same period, East Asia accounted for approximately 26 per cent of world GDP, placing the region almost on par with North America (30 per cent) and Western Europe (32 per cent), and closing the gap rapidly. In 1960, East Asia's share of world GDP was only 13 per cent (Miller 2008: 195; Dent 2008).

The dynamic regional interpenetration extends to other commercial sectors such as pop culture. Aside from the success of Japanese *manga* and animation in Hong Kong, Taiwan, China, South Korea, Thailand, and Singapore, South Korea's cultural industry has also been creating waves in East Asian markets, as a story in an issue of the *Wall Street Journal* (Europe) illustrates:

> Tokyo. Thin and gorgeous in a slinky black dress, Mikimoto pearls and a low-slung diamond Tiffany pendant, 26-year-old Kazumi Yoshimura already had looks, cash and accessories. There is only one more thing this single Japanese woman says she needs to find eternal bliss—a Korean man. […] She may just have to take a number and get in line. In recent years, the wild success of male celebrities from South Korea — sensitive men but *totally* ripped — has redefined what Asian women want, from Bangkok to Beijing, from Taipei to Tokyo. […] Today, South Korea's trend-setting screen stars and singers dictate everything from what hair gels people use in Vietnam to what jeans are bought in China. […] Though the Korean Wave hit Japan relatively late, washing ashore only within the past 24 to 36 months, the country has quickly become the largest market for Korean stars. […] Almost all the major Korean male stars have opened lucrative 'official stores' in Tokyo. In the three-story boutique of Ryu Siwon, a baby-face[d] Korean actor-crooner who sings in phonetic Japanese for the local market, the top floor boasts a recreation of his living room, complete with a life-size[d], high-tech plastic model of Mr. Ryu lounging casually on a white leather sofa. It has become a meeting place of sorts for his Japanese fans, where a gaggle of women sat and stared longingly at his statue on a recent afternoon (Faiola 2006).

Reports from China echo the growing fascination among Chinese with things South Korean generated by the popularity of its television soap operas over the past 15 years. According to Kim Ha Joong, South Korea's ambassador to China, around 100 million Chinese viewers watch Korean soap operas every day. Such popular entertainment is beginning to determine fashion choices among young Chinese consumers:

> Li Chanjuan, a college student from Chongqing, is so crazy about Korean soap operas that she watches them day and night. […] When she watched *Full House*, a romantic story set in a beautiful house, she admired the lips and eyebrows of Korean actress Song Hye Kyo so much that she bought Etude lipsticks and eyebrow powder. […] Li has taken her admiration for South Korean products a step further. She buys only Samsung mobile phones and Korean dishes are always her first choice when she dines out (Lin 2007: 17).

The third major factor influencing the direction of bilateral business relations is China's increased openness to and dependence on international trade. The extent of this shift can be gauged by three separate measures: First, the growth rate of China's imports has kept pace with exports since 1998. In the six years following China's entry into the WTO (2002-2008), US exports to China increased by 341 per cent (Frisbie 2009). Not only was China the largest importer of high-value-added semiconductors, microprocessors, and airplanes in the world, but it was also an important export market for both raw materials and manufactures for a number of countries including Singapore, Malaysia, Taiwan, and Brazil. A report by Oxford Economics and the Signal Group in January 2006 concluded that "China was one of the principal locomotives of global economic growth" over the previous decade (The China Business Forum 2006: 3). Second, average import tariffs were lowered from over 50 per cent in 1982 to under 10 per cent in 2005 – a low figure compared with 2004 tariff levels in India (29.1 per cent), Mexico (18 per cent) and Brazil (12.4 per cent). This marked reduction in trade barriers is part of China's ongoing economic reform process aimed at making its market more accessible to foreign imports. Third, the surging ratio of imports to GDP in China – from 5 per cent in 1978 to 30 per cent in 2005 – is roughly twice the ratio in the United States (17 per cent) and more than three times that in Japan (10 per cent). It is also higher than the ratios in other large developing countries such as Argentina, Brazil, and India (Bergsten et al. 2006: 81-84).

The fourth factor affecting bilateral trade is America's advantage in commercial services, which are of course by no means restricted to the exchange of commodities. Commercial services include a large variety of trade-related activities such as data-processing, banking, accounting, insurance, education, legal counsel, management consulting, royalties and licence fees, telecommunications, and transportation and travel. As the world's largest importer and exporter of commercial services since the 1970s, the US ran a total surplus of 64 billion USD in 2003. In comparison, China has been a net importer of commercial services, especially since it joined the WTO in 2001. With China's trade deficit in commercial services reaching 9 billion USD in 2003, for example, the US has a golden opportunity in this lucrative sector (Tong 2005).

Fifth, in reaction to the post-2008 financial downturn, advocates for a new world economic order have suggested a rebalancing of global demand, which will arguably become a major, politically charged issue in

China's trade relations with the United States in the years to come (Geithner 2009; Samuelson 2010; Pearlstein 2010). There will no doubt be controversy over the definition of "imbalances" and the measures needed to address these "imbalances". To some, this means that the US will need to significantly reduce its deficit, save more and spend less, whereas emerging markets and economies with large surpluses – such as China – should spend more and reduce exports. On the other hand, pro-China critics argue that the characterization of China as a "currency manipulator" is unfounded, and that rebalancing the global economy will come about through fine-tuning the decision-making structures of the IMF, the World Bank and other international organizations, adjustments that would allow emerging economies to play a greater role in monitoring American economic policies (Zhang 2010). These disagreements, however, underscore the fact that US-China economic relations "play a large part in determining the future of humanity", as Edwin O. Reischauer rightly noted in 1976 (Fairbank 1976).

Over the past forty years, growing economic interdependence has quickly presented new challenges and opportunities in bilateral relations, with issues such as human rights, Most-Favoured-Nation status, the Taiwan and Tibet question, the huge US trade deficit, and the uncertain global economy threatening to cloud the relationship at times. With China's emergence as a major power and America's hegemonic ambitions tested in successive wars, the contradiction between a booming commercial relationship and conflict associated with geopolitical and ideological differences will continue to constitute a serious challenge to relations between the two nations. While Sino-American economic relations will continue to face challenges and setbacks, the long-term goal for each side will be to forge economic ties strong enough to create a stable political relationship, rather than to be held hostage by geopolitical constraints.

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