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China Ties Aiding Europe to Its Own Trade Goals

By KEITH BRADSHER



China's Premier Wen Jiabao

BEIJING — If China is going to help ease Europe’s financial crisis, silken strings could be attached.

Premier Wen Jiabao on Wednesday offered to help Europe. But, in an unprecedented move for China, he linked the offer to a potentially onerous demand: that Europe renounce its main legal defense against low-priced Chinese exports.

Mr. Wen urged the European Union to classify China as a “market economy” instead of a “nonmarket economy.”

In international trade legalese, the new designation would make it almost impossible for Europe to impose tariffs on Chinese goods considered unfairly cheap.

His remarks, in a speech at a conference in Dalian in northeast China, were the clearest move by China to link its continuing investments in Europe to specific changes in European trade policies. The linkage is being made as Beijing is showing a new willingness to use its vast financial resources to extend its political influence far from China's shores. On Monday China announced \$1 billion in subsidized loans to Caribbean nations.

Mr. Wen's comments Wednesday seemed to contain more pro quo than specifics about the quid. He was vague on whether China was prepared to increase its monthly lending to Europe by an amount that might ease the euro zone's budget and banking difficulties. He also was not specific about whether China was interested in buying European government bonds or making investments like acquiring more European businesses.

"We have been concerned about the difficulties faced by the European economy for a long time, and we have repeated our willingness to extend a helping hand and increase our investment," Mr. Wen said.

European stock markets were buoyed in part by his remarks.

China, with an estimated \$3.2 trillion in foreign reserves, is seen as potentially a global banker. But most of its lending has come in the form of buying nearly \$2 trillion in United States Treasury bonds and other forms of American debt. China already buys billions of euros worth of European debt each month, but that level of lending has done little to ease the euro zone's crisis.

So a vague promise of more "investment" in Europe, without specifying the amount or form, might not seem to European Union officials to justify granting China the new trade status Mr. Wen proposed.

The World Trade Organization has technical criteria for countries to decide when China has become a market economy, John Clancy, the European Union's trade spokesman in Brussels, said Wednesday. China has made progress, but has not met the criteria, in European Union's view.

"Since China dictates the speed with which market-oriented rules and laws are effectively enforced centrally and locally, the timing of the conclusion on its market economy status is largely in China's hands," Mr. Clancy wrote by e-mail.

The new market economy designation Mr. Wen seeks would let China avoid the steep import duties assessed on Chinese companies that sell goods in Europe for less than it costs to produce and market them — or what trade lawyers describe as the “normal value” of these goods.

Under the terms of China’s accession to the World Trade Organization in 2001, the country will automatically qualify as a market economy in 2016. But Mr. Wen on Wednesday exhorted European nations to “look courageously at China’s relationship from a strategic point of view” on the issue of market economy status. “If European Union nations can demonstrate their sincerity several years earlier,” he said, “it would reflect our friendship.”

China once before, in 2003, asked the European Union to grant it market economy status. That request was denied.

By classifying China as a nonmarket economy, the European Union allows its antidumping investigators to compare the price Chinese exporters to Europe charge with the price of goods from other low-cost countries. Antidumping duties, which can exceed 100 percent, are assessed if Chinese prices are lower.

But if China were labeled a market economy, antidumping investigators would have to compare the export prices Chinese companies charge with the prices they charge for the same goods in China. Virtually all prices in China are very low in terms of other currencies, partly because of China’s extensive intervention in currency markets to keep its currency, the renminbi, weak.

China’s critics also suggest that close links between many companies and the Beijing government make it impossible to assess the extent to which Beijing helps companies keep prices low at home, through subsidies, preferential loans or policies like free or discounted land for factories. So it would become extremely difficult to win an antidumping case if China were labeled a market economy.

China’s foreign exchange reserves surged \$350 billion in the first six months of this year, to reach \$3.2 trillion. While part of the increase reflected accrued interest and shifts in currency valuations, \$200 billion to \$250 billion appeared to be from the currency market intervention.

Based on its practice of keeping roughly a quarter of foreign exchange reserves in euros, mainly in European government debt, China bought \$50 billion to \$60 billion in euro-denominated holdings in the first half of this year. Economists and bankers say that China's extraordinary accumulation of foreign exchange reserves is largely accidental. Its top leaders have mandated that the renminbi not appreciate more than a few percent against the dollar each year, despite large trade surpluses and strong inward investment, and the central bank has been forced to buy dollars and euros on an immense scale to ensure that.

The central bank pays for the dollars and euros with renminbi that it raises mainly by requiring Chinese commercial banks to lend it a fifth of their deposits at very low interest rates. The Chinese central bank also sells notes and has resorted to issuing more renminbi. That has led to a steep increase in the money supply and has contributed to sharply rising prices within China for consumer goods and real estate alike.

Italian finance ministry officials met recently with officials from the China Investment Corporation, the country's sovereign wealth fund. When Italy disclosed word of that meeting, the result was frenzied speculation in Europe that the C.I.C. might help bail out the Italian government by buying large quantities of its bonds. But the Italian government later quieted the speculation by saying the C.I.C., which mainly buys equities, had been interested in making purchases in the Italian industrial sector.

With \$374 billion as of Dec. 31, the C.I.C. is a relatively small player in China's foreign investments. Most of the money is already invested, and the C.I.C. has not received any recent large infusions of money from China's foreign exchange reserves.

By contrast, a rival agency, the State Administration of Foreign Exchange, oversees China's foreign exchange reserves. And, as its acronym might imply, SAFE invests cautiously — buying bonds, not equities — and tends to go with only extremely high-rated instruments. That would seem to rule out the riskiest of Europe's government bonds.

SAFE is famously risk-averse, possibly because it has been under very close scrutiny by the central government since a series of scandals a decade ago.