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## The ASEAN-China Free Trade Area: Issues and Prospects

*Natividad Y. Bernardino*  
*International Gender & Trade Network (IGTN)*

Bilateral and regional trade and investment agreements are not a new phenomenon and have existed parallel but complementary to multilateral trade agreements. But following the collapse of WTO ministerial meetings in Seattle and Cancun, there is a renewed push for bilateral and regional free trade agreements. Most noticeable are those initiated by developed countries like the US which lately has forged bilateral free trade deals with Chile, Singapore and Thailand, that of Japan with Singapore and of course the expansion of EU into the former socialist countries of Eastern Europe.

Another strand of free trade agreement is also happening, i.e. between and among developing countries, such as the ASEAN regional FTAs with the more advanced developing economies of China, India, and South Korea. Among these, it is the framework agreement for an ASEAN-China Free Trade Area that has been inked recently and is hoped to be fully operational by 2010 for the original ASEAN 6 (Singapore, Thailand, Malaysia, Indonesia, Brunei, and Philippines) and 2015 for the newer ASEAN members (Laos, Cambodia, Myanmar, and Vietnam).

For not being the typical FTA initiated and led by developed economies, the ASEAN-China FTA has interestingly elicited varied predictions, ranging from those of nostalgic neo-liberals dreaming of reincarnating the Asian growth miracle, to those of idealistic activists hoping it to be a model for regionalism or alternative forms of South-South trade among developing countries. However, since it has barely gotten off the ground there is little basis to assess its potentials and limitations insofar as alternative trading systems are concerned. Nonetheless, this paper would attempt to capture the present global economic and political context where China and the ASEAN member countries are now situated in order to give us a glimpse of the prospects of such an FTA in the current global power balance. It must be noted that China, along with India, Brazil and other big developing economies, played a leading role in Cancun to "champion" the concerns of developing countries vis-à-vis the US and EU on agricultural subsidies, investment, services and non-agricultural market access which were some of the contentious issues that led to the failed talks.

The first stage of the FTA's implementation involves agriculture, which is also the specific research interest of APNFS. But owing to a lack of basis still to assess its impact, this paper would simply try to identify issues based on the current conditions of the agricultural sector in ASEAN countries and China and suggest areas for further study in the future.

### WORKSHOP PAPERS:

#### Part 1: Regional & Bilateral Trade Agreements: Issues & Challenges

- *Globalization, WTO & Bilateral Trade Agreements* (pdf/ppt) by Dr. Parthapratim Pal /1
- *From Green Revolution to Gene Revolution* (pdf) by Dr. Rene Ofreneo /2
- *Regionalism & South-South Cooperation* (pdf) by Gigi Francisco /3
- *Philippines Under AFTA* (pdf) by Dr. Rene Ofreneo/4
- *SAFTA & LDCs* (pdf) by Raj Kumar K.C. /5
- *ASEAN-China Free Trade Area: Issues & Prospects* (pdf) by Natividad Bernardino /6
- *Thai-US FTA* (pdf) by Auiaporn Suthonthanyakorn /7
- *Thai-China FTA, For Whose Benefit?* (pdf) by Kingkorn Narintarakul /8
- *Indonesia & Bilateral Trade Agreements* (pdf/ppt) by Alex Chandra /9

#### Part 2: Looking at Agriculture Subsidies: North-South Advocacy for Food Sovereignty

- *Agriculture Subsidies and Dumping: Perspective from the South* by Francisco Pascual / 10
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Part 1 discusses the content of the ASEAN-China Framework Agreement on Comprehensive Economic Cooperation. Part 2 explores the global economic and political context of such agreement. Part 3 tackles the agricultural sector and situation of small farmers in the region and China. Finally, Part 4 summarizes the issues and potential implications of the ASEAN-China FTA while at the same time identifying areas for further study in the future.

## THE ASEAN-CHINA FREE TRADE AREA

The Framework Agreement on ASEAN-China Comprehensive Economic Cooperation was signed on November 4, 2002 in Phnom Penh, Cambodia by the 10 member-countries of the Association of South East Asian Nations and China. The formal agreement was based on a decision made by both parties a year earlier during the Annual ASEAN Summit held in Bandar Seri Bagawan, Brunei.

The framework agreement sets the elements and basis for negotiations towards the realization of an ASEAN-China Free Trade Area by 2010 for the 6 original ASEAN members (Indonesia, Malaysia, Thailand, Singapore, Philippines, Brunei) and by 2015 for the 4 new ASEAN members (Laos, Vietnam, Cambodia, Myanmar). Tariff reduction and elimination on trade of goods takes effect July 1, 2003 based on applied MFN tariff rates at said cut-off date.

The free trade agreement covers trade in goods, services and investment with a provision on other areas of cooperation such as trade facilitation, technology transfer, human resources development, telecommunications, transport, tourism and sub-regional development projects. These sub-regional development projects include the ASEAN Mekong River Basin Development Cooperation that shall build the Singapore-Kunming Rail Link and the Bangkok-Kunming Highway project.

For trade in goods, the agreement allows for tariff reduction and elimination on two categories of products called normal and sensitive tracks. Aside from those covered by the Early Harvest Program, the normal track products should have reduced or eliminated tariffs mutually agreed by parties over a period from January 1, 2005 to 2010 for ASEAN 6 and until 2015 for ASEAN 4. Sensitive track products are those submitted by any party with end tariff ceilings and end dates different from the normal schedule but have to be also mutually agreed by parties.

Table 1. Early Harvest Program Modality of Tariff Reduction for ASEAN6.

PRODUCT CATEGORY	Not later than 01 Jan. 2004	Not later than 01 Jan. 2005	Not later than 01 Jan. 2006
With applied MFN tariff rates Higher than 15%	10%	5%	0%
With applied MFN tariff rates Between 5% and 15% (inclusive)	5%	0%	0%
With applied MFN tariff rates Lower than 5%	0%	0%	0%

Source: Philippine Tariff Commission, 2001

### Early Harvest Program

A zero tariff regime is envisioned for trade in goods between China and ASEAN by 2010 for the more advanced ASEAN members and a later timetable of 2015 for the less advanced members. However, a distinct feature of the agreement contained in Article 6 and 4 annexes of the document, referred to as the Early Harvest Program, calls for the implementation of tariff reduction and elimination on certain agricultural goods ahead of schedule supposedly for the parties to enjoy the early benefits of the free trade area.

These products include 562 items at 8/9 digit level in the following Chapters 1-8 in the Harmonized System (HS) of tariffs.

Tariff reduction based on existing MFN rates should have started on July 1, 2003 and reduced to zero in January 2006 for the 6 ASEAN members and until 2010 for the new members. The modality and timeframe of tariff reduction for China and the ASEAN 6 are seen in Table 1.

The Early Harvest Program also allows for an **Exclusion List** whereby a party can exempt certain products from the program's coverage and a **Request List** for inclusion of certain products not covered by the program but mutually agreed by China and the concerned ASEAN member. Brunei and Singapore whose economies are basically non-agricultural have fully subscribed to the provisions of the Early Harvest Program with no exemptions. Vietnam and Cambodia had submitted their exclusion lists in 2002 prior to the signing of the

Chapter	Description
01	Live Animals
02	Meat and Edible Meat Offal
03	Fish
04	Dairy Produce
05	Other Animal Products
06	Live Trees
07	Edible Vegetables
08	Edible Fruits and Nuts

framework agreement while Laos and Malaysia followed suit before the deadline of March 2003. Indonesia and Thailand had no exclusion lists but had request lists. For Indonesia, the request list already agreed with China included coffee, palm oil, coconut oil, vegetable oil and fats, cocoa powder, soap, vulcanized rubber, glass for cathode-ray tubes and furniture wood. Besides including anthracite and coke of coal in its request list, Thailand had earlier agreed with China in June 2003 to implement a zero tariff on fruits and vegetables effective October 2003.

It is only the Philippines that had not clinched any deal yet with China on the Early Harvest Program and ongoing negotiations between the two countries have already surpassed the deadline of March 2003. However, immediately following the state visit of Philippine President Gloria Arroyo to China in September 2004, Philippine Trade and Industry Secretary Cesar Purisima announced that the Philippines would definitely be joining the Early Harvest Program in January 1, 2005. Around 50% or 208 items of the total 415 tariff lines have so far been offered by the Philippines for inclusion in the program on a reciprocal basis with China. Faced with increasing deficits in agricultural trade with China, the Philippines is hesitant to further reduce tariffs on Chinese vegetables, pork, chicken, rice and corn purportedly to protect its local farmers. On the other hand, it wanted to have microelectronics and motor vehicle parts in its request list for tariff concessions from China. These are the main export products of the Philippines to China, which on the whole generates for the Philippines a trade surplus with China despite its deficit in agricultural trade with the latter.

### Optimistic Forecasts

If successful, the ASEAN-China free trade pact would be the world's largest free trade area with 1.8 billion population, combined GDP of 2 trillion dollars and total trade amount of 1.5 trillion dollars. (Table 2)

According to estimates, the free trade area would contribute a 0.9% GDP growth for ASEAN and 0.3% for China. Moreover, China's export volume to ASEAN is said to increase 55% and ASEAN's to China by 48%. (Jianren, 2004) Chinese Premier Wen Jiabao made a forecast during the 2003 ASEAN Summit in Bali that by 2005 China's trade with ASEAN will have increased to US\$100 billion. (Jakarta Post, September 2003)

In recent years, trade between ASEAN 6 and China has been growing at a rate of 30%-40% annually, making China ASEAN's 5th largest export market. China's share in ASEAN's export market grew from 2.3% in 1996 to 6.9% in 2001. (Table 3) In 2003 alone, ASEAN exports to and imports from China reached US\$47.3 billion and US\$30.9 billion, respectively, representing an increase of 51.7% and 31.2% from the previous year. Despite the global economic downtrend in 2001-2002 that hit the US and EU (Japan has been on a recession for a long while) which are ASEAN's major export markets, trade in 2002 between ASEAN and China increased by 31.8% amounting to US\$54.8 billion.

ASEAN 6 has been enjoying a trade surplus with China reaching as much as US\$16 billion in 2003. (China Daily, Sept. 05, 2004) Malaysia supplies 3.1% of China's total imports, followed by Singapore with 2.4 % share, Thailand with 1.9%, Indonesia with 1.5% and Philippines with 1.1%. (Table 4) On the other hand, China ranks 8th among ASEAN's source of imports with 1.4% share in 2001, sliding from a share of 2.6% in 1996. (Table 5)

The main commodities exported by ASEAN 6 to China include electronic parts, semiconductors, electrical machinery, crude petroleum, vegetable oils, and rubber. (Table 6) Those imported by ASEAN 6 from China include the same commodities except for textile products, zinc, watches and clocks, baby carriages, toys, games and sporting goods. (Table 7)

Table 2. Overview of the ASEAN-China FTA

	China (2003)	ASEAN (2002)	Total
Population (billion)	1.3	0.5	1.8
Country area (million km <sup>2</sup> )	9.6	4.5	14.1
GDP (billion USD)	1417.9	610.0	2027.9
Trade amount (million USD)	851.2	748.5	1599.7
Main Trading Partners	Japan, USA, EU, HongKong, Korea, Taiwan, ASEAN	ASEAN, USA, Japan, EU, China	
Per Capita GDP (USD)	1090	1144	2234

Source: Lu Jianren, 2004

Table 3. ASEAN 6 Ten Major Market of Exports, 1996 and 2001 (in %)

1996		2001	
Country	Share (%)	Country	Share (%)
ASEAN	25.0	ASEAN	16.8
USA	18.4	USA	13.1
EU	14.5	EU	9.9
Japan	13.3	Japan	8.0
Taiwan	3.5	China	6.9
Hong Kong	3.3	Korea	4.0
Korea	2.9	Taiwan	2.4
China	2.3	Australia	2.3
Australia	1.9	Hong Kong	1.6
India	1.2	India	1.6
Top-Ten Countries	86.3	Top-Ten Countries	66.7
Others	13.7	Others	33.3
TOTAL	100.0	TOTAL	100.0

Source: ASEAN Statistical Yearbook 2003

# THE GLOBAL ECONOMIC AND POLITICAL CONTEXT OF THE ASEAN-CHINA FTA

One might ask what could be the driving factors for both China and ASEAN countries in forging the ASEAN-China FTA. Beyond the usual rhetoric written in the preamble of the framework agreement, there seems to be a lot more unstated rationale behind the free trade deal.

## Chinese Stakes in the FTA

There are assertions that for China, the main objective is more geo-political than economic, i.e. to counter American containment strategy against China and protect its trade routes in Southeast Asia. (Chandra, 2004) Another thesis asserts that China, now being an industrial economy and net agricultural importer, wants to make ASEAN its backyard garden and source of raw materials. (Ofreneo, 2004) It is believed to be the rationale behind China's push for the Early Harvest Program.

One could also surmise that China could afford a trade-off where on the one hand it is incurring manageable trade deficits with ASEAN while on the other, enjoying huge trade surpluses with the US and EU, amounting in 2002 to US\$42.8 billion and US\$10 billion, respectively. Trade under the Early Harvest Program is also projected to favor ASEAN over China 60% to 40%. Table 8 shows China's trade surpluses and deficits with specific countries.

China's accession to the WTO in November 2001 and continued pressure by the US are seen as another factor behind China's drive to forge alliance with other developing countries. This was evident before and during Cancun where China prominently aligned itself with other major developing country members of the WTO. It has also been actively seeking similar alliances with its East Asian neighbors, specifically ASEAN, Japan and Korea through the ASEAN Plus Three Initiative (China, Japan, Korea). It was a proposal hatched in 2000 and deemed to pave the way for the creation of an East Asia FTA and the East Asia Investment Area.

Membership in the WTO meant that China would now have Most Favored Nation (MFN) status, theoretically enjoying, just like any member, the same market access for its exports that have grown more competitive in the world market. But since China is considered a non-market economy in the WTO framework, the requirements for its accession are greater than those demanded from any other developing country member. China's accession to the WTO followed 15 years of intense negotiations primarily with the US until the US-China Bilateral WTO Agreement was forged in late 1999. Under the terms of the agreement, US companies will secure market access to whole areas of the Chinese economy especially in key sectors such as agriculture, industrial goods, automobiles, telecommunications, internet services, banking and finance. For instance, China has agreed to lower its domestic support to farmers at less than 8.5% of the total value of production, which is lower than the ceiling applied to developing countries. Anti-dumping margins and duties are also higher, as well as the applied in-quota tariffs on imports ranging from one per cent applied to rice, wheat, and cotton to 15 per cent for sugar. (Watkins, 2003)

A year after its accession, average tariff rate in China dropped to 11% from 15.3% in 2001, with zero tariffs on some information and technology imports. (China's WTO Updates, Xinhua News Agency, April 10, 2003)

The US and other big players in the WTO continue to pressure China into opening up its financial services, banking and capital markets. Most recently, an American investment giant, Newbridge Capital, has taken control of the state-owned Chinese bank, Shenzhen Development Bank. Newbridge Capital is known to have also been active in taking over Korean banks immedi-

Table 4. Changes in Importance of Top Suppliers to the China Market, 1995, 2000 and 2002 (in %)

	1995	2000	2002
Japan	22.0	18.4	18.1
European Union	16.1	13.7	13.1
Taiwan	11.2	11.3	12.9
Korea	7.8	10.3	9.7
USA	12.2	9.9	9.2
Hong Kong	6.5	4.2	3.7
Malaysia	1.6	2.4	3.1
Russia	2.9	2.6	2.8
Singapore	2.6	2.2	2.4
Australia	2.0	2.2	2.0
Thailand	1.2	1.9	1.9
Indonesia	1.6	2.0	1.5
Canada	2.0	1.7	1.2
Saudi Arabia	0.4	0.9	1.2
Philippines	0.2	0.7	1.1

Source: Trade Compliance Center, International Trade Administration, US Department of Commerce, 2003

Table 5. ASEAN 6 Ten Major Market Supplier of Imports, 1996 and 2001 (in %)

1996		2001	
Country	Share (%)	Country	Share (%)
Japan	20.9	Japan	17.8
ASEAN	18.3	USA	10.8
EU	16.4	ASEAN	8.4
USA	15.1	EU	5.8
Korea	3.8	Taiwan	2.6
Taiwan	3.6	Korea	2.3
China	2.6	Australia	1.7
Australia	2.5	China	1.4
Hong Kong	1.5	Hong Kong	1.1
Switzerland	1.4	Canada	0.5
Top-Ten Countries	86.1	Top-Ten Countries	52.4
Others	13.9	Others	47.6
TOTAL	100.0	TOTAL	100.0

Source: ASEAN Statistical Yearbook 2003

ately after the Asian crisis in 1997. (Xinhua News Agency, June 07, 2004)

The US and EU have consistently targeted Chinese top exports, e.g. garments, textiles and electronics, in their anti-dumping crusade against China, which now account for 1/5 of all anti-dumping actions in the WTO. These products represent 75% of total Chinese exports and imposing punitive anti-dumping duties reaching as much as over 100% in the US and 40% in EU, could severely hurt Chinese producers. (Watkins, 2003: ) The US in particular wants to correct its huge trade deficits with China and has since unilaterally imposed higher tariffs on Chinese products such as shrimps, furniture, plastics, ironing boards, tetrahydroforfurfyl alcohol, etc. on grounds of dumping and safeguard measures. (China Daily, July 17, 2004)

Agriculture is the only area where the US is enjoying a trade surplus with China. Thanks to the huge agricultural subsidies of the US. It is something that the US wishes to maximize to the hilt by forcing China to further open up its market to such US agricultural exports as corn, wheat and cotton. (Watkins, 2003:) Watkins further argued that:

*Agriculture is an example of the type of issue in which China has much to gain from co-operation with other developing countries. In bilateral negotiations with the US, Chinese policy makers will come under serious pressure to trade-off concessions in agriculture for gains in other areas, such as anti-dumping. However, aligned with Brazil, India, South Africa, and others, China can use the mechanisms of multilateralism and the WTO as a lever for demanding reforms in the US and the EU, and for retaining the right to protect agriculture in the interests of food security. The fact that the alliances emerging before and during Cancun span the traditional divide between Cairns Group exporters (such as Brazil and Thailand), importers (sub-Saharan Africa), and countries motivated by a strong concern to protect local markets from distorted competition (India) is a source of strength.*

One initial advantage that the ASEAN-China FTA has brought for China is that ASEAN has removed its categorization of China as non-market economy, a concession that has supposedly laid the basis for reciprocity in the ASEAN-China FTA.

### ASEAN's Hopes and Post-Crisis Woes

In the FTA with China, ASEAN's wish is to ride on the Chinese economic express train with the objective of re-attracting foreign direct investments (FDI) and hopefully redirect into the region the huge amounts of FDI flowing into China. It also looks at China as its future primary export market, supplying energy raw materials and electronic and

Table 6. Top 20 Export Commodities of ASEAN 6 to China by SITC codes, 2001

SITC	Commodities	Value		Share in ASEAN Export
		(\$M)	%	
759	Parts & accsories for office machn & autmdataproc	3,070	12.1	11.2
776	Transistors, semiconductors devices, valves, etc.	2,952	11.7	5.2
334	Petroleum oils and products	2,725	10.8	20.6
764	Telecommunications eqpmnt, NES & parts	1,067	4.2	6.2
772	Eltrcal switcher relays, curcuits, NES	905	3.6	10.7
778	Eltrcl machinery & apprtus, NES	845	3.3	14.2
333	Crude petroleum	760	3.0	7.1
422	Fixed vegetables fats & oils, other than soft	464	1.8	10.5
231	Natural rubber	445	1.8	13.9
571	Polymers of ethylene, in primary forms	392	1.6	37.0
575	Plastics, NES, in primary forms	362	1.4	29.0
752	Automatic data processing machines	348	1.4	1.0
513	Carboxylic Acids & Anhydrides, Halides and derivatives	296	1.2	24.3
251	Pulp and Waste paper	284	1.1	37.2
716	Rotating Electrc plant & parts thereof, NES	267	1.1	10.7
761	TV receivers	263	1.0	6.0
898	Musical instrumnts, recrds, tapes & snd recordings	261	1.0	12.1
641	Paper and paperboard	258	1.0	12.2
682	Copper	254	1.0	15.1
248	Wood, simply worked	250	1.0	18.7
	ALL COMMODITIES	25,268		

Source: ASEAN Statistical Yearbook 2003

Table 7. Top 20 Import Commodities of ASEAN 6 from China by SITC codes, 2001

SITC	Commodities	Value		Share in ASEAN Export
		(\$M)	%	
759	Parts & accsories for office machn & autm data proc	2,060	10.4	12.7
764	Telecommunications eqpmnt, NES & parts	1,872	9.5	14.5
752	Automatic data processing machines	840	4.2	
772	Eltrcal switcher relays, curcuits, NES	835	4.2	9.3
776	Transistors, semiconductors devices, valves, etc.	566	2.9	1.1
716	Rotating Electrc plant & parts thereof, NES	513	2.6	17.9
771	Electrc power mach & parts	493	2.5	17.1
778	Eltrcl machinery & apprtus, NES	475	2.4	6.9
333	Crude petroleum	459	2.3	2.1
762	Radio broadcast receivers	445	2.2	45.8
334	Petroleum oils and products	414	2.1	3.9
751	Office machines	349	1.8	48.0
773	Equipmnt for distributing electricity	327	1.7	14.7
763	Sound & TV image recorders & reproducers	316	1.6	40.2
523	Metallic salts and peroxy salts	279	1.4	33.6
686	Zinc	238	1.2	46.3
845	Articles of apparel of textile fabrics	228	1.2	33.8
885	Watches and clocks	221	1.1	13.6
894	Baby carriages, toys, games and sporting goods	216	1.1	29.4
653	Woven fabrics of manmade textile materials	212	1.1	16.4
	ALL COMMODITIES	19,792		

Source: ASEAN Statistical Yearbook 2003

machinery parts to Chinese-based plants. The ASEAN-China FTA, is hence viewed by ASEAN as a needed boost to recover from the debilitating effects of the 1997 Asian financial crisis. (Jakarta Post, Sept.03, 2004)

Six years since the 1997 crisis, the amounts of FDI into the region are still way off the pre-crisis level of US\$ 34.09 billion, which in 2000 reached only US\$8.63 billion although it rebounded slightly to US\$ 20.3 billion in 2002. Japanese investments, which are the largest in ASEAN before the crisis amounting to US\$ 4.1 billion in 1995 transformed into an outflow during the crisis and never regained its dominance in the ASEAN market, amounting to a meager US\$ 800 million in 2001. Trade relations with Japan, ASEAN's most important trading partner before the crisis, also deteriorated. In 1995, two-way trade with Japan totaled US\$ 121 billion while in 2001 it had declined to US\$ 99.2 billion or 14.4% of ASEAN trade. (Roberts, 2003)

One significant trend that changed the investment landscape in the region after the crisis is the emergence of the US and EU as the most dominant source of investment flows into ASEAN replacing Japan. The US and EU increased their share of FDI into the region from 9% and 23% in 1995 to 30% and 40% in 2001, respectively. (Table 9) This only shows the extent by which the US and EU took advantage of the Asian crisis and resultant huge losses of Japanese banks in order to take over and control major banking and industrial enterprises in the region, and at bargain prices.

On the other hand, global investment flows shifted dramatically to China in the 90's following the series of market reforms implemented since 1978 by the Chinese government under its so-called "open door policy". The surge, however, in FDI flows to China in the past couple of years is attributed to the devaluation of the yuan in 1994, with foreign investors taking advantage of lower labor costs. As of 2002, there were 220,000 foreign-invested enterprises operating in China with total industrial value-added of US\$ 809 billion and export value of US\$ 170 billion. (Ministry of Commerce, PRC, 2003)

Although some of these enterprises are in high-value added industries such as automobiles, medical, chemical and micro-electronics, the majority of foreign investments are concentrated in labor-intensive export-oriented manufacturing such as toys, garments, shoes and leather. These foreign enterprises employ around 23.5 million workers representing 11% of the total labor force in 2002.

While ASEAN reached a peak level of US\$ 34 billion worth of FDI before the 1997 crisis, China had US\$ 53 billion in 2002, up from US\$ 40.5 billion in 1999. Chinese GDP grows at an annual average of 10% while ASEAN average GDP growth rate dropped from a high of 7.3% in 1996 to a negative 7% in 1998 and has since slowly increased by only an average of 3%-4% in 2001 to 2002. (ASEAN Statistical Yearbook 2003)

Indeed, ASEAN sees China as a major competitor in attracting FDI while at the same time banking on the ASEAN-China FTA as one potential route to speed up its post-crisis recovery.

**Table 8. China's Trade Surpluses and Deficits, 2002**

China's Trade Surpluses		China's Trade Deficits	
Country	Million USD	Country	Million USD
Hong Kong	47,695	Taiwan	-31,493
USA	42,812	Korea	-13,073
European Union	9632	Germany	-5,052
Netherlands	7497	Japan	-5,006
United Kingdom	4,722	Russia	-4,884
Spain	1,679	Malaysia	-4,320
Belgium	855	Thailand	-2,640
Greece	677	Saudi Arabia	-1,764
United Arab Emirates	3,006	Brazil	-1,537
Mexico	1,749	Switzerland	-1,399
Hungary	1,280	Oman	-1,387
Panama	1,270	Australia	-1,263
Bangladesh	1,036	Philippines	-1,174
Vietnam	1,035	Indonesia	-1,074
Poland	947	Argentina	-1,054
Nigeria	926	Angola	-1,026
Turkey	801	Iran	-951
Egypt	761	Sweden	-881
Macau	734	Sudan	-765
Pakistan	685	Kazakhstan	-754
Canada	677		
TOTAL	30,339	TOTAL	30,339

Source: Trade Compliance Center, International Trade Administration, US Department of Commerce, 2003

### ***Intra-TNC Trade in the Region***

Today's logic of economic integration underlying free trade agreements is not simply a matter of enhancing trade relations between and among independent sovereign nations, just like in the old mercantilist era. The emergence and increasing dominance of transnational corporations in the last century has fashioned the contours of the global economy in accordance with their profit-seeking philosophy. Facilitated by advances in information and telecommunications technology, transnational corporations have been able to outsource parts of their production from low-wage locations in developing countries. Hence, global or regional production networks are created wherein the different stages of the production process are located in several countries, either engaged in the production of component parts, sub-assembly of semi-finished products, or distribution and sales. In most

cases, such production system can be very mobile, enabling TNCs to relocate production units from one location to another, wherever it is more profitable, usually where labor is cheaper. Such international production system has significant consequences and implications in trade flows, with a lot of trade taking place within TNCs.

Intra-TNC trade, whether intra-firm or intra-industry, has characterized the nature of trade flows in the region over the past three decades, mainly carried out by Japanese electronics, electrical and automobile firms. Imports come mainly from Japan in the form of capital equipments or machinery, and then parts are shipped from one plant to another within the region before exporting the finished products to the US or EU. This explains why ASEAN countries almost have the same set of export and import commodities, with electronics and electrical parts and devices taking the largest share of exports and imports.

A big percentage of Japanese intra-firm trade takes place with the parent firm rather than among its affiliates on an intra-ASEAN basis, which explains the substantial trade surplus of Japan with ASEAN. In 2000, for example, ASEAN countries imported a total of US\$ 61,404 million worth of goods from Japan against total exports of US\$ 51,982 million. (ASEAN Statistical Yearbook 2003)

Many Japanese TNCs such as those in electronics assembly still run multi-product companies in every country where they served the domestic market since their establishment in the 1960's and 1970's. Toyota Motors, for example, has set up a regional structure of activities, with regional HQs in Singapore, assemblers in Indonesia, Philippines, Malaysia, Vietnam and Thailand, financing and training centers in Cambodia, Thailand and Myanmar, and part suppliers in Malaysia, Philippines and two affiliates in Thailand. In comparison, western TNCs that started operation in ASEAN later than the Japanese, tend to have fewer affiliates in the region focused on single products, as in the case of Siemens, Philips or Bayer from Europe and Caltex, Hewlett-Packard or Motorola from the US. (Giroud, 2003)

Singapore hosts most of the regional headquarters of TNCs operating in Southeast Asia up to the Greater China region owing to its advantages in communications, financial services and highly skilled labor. (Giroud, 2003) It serves as the regional nerve center, attracting the biggest share of FDI flows to the region and demonstrating the highest GDP growth rate in pre-crisis period. However, its role as nerve center and high dependence on foreign capital is also its source of vulnerability, recording negative growth rates in 2001 following the economic recession in the US and EU. The significance of Singapore to transnational capital is demonstrated by the fact that it is the first among ASEAN countries to have inked bilateral free trade agreements with US, Japan, Australia and Chile.

The threat of trade diversion is also an issue in view of the bilateral free trade deals that have already been forged or are being negotiated by some ASEAN members with non-AFTA members like the US and Japan. AFTA or the ASEAN Free Trade Area provides for preferential tariffs enjoyed by ASEAN members since it took effect in 1992. Trade diversion in this case happens when imports by Singapore from the US and Japan are exported to ASEAN countries at zero to five percent tariff rates under the AFTA-Common Effective Preferential Tariffs. With the most recent decision of ASEAN members last September 2004 to revise AFTA's rules of origin (ROO), reducing from 40% to 20% the minimum local content requirement of goods traded within AFTA, the threat of trade diversion could even be bigger.

### ***Market Reforms and Increasing TNC Dominance in China***

The ideological penchant of the Chinese government for market reforms in the last two decades coupled by the aggressiveness of the US and other developed economies to take advantage of such an "open door policy", not to mention China's accession to the WTO, make up the basic recipe for TNC control of the Chinese economy. Predictions are such that in a matter of ten years, China's economy will be radically restructured, inflicting adverse impact on its local entrepreneurs, state-owned industries and most especially its farmers and workers. (Beams, 1999)

According to Chinese economist Han Deqiang, TNCs now control the beverage, brewing, detergent, bicycle, paper, medical, elevator, computer, aviation and machine tool industries. Other industries which are

**Table 9. Share in FDI inflows into ASEAN by Source Country**

Source Countries	1995	2000	2001
ASEAN	15.04	8.39	9.11
Rest of the World	84.96	91.61	90.89
Asian NIEs	8.69	14.49	-3.78
Hong Kong	2.69	7.88	-4.41
South Korea	2.37	0.95	-2.65
Taiwan (ROC)	3.62	5.66	3.28
China	0.65	0.31	1.45
India	-0.08	0.47	0.06
Japan	18.23	-1.59	8.79
EU-15	23.97	30.65	40.45
Switzerland	5.23	19.98	14.96
Canada	8.87	-6.91	1.05
USA	9.06	28.24	30.76
Australia	0.95	-3.46	-4.52
New Zealand	-0.37	0.19	0.12
All Others	9.77	9.24	1.54
Total	100.00	100.00	100.00

Source: ASEAN Statistical Yearbook 2003

under more strict protection by the government, e.g. agriculture, automobile industry, petrochemicals, steel and coal, are also under serious threat from imported products and penetration of TNCs, with some of these domestic firms now serving as production bases of TNCs. (Han Deqiang, 2003)

State-owned enterprises (SOEs) will face stiff competition with TNCs and may be forced to fold up as soon as Chinese banks, which are also up to a tough competition with foreign banks, opt to liquidate the bad debts of SOEs in order to remain competitive. (Beams, 1999)

The terms of China's accession to the WTO are so enormous. Services, investments and intellectual property rights, which are areas that have yet to be negotiated by all the other members in the multilateral system, have already been opened by China from partial to complete market access in a maximum period of 5 years from date of accession.

In a report published by the White House Office of Public Liaison, the US has been so candid outlining the tremendous benefits that US companies would stand to gain from China's opening of its markets. Market access to China ranges from reduction of agricultural tariffs and subsidies to elimination of investment regulations in telecommunications, banking, insurance and securities, including distribution rights, freight services, professional services, travel and tourism and even the entry of Hollywood movies, American sound recordings and videos. (White House Office of Public Liaison, 2001)

As of 2002, the top ten sources of FDI flow to China are seen in Table 10.

As stated earlier, China's main attraction for foreign investors has been its cheap labor and potential of its 1.3 billion population as a huge consumer market. Accounts abound on how Chinese workers are exploited in sweatshops used as production sites of TNCs. A Chinese worker receives as little as 31 US cents an hour and forced to work as much as 12 to 16 hours a day during the peak season of production orders. The average monthly workers' income is US\$ 85 while the minimum wage is around US\$ 40. (China Daily news reports, 2004)

China Labor Watch, a New York-based labor rights watchdog on China, has been reporting on various accounts of labor rights violations in China that are not usually found on official government propaganda. It chronicles labor rights violations of TNCs like Wal-Mart, Mc Donalds, Dell computers, Kodak, and Samsung, whom it said refuse to set up trade unions in their companies despite a Chinese labor law that guarantees a worker's right to join a trade union. It should be mentioned however that trade union membership in China means enlisting only in the state-run and sole trade union in China, the All China Federation of Trade Unions. Hence, Chinese workers, who choose to exercise their rights beyond what is allowed by law, usually end up in jail especially if they violate the extent of labor incentives promised by the Chinese government to foreign investors. (China Labor Watch, 2004)

**Table 10. Top Ten Sources of FDI flows to China, 2002**

Country	Accumulative Amount of FDI in billion USD
Hong Kong	204.875
USA	39.89
Japan	36.34
Taiwan	33.11
Virgin Islands	24.39
Singapore	21.48
S. Korea	15.20
United Kingdom	10.70
Germany	7.99
France	5.54

*Source: Ministry of Commerce of the People's Republic of China*

## **AGRICULTURE IN ASEAN AND CHINA AND THE PLIGHT OF SMALL FARMERS**

There is little evidence yet to assess the impact of the ASEAN-China FTA after only a year that the Early Harvest Program has taken off in July 2003, with Philippines still negotiating its terms of agreement with China. Nevertheless, it is worthwhile to examine the current level of agricultural production and trade of ASEAN members and China including the present situation of small farmers in these countries in order to have a glimpse of the possible implications of the FTA.

### ***Agricultural Production and Trade***

ASEAN can be divided into three sub-groupings in terms of agriculture's share in the country's GDP and employment. The first group would be Singapore and Brunei, which are entirely non-agricultural economies. The second group is those of the middle-income economies of Indonesia, Philippines, Thailand and Malaysia whose farming population consists of about 40%-50% of total labor force but with agriculture's GDP share ranging from 10% to 20%. The third group would be those of the less developed economies of Cambodia, Laos,

Myanmar and Vietnam with farming population of 65%-75% of total population and GDP share of 40%-50%. (ASEAN Statistical Yearbook 2003)

ASEAN's agricultural production output, as well as its agricultural exports, has been declining or stagnant since the late 1990's. Between 1996 and 2001, most of ASEAN's agricultural exports (except fresh bananas) registered negative growth rates, with rice exports declining by 9.7%, coconut oil by 8.8%, crude rubber by 14.5%, sugar by 11%, and shrimps/prawns by 4.2%. (Table 11) Except for Thailand and Vietnam, which registered increases in rice production and exports, the rest of the ASEAN suffered decreasing trade revenues from their main agricultural exports. (ASEAN Statistical Yearbook 2003)

There could be a host of reasons behind the decline in ASEAN's agricultural output and exports in recent years. The El Niño and La Niña phenomena of the late 1990's have been cited as one reason for decreased output. Another is the general slump in world prices of primary exports and finally, the structural effects of fierce competition with cheaper imports following the regime of reduced tariffs under the WTO.

The same is true for China in the past 3 to 4 years. From 1978 to 1999, its annual production grew at a rate of 6.5% annually but in 2002, growth rates dropped to 1% for farm crops, 4% for animal husbandry and poultry and 3% for fisheries and aquatic products. In agricultural trade, China had become a net agricultural importer. In 1998 for instance, its trade deficits in agriculture reached around US\$ 6 billion. (Ministry of Agriculture, PRC, 2003)

Maize is the only agricultural commodity in its list of top commodity exports, generating US\$ 1.1 billion in 2002. However, its primary commodity imports of soybean, wood, non-crude oil, iron and other ores, have been large, outstripping its export earnings from maize. Soybean imports from the US increased 25-fold from 1995 to 2002 reaching US\$ 2.4 billion in 2002. Other agricultural imports from the US include poultry meat, pork, raw bovine hides, flour and animal feeds. (US Department of Commerce, 2003) With lower tariffs and elimination of export subsidies arising from its WTO accession commitments, China's agricultural imports are expected to surge. The US, in particular was very keen about increasing China's market access in agriculture, the only area at present where the US is enjoying trade surplus with China.

As with ASEAN, China's agricultural trade has been somehow balanced, with exports and imports value of US\$ 1.237 billion and US\$ 1.235 billion, respectively in 2001. China is ASEAN's 5th largest agricultural export market, dominated by commodities such as rice, bananas, coconut oil, palm oil and other tropical products. Chinese exports to ASEAN are mainly temperate products and agricultural inputs such as fertilizers and pesticides.

According to Chinese government figures, the one-year old zero tariff agreement on fruits and vegetables between Thailand and China under the Early Harvest program had been to the advantage of Thailand. From January to April 2004, China had imported fruits and vegetables from Thailand amounting to US\$ 96 million, reduced and exempted tariffs worth US\$ 8.5 million. Thailand, on the other hand, imported fruits and vegetables from China amounting to US\$ 13 million. (China Economic Net, July 17, 2004) Alarm has been raised however by some Thai farmer organizations that cheaper temperate fruit and vegetable imports from China have been hurting farmers growing the same produce in Northern Thailand. (Kingkorn Narintarakul, 2004)

The Philippines, which had been skeptical to joining the Early Harvest Program, is also one of China's biggest suppliers of tropical fruits, accounting for 30% of China's total fruit imports in 2003, a 21% increase from 2002 and with values amounting to US\$ 82 million. It is China's biggest supplier of bananas, cornering 89% share in China's total banana imports. Coconut oil is another important Philippine agricultural export to China, which in 2003 reached 60,000 metric tons, a 48% increase from that in 2002. (Embassy of the People's Republic of China in the Philippines, July 2004)

On the whole, however, the Philippines' agricultural trade balance with China has been recording trade deficits amounting to US\$ 11 million in 1996 to a high of US\$ 397 million in 1998 and US\$ 179 million in

Table 11. Annual Rate of Growth of ASEAN Agricultural Exports and Imports, 1993-2001 (%)

Description	Exports		Imports	
	1993-1996	1996-2001	1993-1996	1996-2001
Rice, incl. husk, broken	13.8	-9.7	87.8	-22.6
Banana, fresh	4.2	3.0	-8.6	-39.9
Pineapple Products	5.6	-0.1	-16.6	8.3
Mangoes, pineapple fresh	14.5	-0.4	27.9	-14.8
Oil of palm	11.7	-0.2	2.7	-26.7
Coconut Oil	21.1	-8.8	-11.5	9.7
Cake of Coconuts	8.9	-12.9	40.3	100.5
Soybeans	-5.9	-11.0	21.9	4.0
Sugar and honey	28.7	-11.2	48.5	-11.9
Coffee, green, husk	19.7	-23.1	-6.9	-12.0
Shrimps, prawn, lobster	4.5	-4.2	13.6	0.7
Tobacco	9.0	-19.3	4.2	-13.4
Crude Rubber	23.2	-14.5	16.5	-13.6
Fertilizers, manufactured	15.6	-9.3	11.5	-5.2
Insecticides, fungicide	19.9	-2.7	14.4	-0.7

Source: ASEAN Statistical Yearbook 2003

2003. Rice and other cereals, fruits and vegetables and manufactured fertilizers are the Philippines' top imports from China, with rice imports reaching US\$ 378 million in 1998. (Serrano, 2004)

Aside from declining production and non-competitiveness of its rice and vegetable sector, one reason cited for the Philippines' dilly-dallying towards the Early Harvest Program (EHP) is its already very low tariff rates that would have to be further reduced under the EHP. Another point which Philippine trade officials have been very vocal about is getting more market access in China for its exports of semi-conductors, copper cathodes, and other electrical parts, which currently represent 60% of all its total exports to China.

### ***The Plight of Small Farmers in the Region***

A lot of information has already been documented on the situation of small farmers in the region, including China. One major conclusion arising from previous studies point to the fact that small farmers, given their minimal control of the means of production and distribution chain, are the least to benefit from gains in external trade and the worst to suffer from trade losses. Big landowners and agribusiness firms, whether local or multinational, engaged in trading, integration and processing, are the ones getting the largest share of benefit from any increase in a country's export income. Although they also tend to be hurt by losses in external trade or competition with cheaper imports, especially those engaged in value-added production processes, the small farmer with no access to fallback mechanisms such as credit, insurance, or government bail-out, is still the most to suffer and go bankrupt. Land reform still remains a major issue among farmers in the region. (Bernardino, 2000) ASEAN statistics do not provide data on average farm incomes in the region but in the Philippines for example, average income in rice farming is around US\$ 100 per hectare.

The role of transnational corporations in agriculture has also been fairly documented, spanning the colonial era of corporate plantation farming, the Green Revolution of the 60's and 70's until the most recent "Gene Revolution" of biotechnology and plant genetic engineering. TNCs involved in this wide array of activities are well known, from Dole and Del Monte in bananas and pineapples, to Bayer and Pfizer in agro-chemicals, to Monsanto and Cargill in GMOs and Bt crops. (Ofreneo, 2004)

In China, the series of market reforms implemented in the country's agricultural system radically changed the landscape of the countryside. The household contract responsibility system instituted in 1978 dismantled the people's communes and subdivided the land into small plots contracted out to peasant households. In 1985, the state monopoly of purchasing and marketing agricultural products was dismantled and privatized, allowing the full play of market forces in the country's agriculture. The impact of these market reforms on Chinese farmers had been far-reaching. The average household farm plot is now 0.4 hectares and farm incomes have been declining. In 2003, the National Bureau of Statistics reported an average annual farm income of US\$ 167 while that in purely agricultural areas could be as low as US\$ 80. (China Daily, February 2004) The gap between rural and urban incomes has expanded to about 1:4 in recent years, forcing farmers to move out of farming and migrate to the cities for factory jobs. (Han Deqiang, 2001) The government reported that in 2002, a quarter of the rural labor moved out of agriculture to non-agricultural sectors. (Ministry of Agriculture, PRC, 2003)

The figures depicting poverty and inequality in China are even higher.

*Using the World Bank's '\$1 a day' indicator for absolute poverty (rather than the lower national poverty line), around one-quarter of the rural population – more than 100 million people – are still in extreme poverty... and estimates of rural/urban income ratio may be as high as 1:6... Persistent rural poverty is intimately linked to another challenge currently at the centre of policy debate in China: rising income inequality. Chinese income inequalities are among the fastest growing in the world. The national Gini coefficient increased from 0.24 in 1980 to at least 0.35 in 1999. Some analysts suggest that the real figure today exceeds 0.40. (Watkins, 2003)*

It is interesting to note at this point that most of the middle-income ASEAN countries have Gini coefficient figures in 2000 higher than that of China, with 0.52 in Thailand, 0.45 in the Philippines, 0.44 in Malaysia, and 0.31 in Indonesia. (ASEAN Statistical Yearbook 2003) This stresses the fact that macro-economic growth does not automatically translate into reducing poverty especially if inequality levels are high.

## ISSUES AND PROSPECTS

Based on the discussion above, the following summary presents some issues and questions that may be starting points in studying the potential implications of the ASEAN-China Free Trade Area:

1. The initial take-off of the Early Harvest Program shows complementary trade between the tropical product exports of ASEAN and temperate product exports of China. Rice and corn, which are sensitive commodities to most ASEAN countries and China, are not covered in the Early Harvest Program. Other tariff lines in the EHP like poultry, livestock and vegetables, which maybe sensitive products to some ASEAN countries (as articulated for instance by the Philippines), can be exempted from EHP coverage as allowed by the agreement's provision for an exclusion list and sensitive track products. These are elements in the FTA that make it a potential candidate for an alternative South-South trading system.
2. If China's intention behind the FTA is indeed more geo-political than economic and part of its leverage against the bigger trading blocs of developed countries like the US and EU, the ASEAN-China FTA may once more be seen as a positive development, insofar as consolidating itself as a bloc in the WTO multilateral trading system is concerned. However, it may not always be the case since the US, EU and Japan exercise considerable political and economic influence on many ASEAN countries. The fact that the US chose to forge bilateral FTAs with individual ASEAN countries instead of a regional FTA (which is actually the design of its Enterprise for the ASEAN Initiative) gives it flexibility in optimizing its degree of influence on individual ASEAN countries. In this sense, the ASEAN-China alliance is very fragile.
3. The role of TNCs and national conglomerates in both ASEAN and Chinese agriculture is something that must be examined if we were to assess whether or not the gains from trade are accruing to small farmers. As shown in previous studies, it has not been the case in many developing countries. Structural inequalities persist that prevent small farmers and direct producers from actually participating in trade, much less benefiting from it. South-South alternative trading systems can only be judged ultimately successful if seen from the perspective of small farmers who comprise the majority of direct producers in the region.
4. China's promotion of hybrid corn in the FTA's program for technical cooperation may pose another problematic area. Studies show that the long-term environmental and economic costs of hybrid varieties outweigh the immediate gains from increased productivity. Since Cargill and Monsanto have significant presence in the region for their biotechnology enterprise, it is worthwhile to study whether they have anything to do with China's hybridization program.
5. ASEAN's objective in the FTA of attracting back or redirecting FDI flows from China into the region represents a fixated and misplaced priority. There is evidence to show that net value-added from FDI flows has been minimal given the fact that these are largely investments and trade flows arising from international intra-firm production networks in the region.
6. China's free market reforms have already sown adverse impact on farmers' livelihood and labor rights. Its commitments for accession to the WTO are expected to worsen the problem, bringing to the fore the fundamental contradictions of a free market economy. Some economists assert that it may not take ten years before a similar crisis that hit the emerging markets of East Asia and Latin America occurs in China. These more fundamental issues may overrun whatever potential advantages there may be in the ASEAN-China FTA.



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