

DIRECTORATE-GENERAL FOR EXTERNAL POLICIES  
POLICY DEPARTMENT



# **New trade rules for China?**

## **Opportunities and threats for the EU**

INTA



## *Note from the Policy Department*

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## STUDY

# New trade rules for China? Opportunities and threats for the EU

### ABSTRACT

Paragraph (a) (ii) of Article 15 in China's Accession Protocol to the WTO - which determines the basis on which dumping margins are calculated in Anti-dumping proceedings against China - is about to expire in December 2016. This ad hoc briefing aims to shed light on the economic and political implications that may arise for the EU from different strategies related to the treatment of China after this date, including the possibility of granting it market economy status.

The study provides an economic, legal, as well as political overview of EU Anti-dumping regulation and compares it to that of China's other main trading partners. It demonstrates that Anti-dumping constitutes a significant and frequently used trade defence instrument, although its use is extremely heterogeneous across countries and sectors. Even though market economy status is associated with lower Anti-dumping duties, granting it to China would not render the EU defenceless against dumping.

Beyond first order effects on the magnitudes of AD duties, a unilateral decision will have much wider implications, both for the EU's relations with China as well as with other countries, particularly the USA. These have to be taken into account in the decision making process. This ad hoc briefing can only be a first step towards a full understanding of the impacts of granting MES to China on EU trade policy and European welfare. The briefing illustrates that more research is required.

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## Executive Summary

Paragraph (a) (ii) of Article 15 in China's Accession Protocol to the WTO - which determines the basis on which dumping margins are calculated in Anti-dumping (AD) proceedings against China - is about to expire in December 2016. The purpose of this Ad hoc briefing is to shed light on possible economic implications that may arise for the EU from different strategies related to the treatment of China in AD cases after December 2016, particularly the possibility of granting China market economy status (MES). The analysis is carried out from a legal, economic and political perspective.

In its AD procedure the EU follows the WTO's guidelines. It is in line with China's other main trading partners, although criteria for MES differ across countries. Out of the 32 WTO members having initiated AD proceedings against China, 14 have granted it MES. However, officially declaring MES to China does not necessarily change AD treatment, as is illustrated with the examples of Argentina and Brazil.

The legal implications of the expiry of Article 15 paragraph (a) (ii) are highly controversial. Existing views range from maintaining the status quo to granting MES to China automatically in 2016. MES is critical, as it influences the way dumping margins are calculated. If the EU grants China MES, it may expect average dumping duties to fall by 17 - 28 percentage points. According to several studies this expected drop in AD duties will cause a decline in domestic output and employment.

Between 1995 and 2014, the EU has launched 99 AD initiations against China, constituting 28% of overall AD initiations launched by the EU in that period. AD activity actually increased following China's WTO accession in 2001. At the end of 2014, the EU had 51 AD measures in force against China (47% of total), affecting less than 2% of bilateral imports. This puts the EU at third place, behind the USA (93 measures in force, 38% of total) and India (76 measures, 37% of total). The average EU level of (ad valorem) AD duties in force is 44% (USA 142%, India 80%).

Within Europe, companies from Germany, Italy, France and Spain are most often involved in the filing of AD cases. They tend to be concentrated in the steel and chemical industries. Across countries, AD activity primarily takes place in sectors that have a comparative disadvantage vis-à-vis China. It is however not clear if this stems from a genuine cost advantage or dumping activity. Further research is required to shed light on this issue.

Maintaining China's status as a non-market economy would have obvious political repercussions for the EU, such as in the context of the current negotiations on a bilateral investment treaty. Furthermore, China may use the legal fuzziness to initiate strategic litigations within the WTO, thus increasing dispute complexity. On the other hand, unilaterally granting MES to China may affect relations with third countries, such as the USA (e.g. in the context of TTIP negotiations).

The ad hoc briefing stresses the urgent need for a deeper econometric analysis.

## 1 Introduction

A large number of World Trade Organization (WTO) members still categorize The People's Republic of China as a **non-market economy** (NME), among them the European Union (EU) and the USA. The legal basis for China's current NME status originates from its Protocol of Accession to the WTO from December 2001<sup>1</sup>. Article 15 of the Protocol allows WTO members to define, based on national law, whether China is considered a market economy.<sup>2</sup> China is generally still considered a country in transition from a centralized economic system to a market economy. However, the policy discussion whether China should be granted MES is important in trade defence measures permitted within the WTO. It is crucial for the purpose of price comparability and calculation of Anti-dumping (AD) margins. Paragraph 15(a) of China's Accession Protocol permits member countries to disregard domestic Chinese prices or costs in AD cases and instead base the identification of appropriate dumping margins on external benchmarks (third countries), if Chinese exporters cannot clearly illustrate that market economy conditions prevail in the respective domestic industry.

The comparison of Chinese export prices with third party prices or costs, rather than with Chinese prices, tends to result in higher dumping margins. Given that in the past decade around one-third of all newly initiated AD cases within the WTO have targeted Chinese imports, the economic and political importance of China's NME status for both WTO members and China is comprehensible.

Interestingly, paragraph (d) of Article 15 in China's Accession Protocol defines an expiration clause stating that the provision of subparagraph 15(a)(ii) which permits the use of alternative methodologies based on external benchmarks, shall expire 15 years after China's WTO accession. How the wording of this paragraph should be interpreted is widely varying depending on which stakeholders are consulted. Government representatives from China argue that the Accession Protocol requires all WTO members to grant China market economy status (MES) after 11 December 2016 (automatic grant) and implicitly in new AD cases against China third party reference prices/costs are supposed to be no longer an option. On the other hand lawyers representing US and EU industries interpret the law differently, stating that the Protocol does not confine WTO members to compare Chinese export prices with Chinese domestic prices or costs in AD cases, even if paragraph 15(a)(ii) drops out.

In light of the expiration date in China's Accession Protocol, the EU and other WTO members may require adjustments in their AD regulation which come into force after December 2016.

The purpose of this Ad hoc briefing is to shed light on possible economic implications that may arise for the EU from different strategies related to the treatment of China in AD cases after December 2016. The study analyzes China's MES from three perspectives: economic, legal and political, with special emphasis on economics. Starting with a general overview, the study briefly explains the relevance of the AD instrument within a broader WTO context, as any future amendment in related EU law will most likely affect not only AD related issues but also further areas of economic and political cooperation between China and the EU. Thereafter, a short overview of the MES issue is provided, cumulating in a short presentation of different legal interpretations of Paragraph 15. The study does not aim to assess which legal

<sup>1</sup> Section 2.4 gives a short overview of the relevant Paragraphs in China's Accession Protocol.

<sup>2</sup> The EU lists China and several other countries as NME in its Council Regulation (EC) No 1225/2009.



interpretation of China's accession Protocol is formally correct. The focus of the analysis rather lies on possible economic consequences which can arise from different EU law amendments with respect to China's treatment in AD cases.

The third part of the study provides a comparative analysis, presenting different economic statistics related to AD cases with China. The fourth part of the study intends to illustrate how the EU's treatment of China may influence further economic and political areas including a discussion of how an internationally coordinated or uncoordinated EU approach may influence the European-Chinese relations. The study concludes with policy recommendations.

## 2 Background

### 2.1 Important WTO principles: Reciprocity – Commitment – Flexibility

The ongoing process of global trade liberalization has been based on rules initially defined in the General Agreement on Tariffs and Trade (GATT) and currently organized and refined within the World Trade Organization (WTO). In order to support and maintain a sustainable international trade liberalization process, WTO rules aim at two important principles: a) **WTO member** countries commit to **liberalize international trade reciprocally** and b) binding WTO rules allow member countries to **credibly commit** to national policy reforms, thus fostering a competitive environment.

Accordingly, it is possible to argue that China has been motivated to join the WTO in 2001 with the following expectations: China agreed to undertake substantial import liberalization in exchange for greater certainty with respect to market access for its exports. At the same time China's economic reform program would gain international credibility from trading partners' threat and actual use of WTO dispute settlement procedures to ensure that China sticks to its liberalization commitments (Bown, 2010).

More generally, **WTO** rules are balancing interests of exporting and importing countries on the one hand by supporting **reciprocal trade liberalization** under economically fair conditions and on the other hand by motivating governments to reform national laws compatibly with WTO rules. However, given the large heterogeneity in member countries' economic and institutional development, the ability of these countries to cushion externally or internally driven shocks varies substantially and may **temporarily** cause governments to **deviate from earlier commitments**.

WTO rules have been equipped with a certain degree of **flexibility** in the form of contingent measures, allowing member states to suspend commitments in case of emerging **market failures**, such as **negative external effects** or **unfair competition from other countries**.<sup>3</sup> Among these temporary measures AD regulation takes an important role.

Many countries rely on AD regulation to counteract dumping. Hence, AD regulation may be seen as a form of ex ante **flexibility** required in trade agreements so that countries can make deeper **market access commitments**. AD measures can act like a '**safety valve**' to reduce

<sup>3</sup> Besides AD regulation, WTO rules include further contingency measures such as safeguard measures, countervailing duties and other instruments. For a detailed discussion consult the World Trade report 2009 (WTO, 2009).

protectionist pressure which might otherwise threaten a government's program of trade reform (WTO, 2009).

## 2.2 Overview: EU Anti-dumping procedure

Article VI Paragraph 1 of the GATT 1994 (GATT, 1947; WTO, 1994) defines dumping as selling a product at a price below its '**normal value**'. This means that it:

- '(a) is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country, or,
- (b) in the absence of such domestic prices, is less than either
  - (i) the highest comparable price for the like product for export to any third country in the ordinary course of trade, or
  - (ii) the cost of production of the product in the country of origin plus a reasonable addition for selling cost and profit.'

In case dumping is detected, the importing country is allowed to set an AD duty which may not exceed the difference between the normal price and the dumped price. The EU follows these guidelines (European Commission, 2015c), using AD duties to prevent European companies from injury that may arise from such uncompetitive behaviour of non-European exporters<sup>4</sup>.

Dumping by the exporting producers is thus a necessary, but not a sufficient condition for the European Commission to initiate an AD investigation. In addition, dumping has to cause material injury to EU producers, meaning that they lose market share, make losses and/or have to lay off employees. Finally, AD measures should not be against the broader 'Union interest'. This means that potential negative impacts of AD duties on EU consumers and industrial users – such as higher prices of consumer- and intermediate goods - and other relevant parties have to be taken into account and may not outweigh the benefits to the protected domestic companies ('union interest assessment', European Commission, 2015a, 2015b; European Union, 2009).

The procedural rules for an AD investigation are provided in Articles 5 to 12 of Council Regulation 1225/2009 and can be summarised as follows (European Commission, 2015b, 2015c; European Union, 2009). If a community producer has sufficient evidence to show that the aforementioned criteria are met, he or she may file a complaint to the European Commission, which then assesses the evidence and decides if a case should be initiated. The Commission may also do so on its own initiative. Once a case is initiated, all relevant parties are informed and invited to participate via a note in the European Unions' official journal. Upon investigation the Commission may decide whether to impose provisional measures within nine months after the initiation. The results are published and all relevant parties are given time to respond, before definitive measures are imposed. In case a measure is decided, the exporter concerned may typically agree to respect certain minimum prices, in which case generally no duties are imposed. The total duration of investigation may not exceed 15

<sup>4</sup> Other trade defence instruments include Anti-subsidy duties, global safeguards and China specific transition safeguards (European Commission, 2015b).

months. Once an AD measure is imposed, it typically remains in force for five years, subject to review. The procedure is illustrated in figure A1 in the Appendix.

Duties may be ad valorem or specific. When imposing Ant-Dumping duties, the EU follows the WTO's (WTO, 1994) recommendation and applies the 'lesser duty' rule (European Union, 2009). This means that the **dumping margin** (normal value - import price) is compared to the **injury margin** (EU producer's price – import price). As the EU's goal is not explicitly to harm the exporter but to protect domestic producers from unfair behaviour, the AD duty imposed is based on the lower of the two margins.

## 2.3 Market Economy Status in EU Anti-dumping proceedings

The EU treats all WTO member states that are market economies in the way defined above. However, the GATT 1994 always refers to the prices 'in the ordinary course of trade' for determining a good's 'normal value'. Ad Article VI Paragraph 1.2 of the GATT 1994 recognizes that determining price comparability in the way proposed above may not always be feasible. In particular, in cases of '**complete or substantially complete monopoly** of [a country's] trade [...] where **all prices are fixed by the State**' importing countries may find that using domestic prices may not be appropriate.

Proving the existence of 'complete monopoly' is however difficult in practice (Detlof & Fridh, 2006). The EU and other WTO member states hence rely on their own methodologies, using a softer criterion of market economy status. While the EU does not provide a clear definition of a market economy as such, Article 2 Paragraph 7 (c) of Council Regulation 1225/2009 (European Union, 2009) does provide the following five market economy conditions:

1. 'decisions of firms regarding prices, costs and inputs, including for instance raw materials, cost of technology and labour, output, sales and investment, are made in response to market signals reflecting supply and demand, and without significant state interference in this regard, and costs of major inputs substantially reflect market values,
2. firms have one clear set of basic accounting records which are independently audited in line with international accounting standards and are applied for all purposes,
3. the production costs and financial situation of firms are not subject to significant distortions carried over from the former non- market economy system, in particular in relation to depreciation of assets, other write-offs, barter trade and payment via compensation of debts,
4. the firms concerned are subject to bankruptcy and property laws which guarantee legal certainty and stability for the operation of firms, and
5. exchange rate conversions are carried out at the market rate.'

In 2006 the EU had classified 15 countries as NMEs. 9 of these countries are WTO members in 2015<sup>5</sup> (table 1). However, out of these 15 countries, only seven have so far been targeted by EU AD duties (Bown, 2010; WTO, 2015c, 2015d). For the remaining eight, market economy status is thus currently not overly relevant in this context.

**Table 1: Countries classified as non-market economies by the EU**

Country	Year of WTO Accession	Number of EU AD initiations
Albania	2000	None
Armenia	2003	1
Azerbaijan	observer	None
Belarus	observer	6
China	2001	99
Georgia	2000	None
Kazakhstan	observer	4
Kyrgyzstan	1998	None
Moldova	2001	1
Mongolia	1997	None
North Korea	-	None
Tajikistan	2013	None
Turkmenistan	-	None
Uzbekistan	observer	1
Vietnam	2007	6

Source: Ifo Institute, data from Detlof & Fridh (2006), WTO (2015a, 2015b)

The EU relies on its own methodology when dealing with such non-market economies. It is described in Article 2 Paragraph 7 of Council Regulation (EC) No 1225/2009 (European Union, 2009):

‘ (a) In the case of imports from non-market economy countries, normal value shall be determined on the basis of **the price or constructed value in a market economy third country**, or the price from such a third country to other countries, including the Community, or where those are not possible, on any other reasonable basis, including the price actually paid or payable in the Community for the like product, duly adjusted if necessary to include a reasonable profit margin.

<sup>5</sup> WTO status is relevant since individual companies within a non-market economy which is a WTO member (and Kazakhstan) may receive market economy treatment (MET) if they are able to show that market conditions prevail according to the EU's own definition of a market economy (Article 2.7, European Union, 2009).

An appropriate market economy third country shall be selected in a not unreasonable manner, due account being taken of any reliable information made available at the time of selection.'

**Market economy status thus determines the calculation method of the dumping margin.**

In the case of market economies, export prices are compared to the exporter's domestic costs and prices or his export prices to third countries. In the case of non-market economies, export prices are compared to costs and prices of producers in a market economy third – 'analogue' – country.

In addition to MES and NMES of an entire country, Articles 2.7 and 9.5 of Council Regulation 1225/2009 also specify the following two intermediate cases. First, if a producer within a non-market economy can show that market economy conditions prevail for her with regard to the manufacture and sale of the good in question, it may receive the same treatment as if it was situated in a market economy (**market economy treatment, MET**, European Union, 2009). If the exporter is unable to prove the existence of market economy conditions, normal value for means of price comparison is determined using products from third – 'analogue' – country producers (non-market economy Treatment, NMET<sup>6</sup>) as specified in Article 2 Paragraph 7 of Council Regulation (EC) No 1225/2009.

Second, companies in NMEs that do not qualify for MET may receive **individual treatment (IT)** if they fulfil the following criteria set out in Article 9.5 of Council Regulation 1225/2009, which mainly focus on exports (European Union, 2009):

1. 'in the case of wholly or partly foreign owned firms or joint ventures, exporters are free to repatriate capital and profits;
2. export prices and quantities, and conditions and terms of sale are freely determined
3. the majority of the shares belong to private persons. State officials appearing on the board of Directors or holding key management positions shall either be in minority or it must be demonstrated that the company is nonetheless sufficiently independent from state interference
4. exchange rate conversions are carried out at the market rate
5. State interference is not such as to permit circumvention of measures if individual exporters are given different rates of duty.'

In the case of individual treatment normal value is still established using an analogue country; however the export price is determined using the exporting producer's own data rather than that of the entire exporting country. Hence the producer is subject to an individual duty.

Finally, council regulation No 1972/2002 (European Union, 2002) provides for the possibility to give special treatment to certain producers within market economy countries by means of making adjustments to normal values (Detlof & Fridh, 2006; Puccio, 2015). This concept was

<sup>6</sup> The terms 'market economy treatment MET', 'non-market economy treatment NMET' and 'individual treatment IT' are not officially used in Council Regulation 1225/2009. However, for ease of comparison and presentation purposes, this report follows the literature (Detlof & Fridh, 2006; Scott & Jiang, 2015; Zang, 2012) when naming the respective situations referred to in Council Regulation 1225/2009.

introduced when the EU granted Russia MES in 2002 and refers to ‘a particular market situation, in which sales of the like product do not permit a proper comparison’. This may occur if ‘because of the existence of barter-trade and other non-commercial processing arrangements or other market impediments’ prices are ‘out of line with world market prices’.

In such a case – ‘and if records do not reasonably reflect the costs associated with the production and sale of the product’ (European Union, 2002) – normal value may be constructed using production costs from other producers or exporters in the same country. If such data is not available or cannot be used, information from other “representative markets” shall also be appropriate. While the term ‘analogue country’ is not used explicitly, such a treatment from a non-legal perspective in effect seems similar to non-market economy treatment<sup>78</sup>. The box and table 2 below sum up the five different treatments companies may receive in the context of EU AD legislation.

**Summary: Possible company treatments in EU Anti-dumping legislation:**

**(Council Regulations 1225/2009 and 1972/2002)**

1. The company is situated in a market economy. In this case there are two possibilities:
  - a. The company receives market economy treatment (the default option). The dumping margin is calculated using the difference between the exporters’ EU import price and his or her domestic market price (or production costs).
  - b. Domestic prices do not reflect world prices so that adjustments to the normal value (reference price) are made. The dumping margin is calculated using the difference between the exporter’s EU import price and a constructed normal value of the product using costs from other domestic producers or information from ‘representative markets’.
2. The company is situated in a non-market economy: In this case there are three different possibilities:
  - a. No special treatment: The dumping margin is calculated using the difference between the exporter’s country’s average export prices (of the product concerned) and a constructed normal value of the product using domestic prices or costs in a third/analogue country.
  - b. Market economy treatment: The dumping margin is calculated as if the exporter was situated in a market economy in 1a.
  - c. Individual Treatment: The dumping margin is calculated using the difference between the exporter’s EU import price and a constructed normal value of the product using domestic prices or costs in a third/analogue country.

<sup>7</sup> In the context of China, Australian officials have also stated that adjustments to normal value calculations may be made even for market economies (Stoler, 2004).

<sup>8</sup> Russia has recently challenged these normal value adjustments (WTO, 2015a). Furthermore it is not clear if such provision can easily be applied to China.

**Table 2: Overview of EU dumping calculation method**

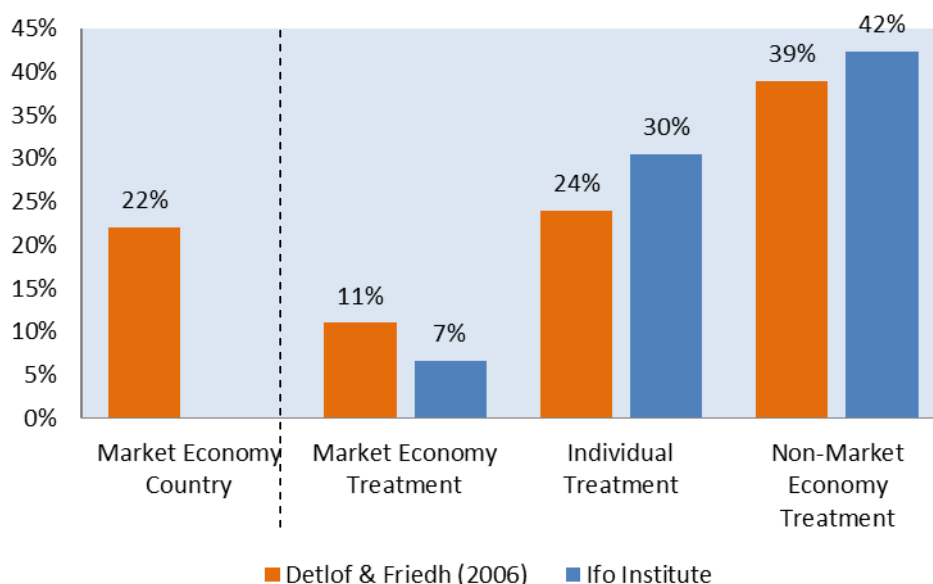
	<b>Country Category</b>	<b>Company Treatment</b>	<b>Constructed normal value (reference price)</b>	<b>Export price (used to calculate dumping margin)</b>
<b>1. a)</b>	Market economy	Market economy treatment <sup>9</sup>	Domestic prices / costs	Exporter's own price
<b>1. b)</b>	Market economy	Adjusted normal value	Costs of other domestic producers / information from representative markets	Exporter's own price
<b>2. a)</b>	Non-market economy	Non-market economy treatment	Analogue country prices	Average export prices of exporting country
<b>2. b)</b>	Non-market economy	Market-economy treatment	Domestic prices / costs	Exporter's own price
<b>2. c)</b>	Non-market economy	Individual treatment	Analogue country prices	Exporter's own price

Note: The choice of a reference price ('Normal value') used for determining the dumping margin of exporters critically depends on the market economy status of the exporter. For exporters in market economies, domestic prices and costs are used. For exporters in non-market economies, prices in a third (analogue) country are used.

Source: Ifo Institute, data taken from European Union (2002, 2009)

Figure 1 illustrates that the category a company is placed in has visible effects on the AD duty to be expected. When comparing duties by company status, Detlof & Fridh (2006) find an average duty of 39% for NMET companies, 24% for IT companies and 11% for MET companies. This is in line with our findings of a small sample of AD duties in force between 2005 and 2010 against 20 products produced by several Chinese companies. Here the non-weighted average duty for companies receiving MET is 7%, that of those receiving IT is 30%, while that of all others is 42%.

<sup>9</sup> The terms 'market economy treatment MET', 'non-market economy treatment NMET' and 'individual treatment IT' are not officially used in Council Regulation 1225/2009. However, for ease of comparison and presentation purposes, this report follows the literature (Detlof & Fridh, 2006; Scott & Jiang, 2015; Zang, 2012) when naming the respective situations referred to in Council Regulation 1225/2009.

**Figure 1: Average EU Anti-dumping duties by company status**

Source: Ifo Institute, data from Detlof & Fridh (2006)

It has been argued that granting China market economy status would reduce average duties imposed by the EU by 28 percentage points, (from 39% NMET to 11% MET, (Scott & Jiang, 2015)). This is certainly possible. However, MET does not necessarily have to be the cause for the low average AD duties. There could also be a selection effect at work, meaning that only the most competitive companies within a non-market economy apply for MET. Once they have received it, duties are lower simply because they can demonstrate that they have low production costs and thus their low prices reflect a competitive advantage. Companies which cannot demonstrate appropriate figures as they do charge prices below costs (potentially both domestically and abroad) do not apply for or do not receive MET. Consequently the most competitive companies are already in the MET group. Hence, granting MES to China may thus not lead to a sudden drop of AD duties to an average of 11%. Instead the average AD duty of 22% for market economy countries reported in figure 1 may be more accurate, as it incorporates duties against very competitive as well as against less competitive companies. This reasoning is of course purely theoretical and econometric research is required in order to determine the true impact of granting MES to China on AD duties.



## 2.4 The treatment of China in EU Anti-dumping proceedings

With exports of more than EUR 300bn (17.9% of total EU imports) in 2014, China is the biggest exporter to the EU (European Commission, 2015d)<sup>10</sup>. AD duties imposed against China may thus potentially have a strong impact on European trade, although less than 2% of imports from China had been affected by AD duties in 2014 (European Commission, 2014). In Article 15 of the Accession Protocol of the People's Republic of China to the WTO in 2001 (WTO, 2001), explicit criteria for determining price comparability are given:

' (a) In determining price comparability under Article VI of the GATT 1994 and the Anti-dumping Agreement, the importing WTO Member shall use either Chinese prices or costs for the industry under investigation or a methodology that is not based on a strict comparison with domestic prices or costs in China based on the following rules:

- (i) If the producers under investigation can clearly show that market economy conditions prevail in the industry producing the like product with regard to the manufacture, production and sale of that product, the importing WTO Member shall use Chinese prices or costs for the industry under investigation in determining price comparability;
- (ii) The importing WTO Member may use a methodology that is not based on a strict comparison with domestic prices or costs in China if the producers under investigation cannot clearly show that market economy conditions prevail in the industry producing the like product with regard to manufacture, production and sale of that product.

[...]

(d) Once China has established, under the national law of the importing WTO Member, that it is a market economy, the provisions of subparagraph (a) shall be terminated provided that the importing Member's national law contains market economy criteria as of the date of accession. In any event, the provisions of subparagraph (a)(ii) shall expire 15 years after the date of accession. In addition, should China establish, pursuant to the national law of the importing WTO Member, that market economy conditions prevail in a particular industry or sector, the non-market economy provisions of subparagraph (a) shall no longer apply to that industry or sector.'

The status quo is thus that China shall essentially be treated as a non-market economy according to the definition of the importing WTO member. Only if a Chinese producer can prove that industry prices are set by the market, domestic prices or costs are to be used for determination of normal value, in line with Article VI paragraph 1 of GATT 1994. If the producer fails to provide such evidence, the importing WTO member does not have to use **domestic**

<sup>10</sup> More detailed figures on EU China trade are reported in Appendix A4.

**prices** but may use an ‘alternative methodology’, which is specified neither by the GATT 1994 nor by the Accession protocol. Consequently, **the EU follows its own definitions and methodology** as outlined above.

Subparagraph (d) has attracted a lot of debate and controversies which shall be briefly presented here<sup>11</sup>. The second sentence is often – and not only by Chinese officials -interpreted as China being granted effectively MES 15 years after its accession to the WTO, i.e. in December 2016 (Tietje & Nowrot, 2011; Zang, 2012). Some EU and US lawyers are however of a very different opinion, arguing that nothing in the WTO rules automatically grants MES to China in 2016 (Hufbauer & Cimino, 2015; O’Connor, 2011).

According to Tietje & Nowrot (2011), the expiry of paragraph 15(a)(ii) means that members are no longer allowed to ‘use a methodology that is not based on a strict comparison with domestic prices or costs in China’. However, the authors also argue that while paragraph 15(a)(ii) is set to expire, paragraph 15(a)(i) remains, meaning that theoretically China may still be considered a NME after 2016. This is supported by the first and third sentence of paragraph 15(d) which explicitly refer to the entire paragraph 15(a), implying a difference between the expiry of just 15(a)(ii) and the expiry of 15(a) as a whole. Furthermore the first and third sentence imply that it is China that has to prove that it is a market economy by the standard of the importing country (O’Connor, n.d.).

Nevertheless the perception of Tietje & Nowrot (2011) and others is that from 2016 onwards, the Accession Protocol of China to the WTO ceases to provide a legal basis for a default NME treatment of China (holman fenwick willan, 2013; Rao, 2013). Instead, it is argued that the burden of proof shifts to the WTO member imposing the duty. The investigating authority has to provide evidence that the industry in question has non-market economy characteristics rather than the producer having to prove that it acts in a market economy environment. In doing so, the investigator needs to prove that the prerequisites of Ad Article VI Paragraph 1 (2) of the GATT 1994 are fulfilled, which by then will provide the only legal basis for NME treatment according to the above authors. The wording in Ad Article VI Paragraph 1 (2) of the GATT 1994 specifically referring to a ‘complete monopoly’ however constitutes a high threshold that will be hard to prove (Rao, 2013).

On the other hand, it may also be argued that the burden of proof remains with Chinese producers as implied by Article 15(a)(i). Simply ignoring Article 15(a)(i) once 15(a)(ii) expires would render the former inutile, which goes against well-established rules of treaty interpretation (O’Connor, n.d.). This argument has been countered by the fact that a methodology not based on a strict comparison with domestic prices or costs in China may still be applicable according to Ad Article VI Paragraph 1 (2) of the GATT 1994, which remains unaffected (Rao, 2013). Taking account of this GATT provision, it is argued that Article 15(a)(i) would still be applicable: If Chinese producers can show that market economy conditions prevail, then Chinese prices or costs are to be used to determine price comparability. If the investigator can show the existence of a ‘complete or substantially complete monopoly’, alternative methodologies may be used. In fact, O’Connor also argues that that the phrase

<sup>11</sup> The overview presented here is by no means exhaustive. For a more detailed discussion of the legal issues involved, see for example Puccio (2015).

'based on' in paragraph 15(a) in principle allows for other applications than the ones set out in subparagraphs (i) and (ii).

While this study does not intend to assess which legal interpretation of China's Accession Protocol is formally correct, it is still helpful to list different publicly available interpretations. Table 3 gives a non-representative overview of different legal interpretations concerning China's MES. A further discussion of China's MES can be found in Puccio (2015), Zhao & Wang (2009) and Cattaneo & Braga (2009), Ruiz, Somerville, Szamosszegi (2015). It becomes clear that there is no unanimous judicial position on how China should be treated after December 2016.

**Table 3: Different positions on China's MES after December 2016**

Author	Assessment	Source
<b>Christian Tietje Karsten Nowrot</b>	Automatic MES for China after December 2016	Policy Papers on Transnational Economic Law, December, 2011
<b>Bernard O'Connor</b>	No automatic MES for China; Paragraph 15(a) remains effective after December 2016	Global Trade and Customs Journal, Volume 10, 2015.
<b>Robert E. Scott Xiao Jiang</b>	China remains NME after December 2016.	Unilateral Grant of Market Economy Status to China would put millions of EU jobs at risk, Economic Policy Briefing Paper #407, September 2015
<b>K. William Watson</b>	MES for China after December 2016	Will Nonmarket Economy Methodology Go Quietly into the Night?, Policy Analysis, Number 763, CATO Institute

Source: Ifo Institute

## 3 Comparative Analysis

### 3.1 The EU approach compared to other WTO member states – criteria for granting Market Economy Status

As all WTO members are bound by the GATT 1994 as well as by the Accession Protocol of China to the WTO, **the treatment of China in AD proceedings mainly depends on the WTO members' individual criteria for granting market economy status since this is left to the individual member's national law.** Market economy status is thus essential as average Anti-dumping duties significantly differ between MET and NMET companies<sup>12</sup>.

While the WTO – apart from its monopoly rule – as well as most other international organisations do not provide clear definitions of a market economy (Thorstensen, Ramos, Muller, & Bertolaccini, 2013), Unctad defines a market economy as 'A national economy of a country that relies heavily upon market forces to determine levels of production, consumption, investment and savings without government intervention' (Unctad, 2015).

Consequently, a non-market economy is 'A national economy in which the government seeks to determine economic activity largely through a mechanism of central planning, as in the former Soviet Union, in contrast to a market economy which depends heavily upon market forces to allocate productive resources. In a 'non-market' economy, production targets, prices, costs, investment allocations, raw materials, labour, international trade and most other economic aggregates are manipulated within a national economic plan drawn up by a central planning authority; hence, the public sector makes the major decisions affecting demand and supply within the national economy'.

<sup>12</sup> It should be noted that out of the 161 WTO members, only 41 members have initiated Anti-dumping proceedings (EU counted as one member). 32 members have initiated proceedings against China. Consequently, in the context of AD, the decision of whether to grant market economy treatment to a country is only important for this subgroup, which however includes the EU, the USA and India (WTO, 2015c, 2015d).

**Table 4: Comparison of legal criteria for market economy treatment in four countries**

EC	USA	Mexico	Malaysia
(Regulation No. 1225/2009) 30.11.2009	(G/ADP/N/1/USA/1) 10.04.1995	(G/ADP/N/1/MEX/1/Suppl.1) 31.01.2001	(G/ADP/Q1/MYS/6) 11.01.2001
<b>1. Decisions of firms regarding prices, costs and inputs, including for instance raw materials, cost of technology and labour, output, sales and investment, are made in response to market signals reflecting supply and demand, and without significant State interference in this regard, and costs of major inputs substantially reflect market values</b>	The extent of government ownership or control of the means of production	Decisions relating to prices, costs and supply of inputs, including raw material, technology, production, sales and investment, in the sector of industry under investigation, must be taken in response to market signals without any significant State interference	The degree of private investment, in particular whether private companies hold the majority of shares in whether government officials are on the board or in key management positions
<b>Same as above</b>	The extent of government control over the allocation of resources and over the price and output decisions of enterprises	Same as above	Company control over sourcing of raw materials and inputs. Freedom to determine export prices and export quantities.
<b>2. Firms have one clear set of basic accounting records which are independently audited in line with international accounting standards and are applied for all purposes</b>	No similar provisions	The industry under investigation must have only one set of accounting records which it uses for all purposes and which is audited according to generally accepted accounting principles	No similar provisions
<b>3. The production costs and financial situation of firms are not subject to significant distortions carried over from the former non-market economy system, in particular in relation to depreciation of assets, other write-offs, barter trade and payment via compensation of debts</b>	No similar provisions	The production costs and financial situation of the sector or industry under investigation must not be distorted in relation to the depreciation of assets, bad debts, barter trade and debt compensation or other factors considered relevant	No similar provisions
<b>4. The firms concerned are subject to bankruptcy and property laws which guarantee legal certainty and stability for the operation of firms</b>	No similar provisions	No similar provisions	No similar provisions
<b>5. Exchange rate conversions are carried out at market rate</b>	The extent to which the currency of the foreign country is convertible into the currency of other countries	The currency of the foreign country under investigation must be generally convertible in the international currency markets	No similar provisions
<b>No similar provisions</b>	The extent to which wage rates in the foreign country are determined by free bargaining between labour and management	Salaries in the said foreign country must be established through free negotiation between workers and employers	Freedom to hire and fire employees and to determine their salaries
<b>No similar provisions</b>	The extent to which joint ventures or other investments by firms of other foreign countries are permitted in the country	No similar provisions	No similar provisions
<b>No similar provisions</b>	Such other factors as the administering authority considers appropriate	No similar provisions	No similar provisions

Source: Ifo institute, Detlof & Fridh (2006), Secretariat of Foreign Trade Brazil (2001), WTO (2004, 2006, 2008)

**Table 4 (continued): Comparison of legal criteria for market economy treatment in four countries**

EC	Brazil	Argentina	Australia
(Regulation No. 1225/2009) 30.11.2009	(Circular No. 59) 28.11.2001	(G/ADP/N/1/ARG/1/Suppl.9) 22.09.2008	(G/ADP/N/1/AUS/2/Suppl.2) 02.02.2004
<b>1. Decisions of firms regarding prices, costs and inputs, including for instance raw materials, cost of technology and labour, output, sales and investment, are made in response to market signals reflecting supply and demand, and without significant State interference in this regard, and costs of major inputs substantially reflect market values</b>	a) The degree of government control over the companies or over the means of production	a) Decisions of firms regarding prices, cost factors (including, for example, raw materials, cost of technology and labour), output, sales and investment are made in response to market signals reflecting supply and demand, without State interference	The firms make decisions about prices, costs, inputs, sales and investments in response to market signals and without significant interference by a government of the country of export; presence of an enterprise owned by a government of the country of export does not prevent market conditions from prevailing in that market or sector
<b>Same as above</b>	b) the level of state control over the allocation of resources, over prices and over the production decisions by companies	Same as above	Utilities supplied to firms under contracts that reflect commercial terms and prices that are generally available throughout the economy of the country of export; if the land on which the entity's facilities are built is owned by a government of the country of export, the conditions of rent are comparable to those in a market economy;
<b>2. Firms have one clear set of basic accounting records which are independently audited in line with international accounting standards and are applied for all purposes</b>	No similar provisions	b) Firms have one clear set of basic accounting records which are independently audited in line with international accounting standards and are applied for all purposes	The firms keep accounting records in accordance with generally accepted accounting standards in the country of export, which are in line with international accounting standards developed by the International Accounting Standards Board and which are independently audited
<b>3. The production costs and financial situation of firms are not subject to significant distortions carried over from the former non-market economy system, in particular in relation to depreciation of assets, other write-offs, barter trade and payment via compensation of debts</b>	e) The level at which distortions inherited from the centralized economy system persist in relation to, inter alia, assets amortization, other assets deductions, direct swap of assets and payments in the form of debt compensation	c) The production costs and financial situation of firms are not subject to distortions carried over from the former non-market economy system, in particular in relation to the depreciation of assets, other write-offs, barter trade and payment via compensation of debts	The production costs or financial situation are not significantly affected by the influence that a government of the country of export had on the domestic price of goods in the country before the country's economy was an economy in transition
<b>4. The firms concerned are subject to bankruptcy and property laws which guarantee legal certainty and stability for the operation of firms</b>	c) The legislation to be applied in terms of ownership, investment, taxation and bankruptcy	d) The firms concerned are subject to bankruptcy and property laws which guarantee legal certainty and stability for the financing of firms	Bankruptcy and property laws exist in the country and the firms are subject to these laws
<b>5. Exchange rate conversions are carried out at market rate</b>	f) The level of state interference on currency exchange operations	e) Exchange rate conversions are carried out at the market rate	No similar provisions
<b>No similar provisions</b>	d) The degree of freedom in the determination of wages in negotiations between employers and employees	No similar provisions	The firms have the right to hire and dismiss employees and to fix the salaries of employees.
<b>No similar provisions</b>	Same as c)	No similar provisions	No similar provisions
<b>No similar provisions</b>	No similar provisions	[...] the implementing authority may request such other evidence as it deems relevant	No similar provisions

Source: Ifo institute, Detlof & Fridh (2006), Secretariat of Foreign Trade Brazil (2001), WTO (2004, 2006, 2008)

The European Union (European Union, 2009) does not have a definition of a market economy country (Detlof & Fridh, 2006). However, the market economy conditions needed to be fulfilled by a country seem to be the same as those that need to be fulfilled by an individual producer to receive MET (Puccio, 2015). It is summarised again in table 4 above, together with the definitions of the USA (United States International Trade Commission, 2012), Mexico, Malaysia, Brazil (Secretariat of Foreign Trade Brazil, 2001), Argentina (WTO, 2006, 2008) and Australia (WTO, 2004, 2015b)<sup>1314</sup>. As can be seen from the table, the criteria are relatively similar across countries. All of them consider the way prices are formed and see evidence of non-market economy conditions reflected in a non-balanced **interaction of demand and supply**. In addition, they all consider the **degree of state interference** in a company's decisions such as input choice as well as convertibility of the exchange rate (except Malaysia and Australia).

While the EU does not explicitly mention the importance of free bargaining, this may be incorporated in the provision of free input choice (including labour) and the requirement of costs reflecting market values (criterion 1). The EU, Argentina and Australia make explicit provisions on accounting standards, bankruptcy and property law Mexico only accounting standards). The USA is in turn the only countries explicitly mentioning joint ventures. Furthermore, the USA and Argentina give themselves additional discretion when incorporating 'other factors as the administering authority considers appropriate'. Malaysia, Brazil, Argentina and Australia have actually granted China market economy status. Of all 32 WTO members having initiated AD proceedings against China, 14 have granted it market economy status<sup>15</sup>. These are illustrated in table 5 further down. It should be noted however that an official declaration of granting MES to China does not necessarily change a country's practice with regard to AD treatment.<sup>16</sup>

In addition to the general criteria of granting market economy status, there are other differences between the EU and the USA that affect their treatment of Chinese companies in AD proceedings. The EU may grant MET to individual companies, although this has not happened since 2011 (European Parliament, 2015). The USA may grant a form of individual treatment to producers, or declare individual industries to be 'market-oriented' (United States Government Accountability Office, 2006). The latter has however not been granted to date in the case of China. This difference might explain the additional criterion of a clear, independently audited set of accounts as this is necessary when individual companies are investigated. Giving individual economies MET is a more liberal approach and would – together with the observation that average AD duties to MET companies are below those of NMET companies – lead to lower average AD duties imposed against China by the EU

<sup>13</sup> The EU's, Australia's and Argentina's criteria refer to individual producers. EU criteria also seem to be the criteria for determining MES of an entire country (see explanation in text). The US criteria refer to an entire country. Brazil's, Malaysia's and Mexico's criteria are more general.

<sup>14</sup> These are some of China's main trading partners for which information on MES criteria was available. No such comprehensive list could be found for Russia. However, its AD regulation also states that 'data [have to be] consistent with generally accepted principles and accounting rules and reporting in the exporting foreign country and fully reflect the costs associated with the production and selling product.' (WTO, 2012)

<sup>15</sup> These are Argentina, Brazil, Indonesia, Malaysia, New Zealand, Pakistan, Peru, Philippines, South Africa, Thailand and Venezuela (all in 2004) as well as Australia, Jamaica and South Korea (in 2005).

<sup>16</sup> Argentina and Brazil e.g. signed a memorandum in 2004, which can be interpreted as a declaration of intent. It's AD practices against China were not affected by this (Urdinez, 2014)



compared to those imposed by the USA. This is in fact exactly what is observed (see next section).

The EU and the USA also differ substantially in the way they choose an analogue country for the determination of normal values. In the EU, the only requirement in Council regulation 1225/2006 Article 2 paragraph 7 (a) is that the third country 'shall be selected in a not unreasonable manner' (European Union, 2009). In the USA, the analogue country should be a significant producer of the good under consideration, have similar wages / per capita income and should in general be at a similar level as the exporting country under investigation. This difference in rules has resulted in very different analogue countries chosen by the EU and the USA. While the most often chosen third country in the EU is actually the USA, the most frequently chosen third country in the USA is India, which is more similar to China in terms of its development level. Intuitively, given wage levels in the USA, China and India, one would conclude that using India as an analogue country results in lower 'normal values' and hence lower AD duties than when choosing the USA. While this may or may not play a role, it is still true that the EU imposes lower average AD duties on China than the USA, as will be shown in the next section. The main differences are summarised in table 5 below.

**Table 5: Main differences between EU and US Anti-dumping procedure against China**

EU	USA
<b>MET treatment possible for individual producers</b>	IT treatment possible for individual producers (conditions differ from MES criteria <sup>17</sup> ), MET possible for individual industries
<b>Analogue country to be 'selected in a not unreasonable manner' (main Analogue country: USA)</b>	Analogue Country to have similar level of development and wages (main Analogue country: India)
<b>No such provision</b>	Condition of market economy includes such factors as the administering authority considers appropriate
<b>Applies lesser duty rule (injury margin vs dumping margin)</b>	No such provision

Source: Ifo Institute

### 3.2 Anti-dumping initiations around the world

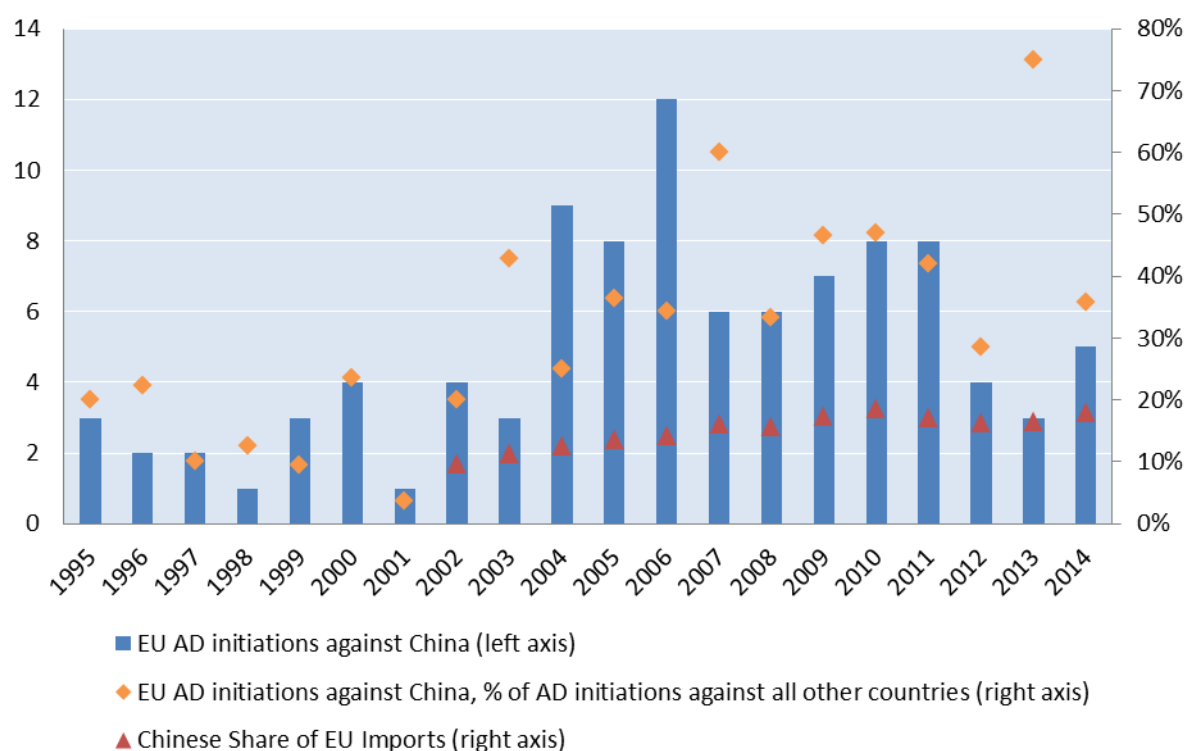
Figure 2 shows the number of European AD Initiations per year for the period 1995 until 2014. Overall the EU has launched 99 initiations against China which constitutes 28% of the 359 AD initiations launched by the EU in that period. As can be seen from the graph, AD initiations have increased after China's accession to the WTO in 2001, with an average of 6 initiations by year post Accession compared to only 2 initiations in the period before. There seems to be no

<sup>17</sup> (United States Government Accountability Office, 2006)



obvious relationship between the number of EU AD initiations against China and aggregate Chinese imports into the EU relative to total imports (figure 2).

**Figure 2: EU Anti-dumping Initiations against China**

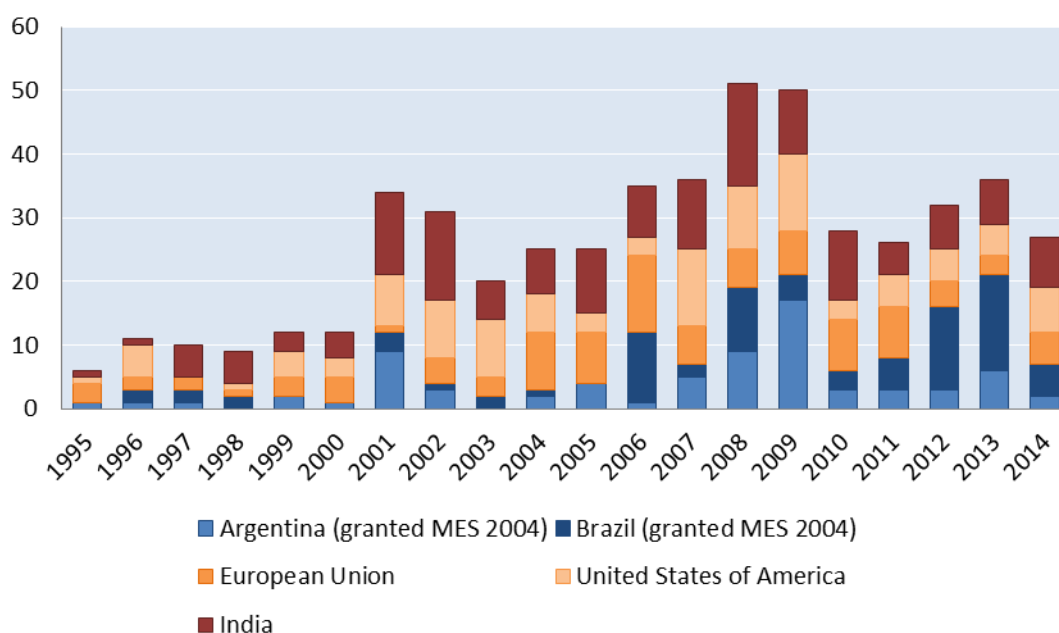


Source: Ifo Institute, AD data from WTO (2015a), import data from Eurostat (2015)

Figure 3 compares the European policy with other main users of AD Duties against China<sup>18</sup>. It can be seen that the EU is in third place behind India (152 AD initiations 1995 – 2014) and the USA (111). Overall, AD initiations by the top 5 imposing countries have increased since China's WTO accession but have fallen back again since 2010. This is mainly due to Argentina (which declared China a market economy in 2004<sup>19</sup>) and the USA which have both reduced their AD initiations from 2010 onwards.

<sup>18</sup> A complete list of countries imposing AD against China is provided in Appendix A3.

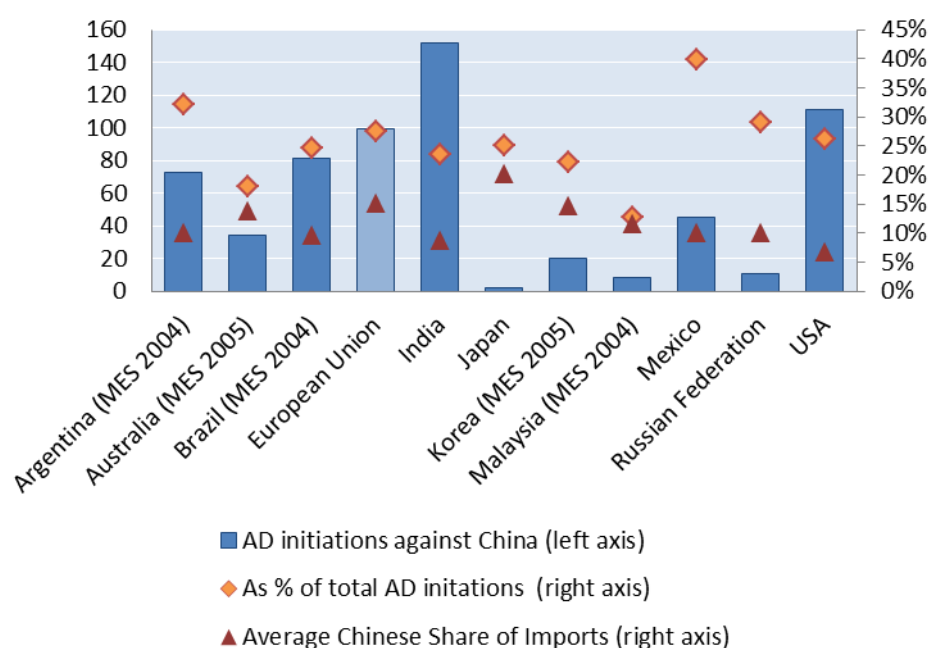
<sup>19</sup> Argentina signed a memorandum in 2004, which can be interpreted as a declaration of intent. Its AD practices against China were not affected by this (Urdinez, 2014).

**Figure 3: Anti-dumping initiations against China by the top 5 imposing countries, 1995 - 2014**

Source: Ifo Institute, AD data from WTO (2015a)

Relative to AD cases initiated against all countries between 1995 and 2014, figure 4 shows the EU roughly in the middle of China's main trading partners. Interestingly, those five countries in the sample that have granted market economy status to China on average initiated fewer AD cases against China, relative to their overall initiations (22%), compared to the six countries that did not grant MES to China (28%). However, when looking at MES granting countries individually, there is no clear trend showing a fall in AD initiations after granting MES to China<sup>20</sup>. This is illustrated in table 6, which provides the average number of initiations for those countries having granted MES to China both before and after doing so. **Argentina and Brazil** are noteworthy because for them AD initiations actually increased quite significantly after granting MES to China. However, they only **signed a memorandum of understanding, so they didn't change their treatment of China in their AD procedures despite officially declaring it to have received MES** (Puccio, 2015; Urdinez, 2014).

<sup>20</sup> (Urdinez & Masiero, 2015) actually find a negative impact of recognition of Chinese MES on the number of Anti-Dumping initiations. However their analysis may potentially suffer selection bias as MES granting countries had fewer AD initiations against China compared to non-MES granting countries even before granting MES. Further research is thus required to shed more light on the issue.

**Figure 4: Anti-dumping initiations against China by the top 5 imposing countries and other major trading partners 1995 - 2014**

Source: Ifo Institute, AD data from WTO (2015a), import data from Eurostat (2015) and (UN, 2015)

**Table 6: Average number of AD initiations against China per year, before and after granting MES**

Country	Year MES granted	Mean AD p.a. before MES	Mean AD p.a. after MES	Δ mean
Argentina	2004	2.0	5.3	3.3
Australia	2005	0.9	2.6	1.7
Brazil	2004	1.3	6.8	5.5
Indonesia	2004	0.1	1.4	1.3
Jamaica	2005	0.1	0.0	-0.1
Korea, Republic of	2005	0.8	1.1	0.3
Malaysia	2004	0.1	0.7	0.6
New Zealand	2004	0.1	0.3	0.2
Pakistan	2004	0.0	1.1	1.1
Peru	2004	1.2	0.5	-0.7
Philippines	2004	0.1	0.0	-0.1
South Africa	2004	1.8	1.9	0.1
Thailand	2004	0.2	1.5	1.3
Venezuela	2004	0.6	0.0	-0.6

Source: Ifo Institute, data from Urdinez & Masiero (2015) and WTO (2015a)

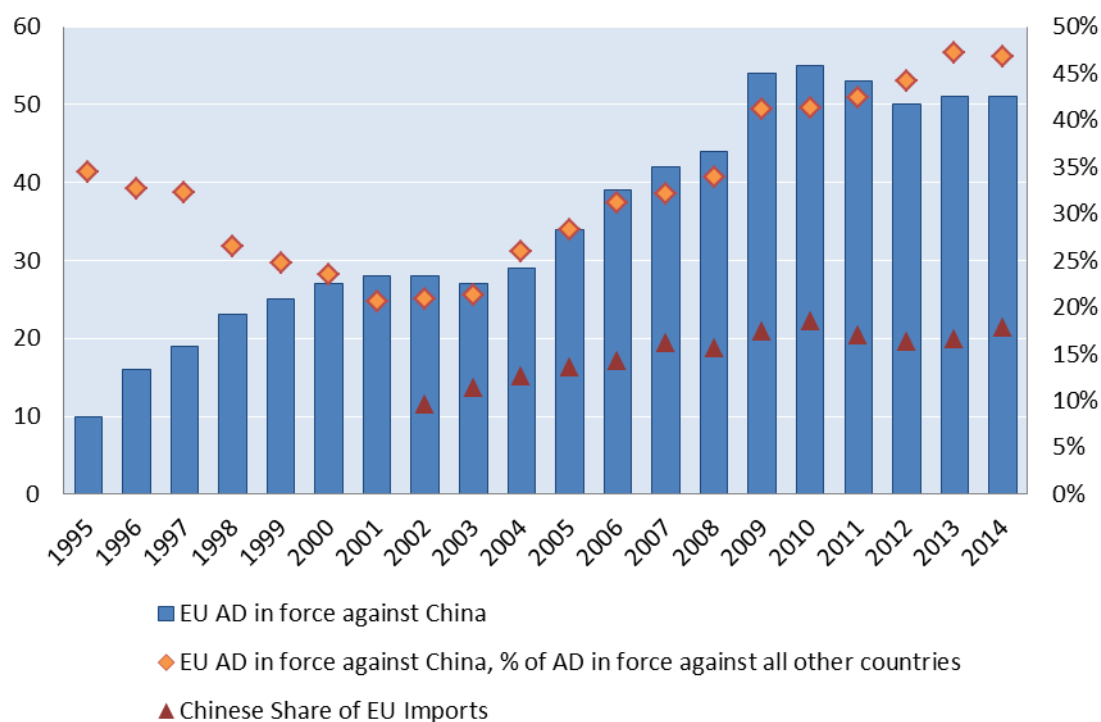
Furthermore, when looking at a country's imports from China relative to its total imports, there is no obvious correlation between the relative number of AD duties initiated against China compared to overall AD measures initiated and the relative importance of Chinese imports. More imports from China therefore do not necessarily lead to more AD measures being initiated against China. In fact the correlation coefficient is negative, though not very large (-0.2), meaning that countries importing more from China actually initiated fewer AD investigations. This aggregate analysis ignores potential heterogeneity across sectors, the significance of which is treated briefly further down. A detailed analysis is beyond the scope of this paper but should be addressed in future research.

On the one hand, this negative correlation could mean that importing more and increasing dependence reduces aggressive behaviour by the importer, possibly due to increased pressure not to bring AD complaints forward. On the other hand, the causal link could be the other way around, meaning that imposing fewer AD measures leads to more aggressive behaviour of Chinese exporters. The data does not allow any conclusion on this and deeper econometric analysis is required to obtain the direction of causality. There is no visible correlation between AD measures in force and relative imports.

### 3.3 Anti-dumping measures in force across the world

Figure 5 shows the number of European AD measures in force against China at the end of each year, both in absolute terms and as percentage of overall measures in force against all countries. The graph shows a clear reversal in trend, with 28 (21% of total) measures in force against China at the end of 2001 compared to 51 (47% of total) measures in December 2014. The reason for this increase in AD activity from 2002 onwards is, however, not clear. On the one hand, WTO entry could have established a clear legal framework, facilitating AD investigations. On the other hand, China's WTO entry was accompanied by an increase in trade volume (also shown in figure 5), which simply offers more potential for disputes. In fact AD measures should be seen in relation to the volume of European imports from China. In March 2014, the EU had 52 anti-dumping and three anti-subsidy measures in place against China which however affected less than 2% of total imports from China (European Commission, 2014). This figure however ignores the counter-factual, as it is not clear to what extent further dumped imports have been deterred by existing AD regulation.

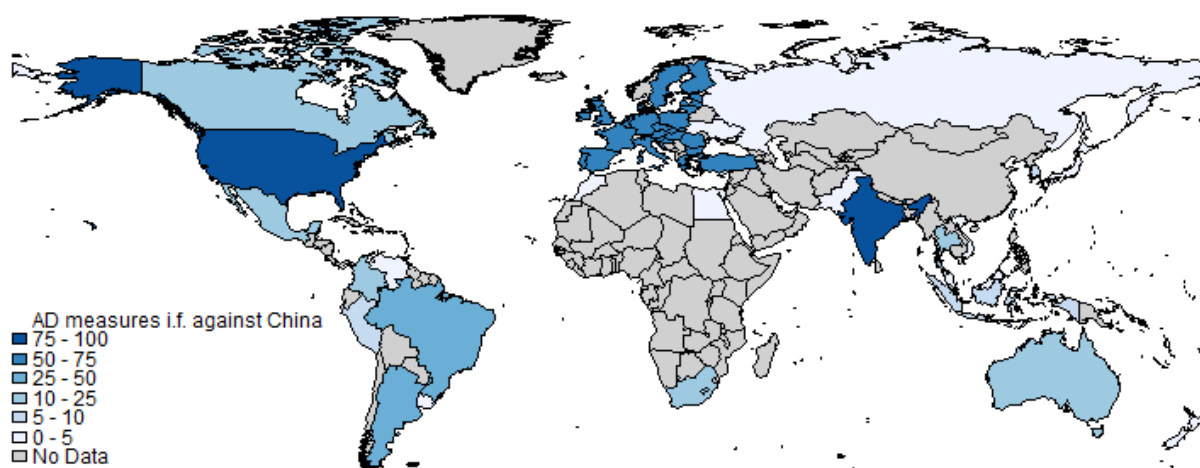
**Figure 5: EU Anti-dumping measures in Force against China**



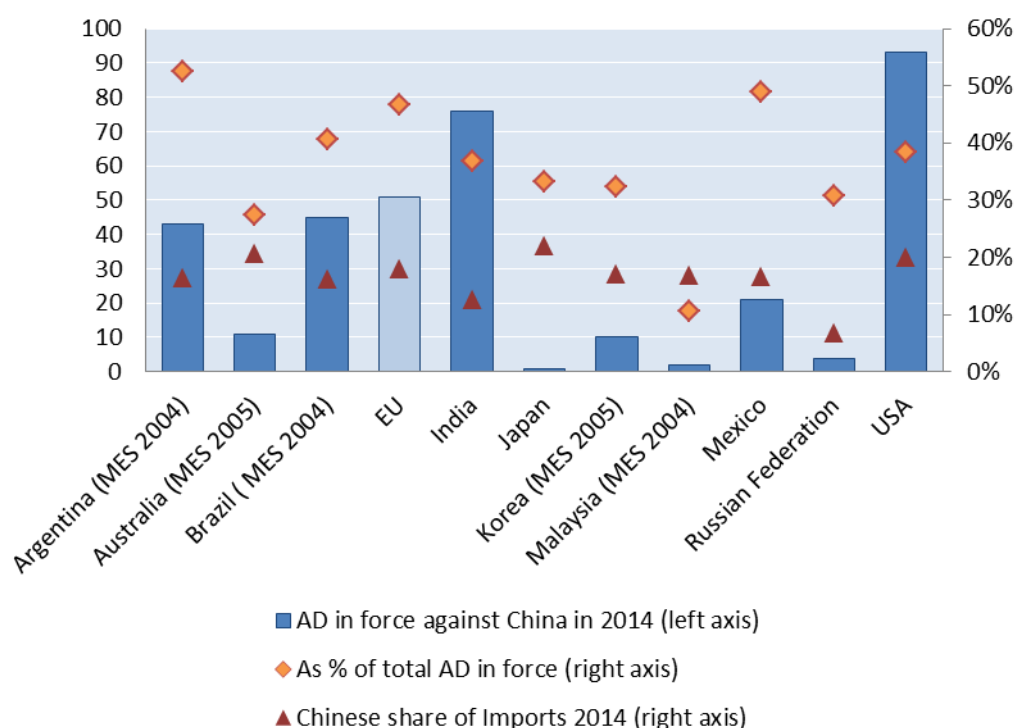
Source: Ifo Institute, data taken from Eurostat (2015) and WTO (2015a)

Figure 6a provides an overview of **AD measures in force** against China across the world. Figure 6b shows that the EU has the third largest number of AD measures in force, behind the USA (93) and India (76). In relation to overall AD measures in place, the EU targets China more frequently (47%) compared to both the USA (38%) and India (37%).

**Figure 6a: Anti-dumping measures in force against China by major trading partners in December 2014**



Source: Ifo Institute, AD data from WTO (2015a)

**Figure 6b: Anti-dumping measures in force against China by major trading partners in December 2014**

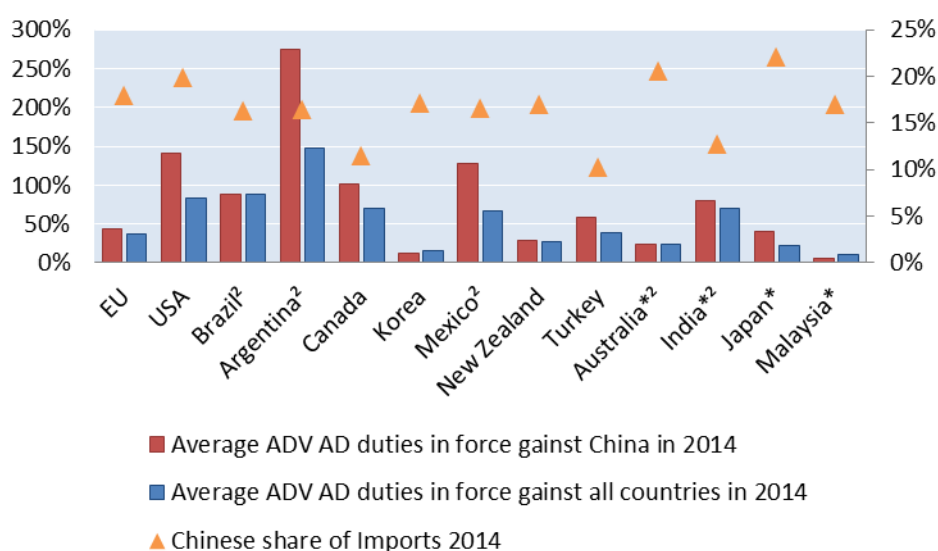
Source: Ifo Institute, AD data from WTO (2015a), import data from Eurostat (2015) and UN (2015)

### 3.4 Level of Anti-dumping measures across the world

Out of the 49 AD duties in force against China by the EU in 2014<sup>21</sup>, 41 consisted of an ad valorem (ADV) duty, which allows for easy comparison of duty levels across imposing countries (Bown, 2015). As illustrated in figure 7a below, the average European ADV AD duty of those measures in force in 2014 against China was 44%. This value is much lower than the average duty imposed by the USA (142%). The average levels of anti-dumping duties in force imposed by Argentina and Mexico are also extremely high but have to be viewed with caution, since only a small fraction of AD duties in those countries is ADV. The same is true for Australia and India. Considering the importance of imports from China compared to overall imports for a specific country, it is evident that countries which are more import dependent on China do not impose higher AD duties. As before these averages may disguise potential sector heterogeneity and further research should be conducted to address this. The map in figure 7b provides an alternative way to illustrate the heterogeneity between different countries.

<sup>21</sup> This number of AD duties in force (49) differs slightly from the number given above (51). This is due to the use of a different dataset for the calculation of average AD duties.

**Figure 7a: Average level of ADV AD duties in force against China in 2014**

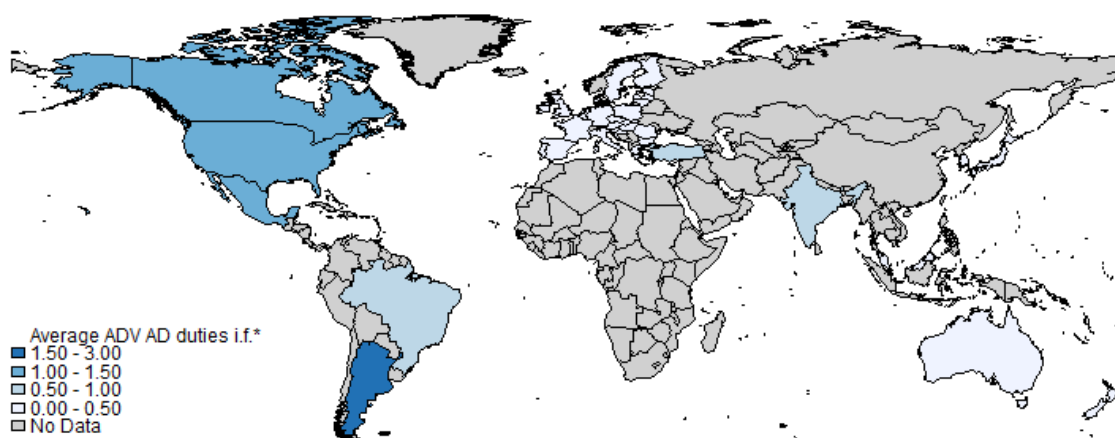


\*Mean of maximum and minimum margin imposed

<sup>2</sup> only very few ADV duties, so not necessarily representative

Source: Ifo Institute, AD data from Bown (2015), import data from UN (2015)

**Figure 7b: Average level of ADV AD duties in force against China in 2014**



\*in ADV AD expressed in ratios. For example, an ADV AD duty of 3.00 means 300%.

Source: Ifo Institute, AD data from Bown (2015)

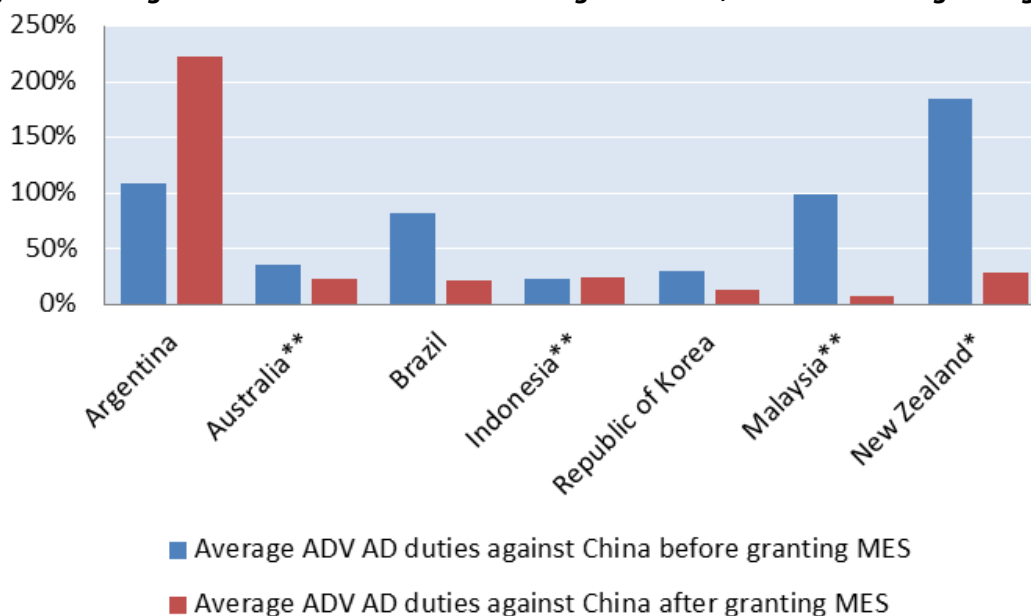
Figure 8 looks at countries that have granted China market economy status, comparing average levels of ad valorem AD duties initiated against China before and after granting it MES<sup>22</sup>. With the exception of Argentina<sup>23</sup> and India, average levels of ad valorem AD duties fell

<sup>22</sup> The numbers are not comparable to those in figure 7, since figure 8 looks at AD initiations. These may but don't have to still be in force.

<sup>23</sup> Argentina and Brazil are problematic since they only signed a memorandum of understanding, so they didn't change their AD policy towards China despite officially granting it MES.

after granting MES to China. This is in line with the lower EU AD duties observed for Chinese MET producers (figure 1 above). The reasons for this could be manifold, such as selection (most aggressive dumping with highest margins tackled first once China joined the WTO – a static view) and learning by producers (detering effect of high AD duties reduces dumping - dynamic). Both would lead to a decline of AD levels over time. Finally, if the analogue country principle leads to a price bias by means of the calculation of a normal value that is systematically above a normal value constructed using domestic prices, abolishing the analogue country system would lead to a fall in constructed dumping margins (Roberts, 2008). Further research could shed more light on this issue.

**Figure 8: Average level of ADV AD duties initiated against China, before and after granting MES**



\* Year of granting MES included in pre-MES sample, as no ad valorem duties were observed before the year of granting MES

\*\* Mean of Min and Max Margin imposed

Source: Ifo Institute, AD data from Bown (2015), import data from UN (2015)

### 3.5 Internal heterogeneity – Anti-dumping measures within the EU

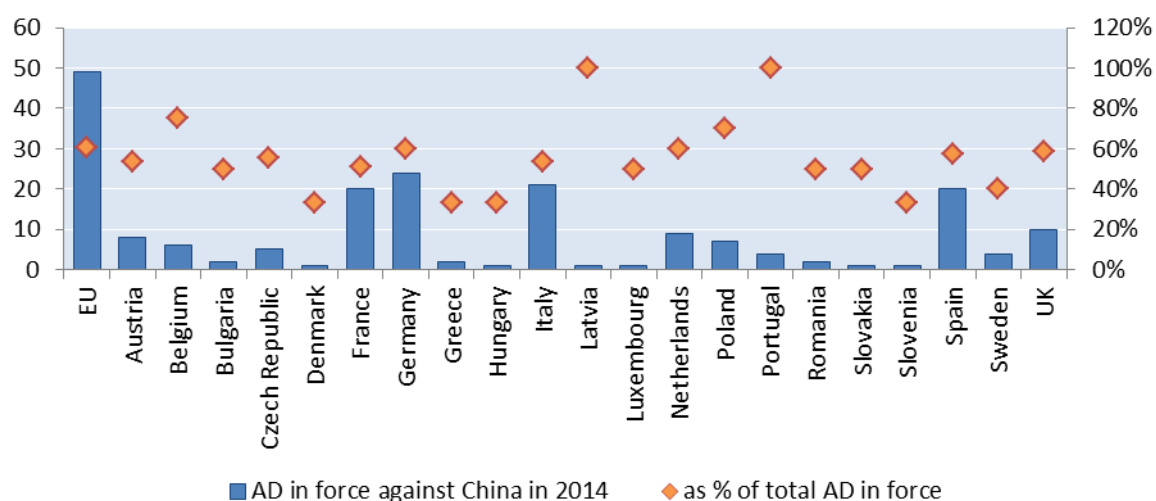
The aggregate number and average level of EU AD duties in force mask significant heterogeneity within the EU, both regional and sectoral. Figures 9a and 9b show the number of AD measures in force, sorted by origin of firms that initiated it (Bown, 2015)<sup>24</sup>. Once imposed, the AD duty affects imports into all European countries. However, looking at the origin of these AD duties may help identifying the firms that feel most threatened by Chinese dumping behaviour. It can be seen that there is a lot of variation in terms of the origin of the AD measures in force. This is true both in absolute terms as well as in relation to AD duties in force against all countries.

<sup>24</sup> For example, the figure for the UK is 10. This means that in 2014 there were 10 AD measures in force that were initiated through filings involving UK companies. If a case is filed by several companies headquartered in different countries, the measure is associated with all of these countries, so that double counting exists. Cases put through EU associations are excluded.



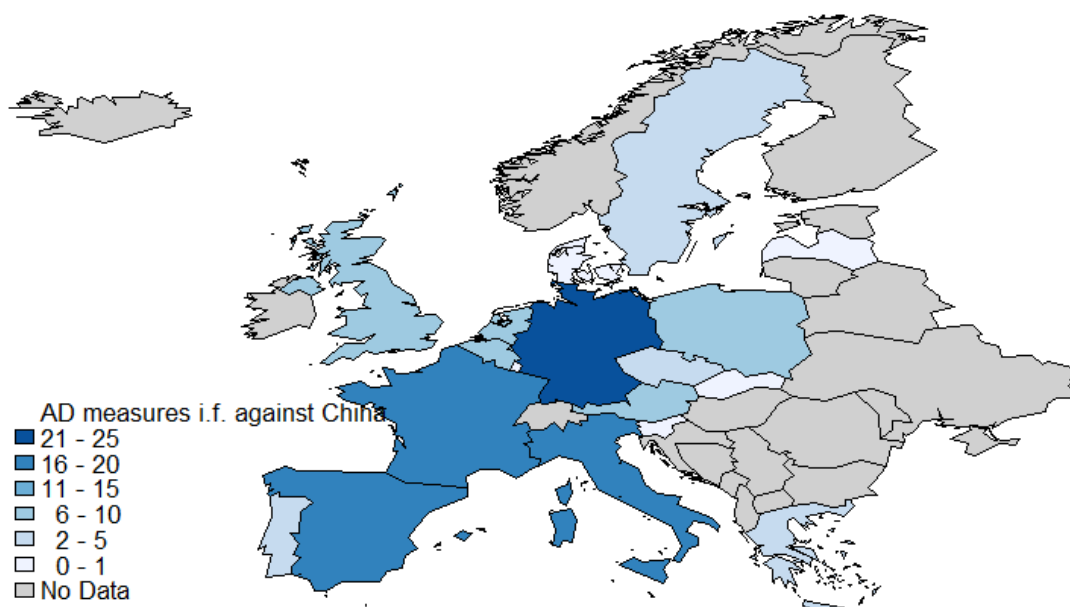
Companies in Germany, France, Italy, Spain and the UK were most often involved in the filing of AD cases. This is however not very surprising, since these countries are also the largest economies within the EU. It may thus be more informative to look at the number of AD measures against China relative to all other countries. If one excludes Latvia (just one case involving a Latvian firm), Belgium, Poland, Germany, the Netherlands and the UK are the countries where most AD cases were filed against China relative to overall cases. Although Germany, the Netherlands and the UK are also the countries with the highest share of Chinese imports, there is no clear correlation between relative imports from China and relative AD measures in force.

**Figure 9a<sup>25</sup>: Anti-dumping measures in force against China, by origin of firm initiating it**



Source: Ifo Institute, AD data from Bown (2015)

<sup>25</sup> EU AD measures in force differ from those in figure 7 due to the use of a different database. Individual countries' AD cases do not add up to EU total as companies from several countries can be involved in a single AD case.

**Figure 9b: Anti-dumping measures in force against China, by origin of firm initiating it**

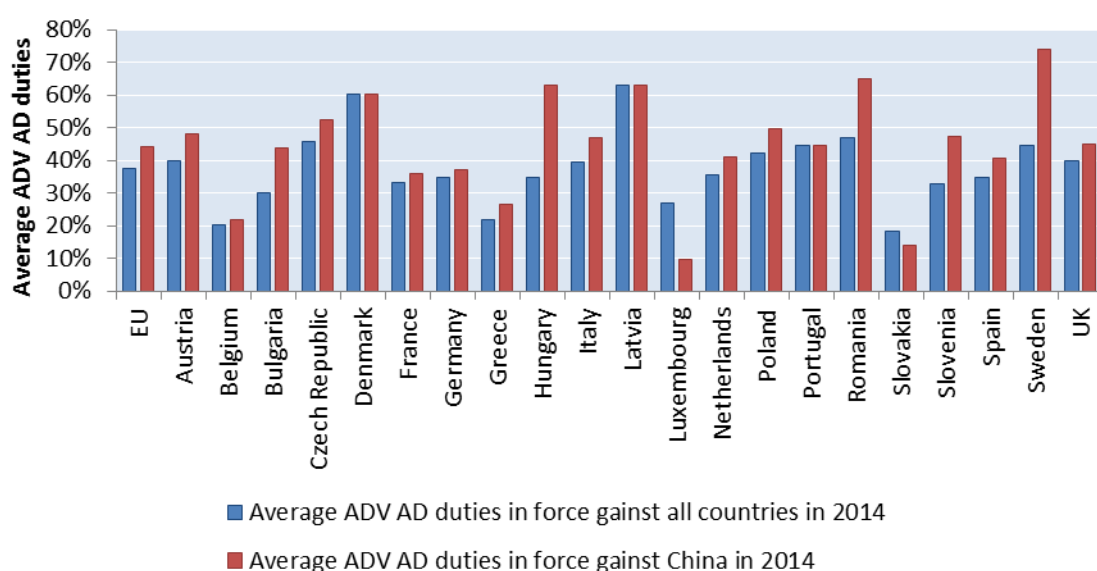
Source: Ifo Institute, AD data from Bown (2015)

The picture is different if one looks at the level of AD measures in force, as figures 10a and 10b do. Figure 10a shows that AD measures initiated due to filings of firms in Sweden, Latvia, Denmark and the Czech Republic lead to the highest levels of AD duties, followed by Italy, Austria and Poland. AD cases filed in Sweden, Slovenia and Italy show the largest difference between duty levels imposed against China and those imposed against other countries. On the one hand, this could simply stem from the way the statistic is constructed: If ad valorem duties are mainly imposed against China and specific duties mainly against other countries, China would dominate the 'all countries' category, leading to more or less equal AD duties.

On the other hand, the regional difference could stem from differences in sector concentration in individual countries. If a country's industrial activity is concentrated in a particular sector which experiences a lot of dumping from Chinese firms, this would result in higher average levels. To illustrate this, for companies from each country, figure 10b shows the level of ADV AD duties in force, together with the number of initiations<sup>26</sup> and the number of different sectors involved<sup>27</sup>. It shows that averages for large countries such as Germany, France Italy and Spain are constructed from many cases in 6 to 8 sectors, whereas in countries such as Sweden and Denmark, there were only very few cases in a few sectors.

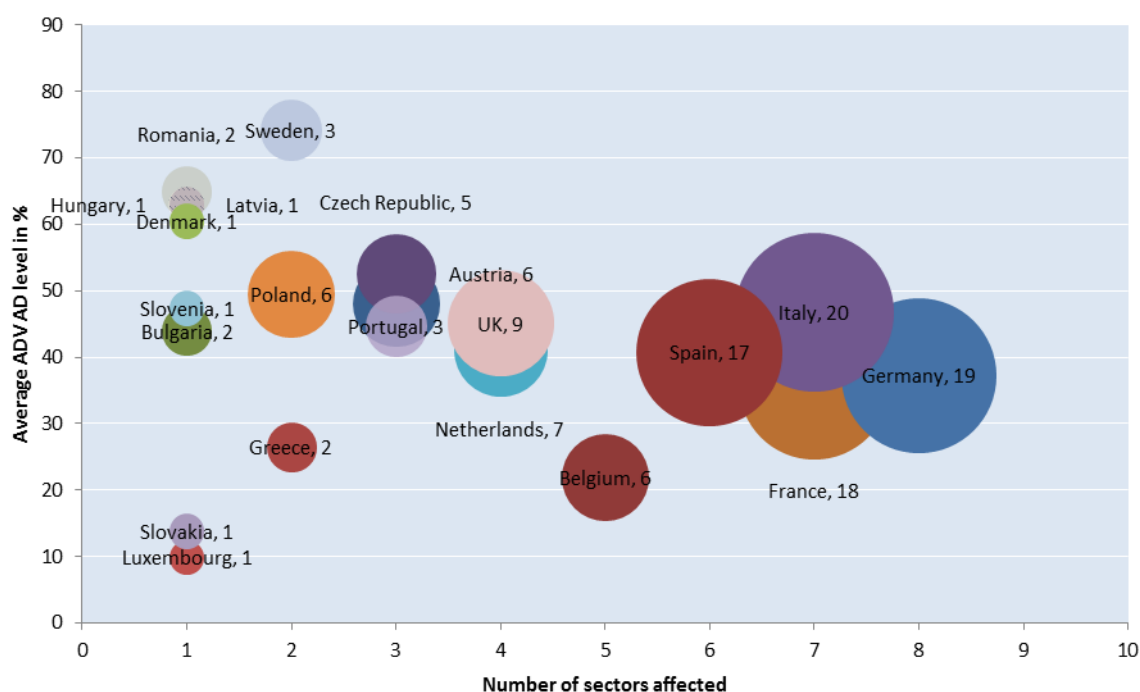
<sup>26</sup> ADV AD duties only<sup>27</sup> HS2 codes lumped together into 16 sectors, following (Foreign Trade, 2015)

**Figure 10a: Average level of Anti-dumping duties in force, by origin of firm initiating it**



Source: Ifo Institute, AD data from Bown (2015)

**Figure 10b: Average level and number of Anti-dumping duties in force and number of sectors affected, by origin of firm initiating it**



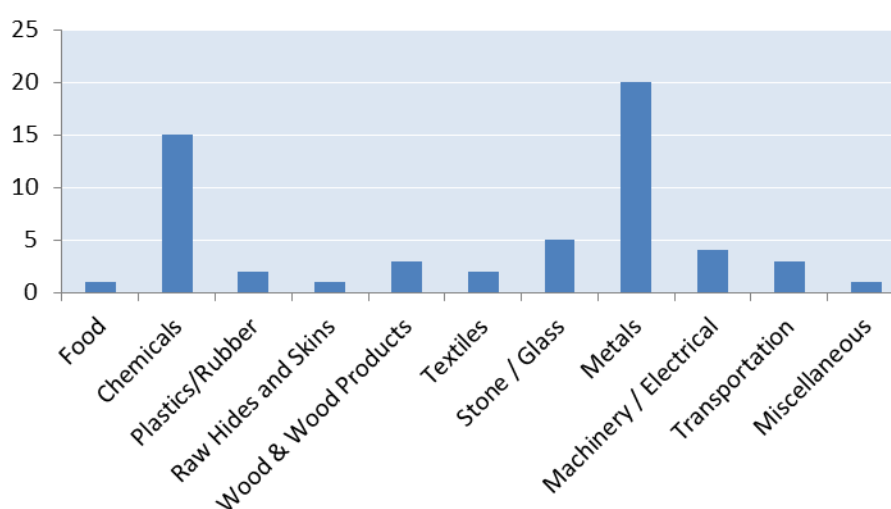
Bubble size: Number of ADV AD measures in force

Source: Ifo Institute, AD data from Bown (2015)

### 3.6 Sectoral variation of Anti-dumping measures

The previous section has shown that aggregate numbers hide a significant heterogeneity across sectors, which also drives the heterogeneity across countries. As illustrated by figure 11 below, the **metals** and the **chemical sector** account for most EU AD measures in force against China, with 20 and 15 AD measures respectively<sup>28</sup>. They are driven by Europe's large economies Germany, France, the UK, Italy and Spain. This sectoral division is noteworthy, because China has a comparative advantage in the metals sector vis-à-vis the large European economies, meaning that its companies are on average more productive than their European counterparts<sup>29</sup> (Leromain & Orefice, 2013). Nevertheless, the chemical sector does not exhibit such large differences in comparative advantage, with no significant differences between China and the five largest EU countries.

**Figure 11: EU Anti-dumping measures in force against China in 2014, by sector<sup>30</sup>**



Source: Ifo Institute, data from Bown (2015)

It should be noted however that the data does not provide clear guidance on how the comparative advantage is to be interpreted. On the one hand it could stem from a **genuine cost advantage of Chinese producers**. On the other hand it might stem from **dumping activity** if the price of steel in China does not reflect the 'true resource cost' (Ruiz, Somerville, & Szamosszegi, 2015). In the latter case, the frequent occurrence of AD activity in these sectors may be interpreted as a successful identification of dumping activity. However, this would imply systematic dumping across producers within an entire sector (e.g. because of excess capacity). Finally, there could also be an endogenous relationship between AD and comparative advantage, meaning that each affects the other (see section 4.4). Identifying the forces at work here should be the task of future research.

<sup>28</sup> The figure lists the number of AD measures in force by sector. Hence double counting is possible if a case involves products from different sectors, which does happen occasionally.

<sup>29</sup> Appendix A5 provides a detailed overview of countries' comparative advantage by sector.

<sup>30</sup> As footnote above.

A similar concentration of AD cases in a few sectors can be observed across countries. As illustrated in table 7 below, most AD cases are in force in the metals and chemicals sectors, followed by machinery/electrical, textiles and plastics/rubbers. The table shows that AD most often takes place in sectors in which countries have a comparative disadvantage against China. In fact, there exists a (weak) negative within country correlation between comparative advantage vis-à-vis China and the number of AD measures in force<sup>31</sup>.

Nevertheless sectors in which China generally has a comparative disadvantage - such as chemicals and plastics/rubbers - are also frequently targeted. In addition to the above mentioned frequently targeted sectors, there are also some notable differences across countries, potentially reflecting domestic industry structure. For example, while the USA and the EU both primarily have AD measures in force in the metals, chemical and machinery sector, Argentina and Brazil are also quite active in the plastics / rubbers and textile sectors<sup>32</sup>. There is no obvious relationship between a country's decision to grant MES to China and the structure of its comparative advantage.

To sum up, it is essential to realize that **AD duties are not an economy wide phenomenon**, but are **highly concentrated in specific sectors**. These sectors may indeed be very vulnerable to dumping activity (see for example Ruiz et al. (2015) for the steel industry in the USA, Mexico and Canada). Therefore, even if the EU grants China market economy status, a middle-ground solution might see individual sectors continuing to receive special treatment as indicated in council regulation No 1972/2002, allowing the remaining ones to receive MET.

<sup>31</sup>Negative for Argentina (-0.4), Australia (-0.3), EU (-0.1), South Africa (-0.3), USA (-0.1); positive for Brazil (0.6), India (0.2) and South Korea (0.2)

<sup>32</sup> The Stone and Glass sector also experiences a lot of AD activity. It is excluded here since no data on comparative advantage is available. AD cases in missing sectors are listed in table A7 in the Appendix.

**Table 7: AD cases in force and revealed comparative advantage against China by country and sector**

Country	Sector	AD cases i.f. 2014	RCA Country	RCA China	Advantage vs. China	RCA relative to China
Argentina	Machinery / Electrical	11	0.81	1.12	-	0.72
Argentina	Plastics / Rubbers	5	0.98	0.99	-	0.99
Argentina	Textiles	5	0.79	1.44	-	0.55
Argentina	Metals	5	0.82	1.18	-	0.69
Argentina	Transportation	3	0.89	1.16	-	0.77
Argentina	Chemicals & Allied Industries	1	0.84	0.99	-	0.85
Argentina	Wood & Wood Products	1	1.01	1.13	-	0.89
Australia	Metals	5	1.01	1.18	-	0.86
Australia	Chemicals & Allied Industries	3	0.95	0.99	-	0.96
Australia	Machinery / Electrical	1	1.00	1.12	-	0.90
Australia	Transportation	1	0.95	1.16	-	0.82
Australia	Foodstuffs	1	1.24	0.85	+	1.46
Brazil	Metals	11	1.11	1.18	-	0.94
Brazil	Plastics / Rubbers	6	0.96	0.99	-	0.97
Brazil	Chemicals & Allied Industries	5	0.85	0.99	-	0.86
Brazil	Machinery / Electrical	5	0.86	1.12	-	0.77
Brazil	Textiles	3	0.81	1.44	-	0.56
Brazil	Transportation	1	0.91	1.16	-	0.78
EU	Metals	20	1.01	1.18	-	0.86
EU	Chemicals & Allied Industries	15	1.01	0.99	+	1.02
EU	Machinery / Electrical	4	1.00	1.12	-	0.89
EU	Wood & Wood Products	3	1.05	1.13	-	0.93
EU	Transportation	3	0.99	1.16	-	0.85
EU	Plastics / Rubbers	2	1.00	0.99	+	1.01
EU	Textiles	2	1.02	1.44	-	0.71
EU	Foodstuffs	1	1.04	0.85	+	1.22
India	Chemicals & Allied Industries	44	1.03	0.99	+	1.04
India	Textiles	12	1.26	1.44	-	0.88
India	Machinery / Electrical	11	0.99	1.12	-	0.89
India	Plastics / Rubbers	10	1.09	0.99	+	1.10
India	Metals	6	1.01	1.18	-	0.86
India	Wood & Wood Products	3	0.95	1.13	-	0.84
India	Transportation	2	0.93	1.16	-	0.80
India	Foodstuffs	2	1.03	0.85	+	1.21
Indonesia	Metals	28	1.06	1.18	-	0.90
Indonesia	Textiles	1	1.16	1.44	-	0.81
South Korea	Chemicals & Allied Industries	2	1.12	0.99	+	1.13
South Korea	Textiles	2	1.04	1.44	-	0.72
South Korea	Plastics / Rubbers	1	1.07	0.99	+	1.08

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South Korea	Wood & Wood Products	1	0.75	1.13	-	0.66
South Korea	Foodstuffs	1	0.72	0.85	-	0.85
Russia	Metals	4	1.10	1.18	-	0.93
South Africa	Metals	7	0.95	1.18	-	0.81
South Africa	Textiles	2	0.85	1.44	-	0.59
South Africa	Chemicals & Allied Industries	1	0.86	0.99	-	0.87
South Africa	Plastics / Rubbers	1	1.12	0.99	+	1.13
USA	Metals	40	0.98	1.18	-	0.83
USA	Chemicals & Allied Industries	25	1.06	0.99	+	1.07
USA	Machinery / Electrical	10	1.07	1.12	-	0.96
USA	Wood & Wood Products	7	1.13	1.13	-	1.00
USA	Textiles	7	0.86	1.44	-	0.60
USA	Foodstuffs	6	1.02	0.85	+	1.20
USA	Plastics / Rubbers	5	1.01	0.99	+	1.02
USA	Transportation	1	0.99	1.16	-	0.85
USA	Mineral Products	1	1.02	1.05	-	0.97

Note: RCA data is for 2010. RCA for EU is average of Germany, Italy, Spain, France, UK and Netherlands. RCA for Machinery/Electrical sector is mean of the two individual sectors. Sectors for which no RCA was available are dropped and presented in a separate table in the Appendix. Total number of AD in force by country may exceed the aggregate presented earlier because one AD case may affect several sectors, leading to double counting.

Source: Ifo Institute, AD Data from Bown (2015), RCA data from Leromain & Orefice (2013)

## 4 Opportunities and threats for the EU

Assessing the effects of granting MES to China solely based on the impact of changing AD duties on trade volumes and employment in the EU is insufficient. It neglects important opportunity costs which may arise on further economic and political levels that are not directly linked to AD policies. First of all, not granting MES to China certainly will have an impact on how China strategically acts within the WTO (litigation). In addition, China may put the MES issue on the agenda in bilateral investment treaty negotiations with the EU. Finally, the EU has to assess how a unilateral approach may affect further economic and policy relations with third countries. To give an example, if the USA decides to choose another treatment of China than the EU, this may have implications for bilateral policies such as the ongoing TTIP negotiations.

### 4.1 Employment effects of granting MES to China

Quantifying trade and employment effects that may result from granting China MES is a difficult task. To the best of our knowledge, there is no academic literature to date which has presented a comprehensive analysis<sup>33</sup>. An exception is a recent policy paper by Scott & Jiang (2015) that presents the potential effects of granting MES to China on European output and employment. Core findings of the paper are that a unilateral decision of the EU to grant China MES would risk up to 3.5 million jobs and reduce EU output by up to EUR 228 billion per year. To put the importance of AD measures into perspective, it should be noted that EU imports from China in 2014 amounted to around EUR 300 billion (European Commission, 2015d), of which only 2% (EUR 6 billion) have been affected by AD cases (European Commission, 2014)<sup>34</sup>. A fundamental assumption of this policy paper is that all Chinese companies will receive MET in the future. Clearly, assuming a complete disappearance of NMET may be an appropriate way to estimate an upper bound of the effect<sup>35</sup>.

While it is beyond the scope of this ad hoc briefing to perform a general equilibrium analysis and calculate full employment effects, it is nevertheless possible to conduct a preliminary back of the envelope calculation in order to put the findings of Scott and Jiang (2015) into perspective.

Using the finding of Detlof & Friedh (2006) - which is confirmed by our small sample for China - of an average AD duty of 11% for MET companies compared to 39% of NMET companies - one can assume a fall in the average AD duty against Chinese companies of 28 percentage points from 2016 onwards if MES is granted. This is indeed what Scott & Jian (2015) do. However, those countries already receiving MET may well be the ones that are most competitive, have the lowest domestic prices and thus face the lowest Anti-Dumping Duties (see section 2 for detailed discussion). For this reason, the market economy average of 22% might be more realistic than the MET average of 11%. This would imply a fall in average duties of only 17 percentage points, rather than 28.

<sup>33</sup> There have however been studies looking at the effect of MES on the number of AD initiations and other related topics (Davis, 2009; Sun & Whalley, 2015; Urdinez & Masiero, 2015; Ruiz et al. 2015).

<sup>34</sup> This does not take into account the deterring effect of AD duties as discussed further down.

<sup>35</sup> Even with MES it may be possible to grant individual companies or sectors NMET, as outlined in section 2. Further research is however required to determine if this is feasible in the case of China.



A 28 percentage point difference could constitute an upper bound for the prospective change in average AD duties. Scott & Jiang (2015) use this estimate (rounded to 30%) to calculate a demand increase of 40.5% to 55.2%. This calculation is based on parameters reflecting behaviour of **Non-OECD** countries (Tokarick, 2010). Given the composition of the EU, using parameters from OECD countries would seem more intuitive. More importantly, the authors ignore adjustments in goods and labour markets. Incorporating such adjustments would – still on a basis of a 28 percentage point decline in duties – only lead to change in imports of 19% to 25%, about half the estimates of Scott and Jiang (2015)<sup>36</sup>.

Nevertheless, once again using an upper bound, let us consider an estimated increase of 40.5% to 55.2%. Scott and Jiang (2015) seem to implicitly assume that this change applies to all Chinese imports into the EU. However, as only 2% of imports from China into the EU have been affected by AD duties in 2014 (European Commission, 2014), this is not very plausible. It could of course be true that some firms that previously have not exported to the EU using dumped prices may feel encouraged to do so once they are guaranteed MET. However, there is no evidence that this would cause an effect as big as suggested by Scott and Jiang (2015). Hence, based on 2% EU imports from China, granting all Chinese exporters MET would imply an increase in EU imports of between 0.81% and 1.1% using the methodology of Scott and Jiang (2015). Taking into account adjustments in goods and labour markets would reduce the increase of Chinese imports to 0.38% - 0.49%. Finally, if the change in average AD duties turns out to be closer to 17 rather than 28 percentage points, the increase in exports would reduce to 0.23% to 0.30%. This is equal to an increase in imports from China of EUR 0.67 billion to EUR 0.9 billion.

As delineated above recently published studies such as Scott and Jiang (2015) present potential effects which may result after granting China MES. From an academic point of view the results have to be questioned, given the extreme assumptions of the analyses. At the same time, the lack of academically sound empirical quantifications points towards an urgent need to shed more light on these effects.

## 4.2 Externalities of not granting MES to China

As briefly discussed in section 2.1, the WTO dispute settlement including AD cases has to be seen in a broader context. AD disputes permit to resolve trade conflicts on the basis of rules in a peaceful manner. At the same time they enable member states to conduct free trade and address domestic liberalization processes. Given the legal ambiguity of whether **China** will receive MES in 2016 it is most likely that its government will use this judicial fuzziness to **initiate strategic litigations** if WTO members get entangled in legal parsing (Hufbauer & Cimino, 2015; Watson, 2014). In recent years, China has challenged various aspects of certain contingent measures resulting in prolongation and increasing dispute complexity.<sup>37</sup>

Moreover, beyond a possible increasing confrontation between China and the EU within the WTO, there is a real risk that not granting MES will have externalities on other bilateral negotiations taking place. China has good reasons to question why it should agree to a deep and comprehensive Bilateral Investment Treaty (BIT) with the EU, resulting in stronger vertical

<sup>36</sup> A more detailed analysis of their methodology is given in the Appendix.

<sup>37</sup> See e.g. WTO DISPUTE DS437.

and horizontal (Hufbauer & Cimino, 2015; Watson, 2014).<sup>38</sup> Once a Sino-European BIT is signed, a larger share of Foreign Direct Investments (FDI) by European firms to produce e.g. intermediate goods for the EU market in China can be expected.<sup>39</sup> It should be difficult to convince Chinese negotiators why the whole Chinese economy is still considered to be a NME while at the same time an increasing number of foreign owned investments are promoted.

Generally stated, the EU's decision on whether China should be granted MES will certainly have an impact on the general atmosphere of commercial relations at latest after December 2016.

### 4.3 Externalities of a Unilateral Grant of MES to China

While the EU should expect increasing confrontation with China in its economic relations if NMES is maintained, on the other hand granting MES is most likely to result in negative repercussions with third countries if the EU does not coordinate its AD policy adjustment with other important WTO members such as the USA. Different stakeholders in the USA have started to push the government in order to enforce retention of China's MES in EU law claiming that '... If the EU makes a change in treatment of China under its AD regulation when China has not in fact truly engaged in comprehensive reform of its economy, there will be broad repercussions for how fair market conditions will be assessed in Europe and, in terms of American exports to the EU, could result in dramatically lower opportunities for the export of America's manufactured products [trade diversion].

Particularly, the steel industry, which is subject to regular AD cases with China insists that if the EU chooses to grant China MES, either for the whole economy or for some industries or firms, it will subject US products to a potential risk of having to compete against unfairly traded products in the EU and, potentially, as components in products shipped to the USA or to third country markets. Thus, the EU's decisions on granting China MES must be addressed as part of the on-going TTIP negotiations.<sup>40</sup>

To sum up, a major challenge for the EU thus will be to find a viable AD regulation adjustment which balances both the expectation of China's government and at the same time to assuage third countries' or groups' justified concerns that may also result in tightened relations with respective countries such as the USA.

### 4.4 Dynamic effects of a special AD regulation against China

In order to derive a final policy conclusion on whether China should be granted MES it is desirable to build on evidence based on empirical analysis estimating employment and further economic effects. Unfortunately, the available academic literature has not much to say on AD effects in the context of China and MES. This is not surprising, as a causal analysis of how a change in China's treatment in AD regulations may affect other countries requires a comparable case or alternatively an ex-post analysis once China has been granted MES. These data requirements are simply not met so far and as illustrated in section 3.1 those cases which

<sup>38</sup> The first round of negotiations for an EU-China investment agreement took place in Beijing on 21-23 January 2014.

<sup>39</sup> A large empirical literature illustrates the average positive effect of BITs on FDI flows once investment treaties are in force (Egger & Pfaffermayr, 2004).

<sup>40</sup> This position has been expressed by the United Steelworker (USA) in a letter to United States Trade Representative in October 2014.

granted China MES (or only declared their intention) are very specific countries which did not always implement the MES of China into AD laws.

Two important effects, however, have been discussed based on neat empirical estimations. Lu, Tao, & Zhang (2013) illustrate how Chinese exports to the USA are affected by AD. A core finding is that the decrease in Chinese exports following AD measures is to a large extent driven by less productive Chinese firms. The export volume of firms that can bear the AD duties does not change significantly. Hence, AD duties against Chinese firms affect primarily weaker exporters, thus increasing average productivity in the respective Chinese industries. Differently stated, temporary AD duties against an entire industry – by eliminating less productive producers - increase competitiveness of the surviving firms in the long run. Hence, **an undiversified (not firm specific) AD regulation against China exposes domestic producers to a fiercer competition with China in the long run** (Lu et al., 2013).

Finally, an issue which has not been investigated in detail in the trade literature is the fact that a special AD regulation for China may result in more affirmative dumping decisions due to the specific regulations. Roberts (2008) illustrates for the USA that AD cases against China with a non-market economy method of calculating prices biases the “normal price” upwards. As a consequence China experiences significantly more AD decisions compared to other countries. At the same time in AD cases in which NME status is not taken into account, China experiences affirmative decisions of the same rate as the international average (Roberts, 2008).

While these two important findings are based on individual academic analyses they still point on two important effects that appear to arise if China receives a special treatment. Implicitly, maintaining a NME method in AD regulation for China may confront the EU with an unintended fiercer competition in the long run. Furthermore, applying a price comparison on the basis of analogue countries can result in a biased AD decision due to the applied methodology but not because of real dumping. A discrimination of Chinese imports based on the chosen regulation will certainly put the EU regulation under pressure, as it cannot be sustainable within WTO regulations.

Of course AD regulations of the EU and the USA against China differ substantially (see section 3.1). Consequently, a broader and deeper analysis based on EU data is required in order to make sensible policy recommendations.

## 5 Policy recommendations and conclusion

Paragraph (a) (ii) of Article 15 in China's Accession Protocol to the WTO - which determines the basis on which dumping margins are calculated in AD proceedings against China - is about to expire in December 2016. This requires a decision by the EU of whether to adjust its AD regulation. This ad hoc briefing has illustrated the complexity of the MES question related to China.

The legal implications of the expiry are highly controversial. Existing views range from maintaining the status quo to granting MES to China automatically in 2016. This briefing is not intended to assess which of the publicly discussed legal interpretation is correct. Instead the focus is put on economic aspects related to China's treatment in EU AD regulation.

The comparative analysis has illustrated several differences in how the EU and other countries deal with China in their AD regulation. First of all conditions for granting market economy differ across countries. For example, while the EU has defined a clear list of criteria such as a basic set of accounting records, other countries including the USA and Argentina allow themselves more discretion.

Differences across China's major trading partners are also found in the number and levels of AD measures in force against the country. With 51 AD measures in force against China (47% of total), the EU is at third place, behind the USA (93 measures in force, 38% of total) and India (76 measures, 37% of total). The average EU level of (ad valorem) AD duties in force is 44% (for the USA 142%, and for India 80%). If the EU grants China MES, it may expect average dumping duties to fall by 17 - 28 percentage points. According to several studies this expected drop in AD duties will cause a decline in domestic output and employment. However, the presented large quantitative effects have to be treated with caution as they rely on extreme assumptions.

The comparative analysis has also shown that AD measures are not equally applied across all industries within the EU. In fact they are concentrated in the steel and chemical industries. A comparison of comparative advantage indicators in the steel industry shows China in front of the EU. However, the available data does not provide clear guidance on how the comparative advantage is to be interpreted. On the one hand it could stem from a genuine cost advantage of Chinese producers. On the other hand it might stem from dumping activity. Preliminary evidence suggests that similar patterns exist in other countries.

Beyond the publicly discussed employment effects potentially associated with granting China MES, the study highlights further opportunities and threats that should be taken into account in order to fully understand the impact of adjustments in EU AD regulation. For example, in light of the legal ambiguity of whether China's WTO Accession Protocol grants the country an automatic recognition of MES, it is possible that if the EU maintains China's NMES, the country will use the legal fuzziness to initiate strategic litigations within the WTO.

On addition, the EU is attempting to advance commercial relations with China in many areas that will shape Europe's competitiveness in the next decades. Based on the currently negotiated comprehensive BIT between China and the EU, bilateral trade and investment are most likely to intensify. Not granting MES to China may affect EU negotiations with China. On the other hand, a unilateral policy decision may lead to bilateral tensions between the USA and the EU, e.g. within the context of the TTIP negotiations.

To sum up, this ad hoc briefing identifies several potential effects that may result from different adjustments in EU AD regulation with respect to China. An important question now is

whether the EU only has two policy options available, namely maintaining China's NMES or granting the country MES. In fact, a middle-ground solution might be granting MES to China with a degree of discretion. Council regulation No 1972/2002 (European Union, 2002) constitutes a precedence providing for the possibility to treat certain producers within market economy countries with non-market economy treatment. Such a procedure was introduced when the EU granted Russia MES in 2002 and allows the use of prices or production costs of a third country if 'a particular market situation' exists. Whether such a third option is legally and practically feasible in case of China however should be the subject of further investigation.

Indeed, this briefing was just a first step. It has clearly demonstrated the need for further research to identify and understand the underlying forces at work so that policy makers can make an informed decision.

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## Appendix

### A1 Critique of the methodology employed by Scott and Jiang (2015)

Scott & Jiang (2015) combine the projected change in AD duties of 28% (rounded to 30%) with an import demand elasticity of -1.35 to -1.84 in short and long run respectively, yielding a demand increase of 40.5% to 55.2%<sup>41</sup>. First of all they use elasticities from High income Non-OECD countries, whereas, given the nature of the EU, High income OECD countries would probably be more appropriate. This would actually increase the elasticity to -1.46 to -2.01 in the short and long run respectively (Tokarick, 2010). However, we see no reason why general equilibrium effects should be ignored as goods and labour markets adjust. Allowing for general equilibrium effects would cut the elasticities by half, to -0.67 and -0.88.

With general equilibrium effects, a 28% change in the price would thus lead to a change in imports of 19% to 25%, an increase only half the size of Scott & Jiang's (2015) estimate. Taking into account the fact that only 2% of Chinese imports are affected, this number falls to 0.38% to 0.49%. Table A1 below compares three different calculation methods to demonstrate the importance of the individual assumptions.

**Table A1: Naïve estimate of change in EU AD duties on imports from China**

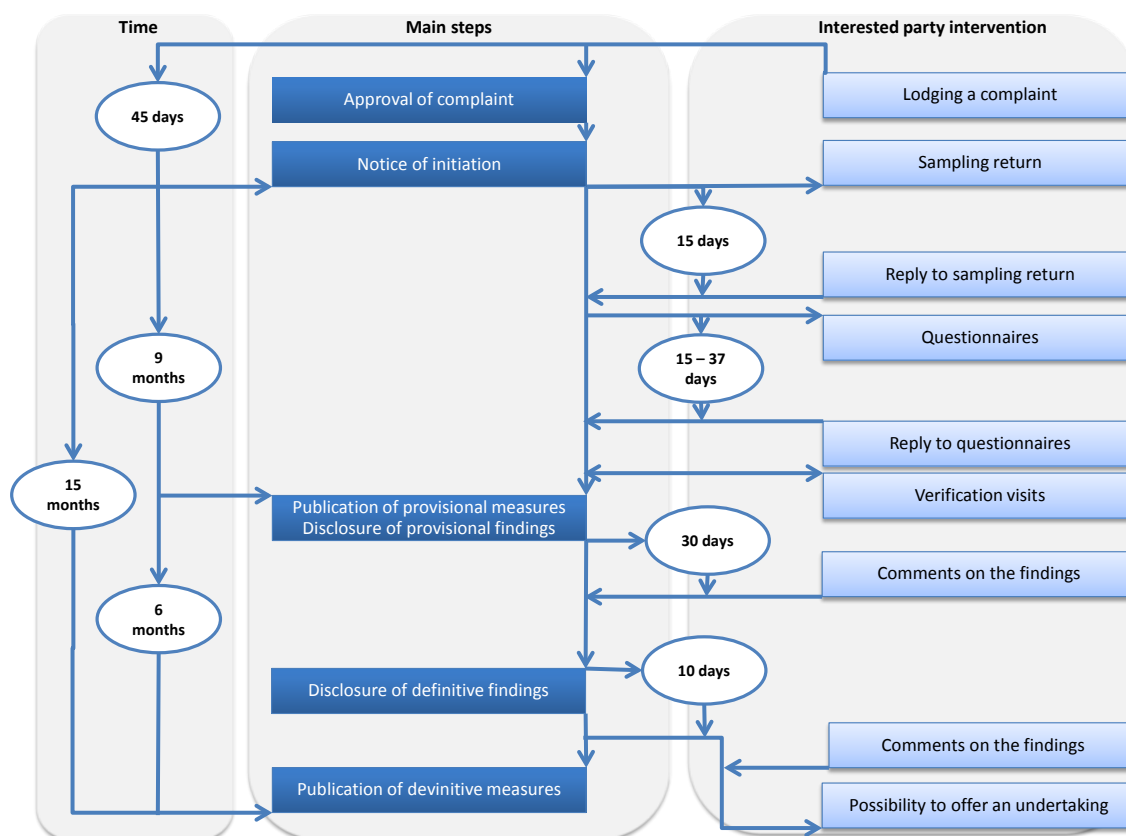
	Change in average AD duties	Short term elasticity	Long term elasticity	Short term change in imports in affected sectors	Long term change in imports in affected sectors	Short term change in aggregate imports	Long term change in aggregate imports
<b>Scott &amp; Jiang (2015)</b>	-30%	-1.35	-1.84	40.5%	55.2%	0.81%	1.10%
<b>GE effects</b>	-28%	-0.67	-0.88	18.8%	24.6%	0.38%	0.49%
<b>GE effects and smaller change in average AD duties</b>	-17%	-0.67	-0.88	11.4%	15.0%	0.23%	0.30%

Source: Ifo Institute

<sup>41</sup> They claim to use the mean elasticities, whereas on inspection of the data provided by Tokarick (2010), it seems to be the median. For ease of comparison we also use median estimates.

## A2 The anti-dumping investigation process in the EU

**Figure A1: Flowchart of the EU anti-dumping investigation process**



Source: Ifo Institute, European Commission (2013)

## A3 Anti-dumping initiations and measures in force against China

**Table A2: Anti-dumping Initiations against China, 1995 - 2005**

Country	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Argentina	1	1	1	0	2	1	9	3	0	2	4
Australia	0	0	0	0	0	1	4	1	2	1	2
Brazil	0	2	2	2	0	0	3	1	2	1	0
Canada	0	1	1	0	0	1	4	2	2	3	0
Chinese Taipei	0	0	0	0	0	0	0	0	0	0	0
Colombia	0	1	0	0	0	0	0	0	0	2	2
Egypt	0	0	0	0	1	2	1	1	1	0	1
European Union	3	2	2	1	3	4	1	4	3	9	8
Guatemala	0	0	0	0	0	0	0	0	0	0	0
India	1	1	5	5	3	4	13	14	6	7	10
Indonesia	0	0	0	0	0	0	0	0	1	1	0
Israel	0	0	1	0	0	0	0	0	0	1	2
Jamaica	0	0	0	0	0	0	0	0	1	0	0
Japan	0	0	0	0	0	0	0	0	0	0	0
Korea, Republic of	0	0	3	0	0	0	0	1	3	1	2
Malaysia	0	0	0	0	0	0	0	1	0	0	0
Mexico	0	3	0	1	0	0	3	2	3	1	5
Morocco	0	0	0	0	0	0	0	0	0	0	0
New Zealand	0	0	0	0	0	0	0	0	1	1	0
Pakistan	0	0	0	0	0	0	0	0	0	0	1
Peru	1	1	0	1	2	0	3	1	2	2	1
Philippines	0	0	1	0	0	0	0	0	0	0	0
Russian Federation	0	0	0	0	0	0	0	0	0	0	0
South Africa	1	3	0	4	2	2	0	0	4	1	5
Thailand	0	0	0	0	0	0	1	0	1	0	0
Trinidad and Tobago	0	0	0	0	1	0	0	0	1	0	0
Turkey	0	0	0	0	1	2	4	5	7	9	4
Ukraine	0	0	0	0	0	0	0	0	1	0	1
United States of America	1	5	0	1	4	3	8	9	9	6	3
Uruguay	0	0	0	0	0	0	0	0	0	0	0
Venezuela, Bolivarian Republic of	0	0	1	4	0	0	0	0	0	0	0
Viet Nam	0	0	0	0	0	0	0	0	0	0	0

Source: Ifo Institute, data from WTO (2015)

**Table A3: Anti-dumping Initiations against China, 2006 - 2014**

Country	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total
Argentina	1	5	9	17	3	3	3	6	2	73
Australia	3	1	2	2	1	3	3	4	4	34
Brazil	11	2	10	4	3	5	13	15	5	81
Canada	1	1	3	3	1	2	2	4	2	33
Chinese Taipei	3	0	0	1	2	0	2	2	0	10
Colombia	9	1	3	3	0	2	2	9	3	37
Egypt	3	2	0	1	0	1	0	1	2	17
European Union	12	6	6	7	8	8	4	3	5	99
Guatemala	0	0	0	0	0	0	0	0	1	1
India	8	11	16	10	11	5	7	7	8	152
Indonesia	1	0	1	2	1	2	2	3	2	16
Israel	0	0	0	0	2	0	0	0	0	6
Jamaica	0	0	0	0	0	0	0	0	0	1
Japan	0	1	0	0	0	0	0	0	1	2
Korea, Republic of	1	5	1	0	0	0	1	1	1	20
Malaysia	0	0	0	0	0	0	2	2	3	8
Mexico	3	3	0	2	2	2	3	6	6	45
Morocco	0	0	0	0	0	1	0	0	0	1
New Zealand	1	1	0	0	1	0	0	0	0	5
Pakistan	1	0	1	3	2	2	1	0	0	11
Peru	0	0	0	1	0	1	1	1	0	18
Philippines	0	0	0	0	0	0	0	0	0	1
Russian Federation	1	0	1	1	0	2	1	0	5	11
South Africa	1	4	1	2	0	2	1	2	1	36
Thailand	3	1	1	1	1	5	3	0	0	17
Trinidad and Tobago	0	0	0	0	0	0	0	0	1	3
Turkey	6	3	5	5	2	0	3	3	4	63
Ukraine	0	2	3	0	0	0	1	1	0	9
United States of America	3	12	10	12	3	5	5	5	7	111
Uruguay	0	0	0	0	1	0	0	0	0	1
Venezuela, Bolivarian Republic of	0	0	0	0	0	0	0	0	0	5
Viet Nam	0	0	0	0	0	0	0	1	0	1

Source: Ifo Institute, data from WTO (2015)

**Table A4: Anti-dumping measures in force against China, 1995 - 2004**

Country	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
<b>Argentina</b>	0	3	4	5	6	8	6	5	13	14
<b>Australia</b>	1	1	2	2	2	2	3	3	4	5
<b>Brazil</b>	2	4	5	8	10	10	10	10	11	13
<b>Canada</b>	3	3	5	5	5	4	6	7	9	10
<b>Chinese Taipei</b>	0	0	0	0	0	0	0	0	0	0
<b>Colombia</b>	0	1	1	1	1	1	0	0	0	0
<b>Egypt</b>	0	0	0	0	0	1	2	4	5	6
<b>European Union</b>	10	16	19	23	25	27	28	28	27	29
<b>India</b>	1	1	3	6	13	15	21	29	38	37
<b>Indonesia</b>	0	0	0	0	0	0	0	0	0	0
<b>Israel</b>	0	0	0	0	2	2	2	2	2	2
<b>Jamaica</b>	0	0	0	0	0	0	0	0	0	1
<b>Japan</b>	0	0	0	0	0	0	0	0	0	0
<b>Korea</b>	0	0	0	1	1	2	1	1	1	5
<b>Malaysia</b>	0	0	0	0	0	0	0	0	1	1
<b>Mexico</b>	7	7	10	11	18	18	18	19	22	22
<b>Morocco</b>	0	0	0	0	0	0	0	0	0	0
<b>New Zealand</b>	3	3	3	3	3	3	1	1	1	1
<b>Pakistan</b>	0	0	0	0	0	0	0	0	0	0
<b>Peru</b>	1	2	2	2	3	5	5	8	8	10
<b>Russian Federation</b>	0	0	0	0	0	0	0	0	0	0
<b>South Africa</b>	4	5	8	9	13	15	15	14	13	13
<b>Thailand</b>	0	0	0	0	0	0	0	1	1	2
<b>Trinidad and Tobago</b>	0	0	0	0	0	1	1	1	1	2
<b>Turkey</b>	0	0	0	1	1	2	3	8	14	20
<b>Ukraine</b>	0	0	0	0	0	0	0	0	0	1
<b>United States of America</b>	25	26	31	33	34	34	35	40	43	50
<b>Uruguay</b>	0	0	0	0	0	0	0	0	0	0
<b>Venezuela</b>	0	0	1	1	1	5	5	5	5	4
<b>Viet Nam</b>	0	0	0	0	0	0	0	0	0	0

Source: Ifo Institute, data from WTO (2015)

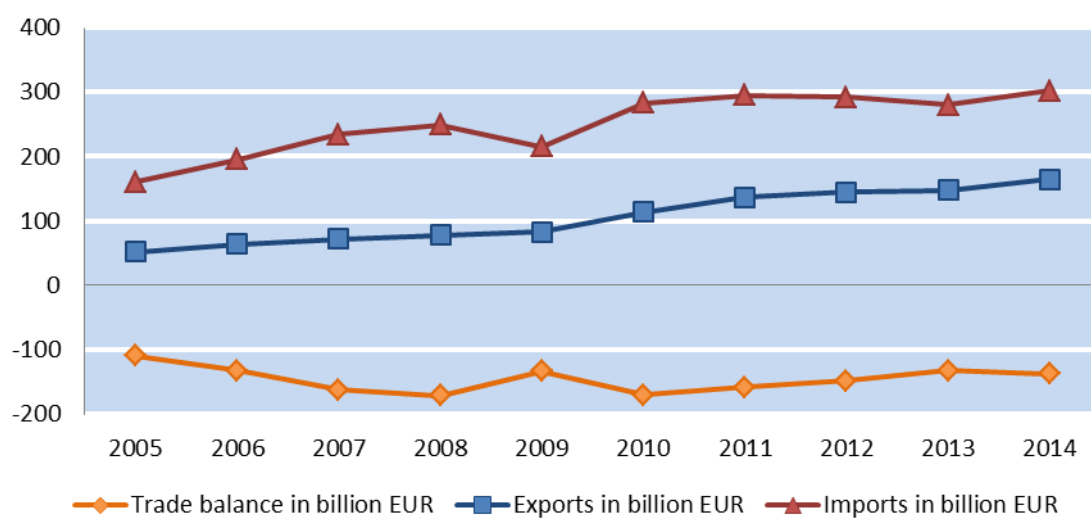
**Table A5: Anti-dumping measures in force against China, 2005 - 2014**

Country	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
<b>Argentina</b>	14	15	14	16	25	33	39	42	43	43
<b>Australia</b>	7	9	9	8	9	7	6	8	10	11
<b>Brazil</b>	12	12	18	21	24	28	30	32	34	45
<b>Canada</b>	11	11	10	11	12	13	13	15	14	16
<b>Chinese Taipei</b>	0	1	2	2	2	4	5	5	6	6
<b>Colombia</b>	0	1	10	10	13	13	12	8	9	13
<b>Egypt</b>	6	7	8	10	9	10	7	5	5	4
<b>European Union</b>	34	39	42	44	54	55	53	50	51	51
<b>India</b>	42	47	50	53	54	67	75	79	77	76
<b>Indonesia</b>	1	2	2	3	3	2	3	5	6	7
<b>Israel</b>	2	1	3	4	3	2	2	1	0	0
<b>Jamaica</b>	1	1	1	1	0	0	0	0	0	0
<b>Japan</b>	0	0	0	1	1	1	1	1	1	1
<b>Korea</b>	6	7	8	12	13	12	9	8	9	10
<b>Malaysia</b>	1	1	1	0	0	0	0	0	2	2
<b>Mexico</b>	25	28	26	9	10	11	12	13	13	21
<b>Morocco</b>	0	0	0	0	0	0	0	0	1	1
<b>New Zealand</b>	2	3	3	3	3	3	4	4	4	3
<b>Pakistan</b>	0	1	2	2	3	3	3	2	4	3
<b>Peru</b>	10	12	12	12	10	9	8	6	6	7
<b>Russian Federation</b>	0	0	0	1	1	2	3	4	5	4
<b>South Africa</b>	14	14	11	12	10	12	12	12	12	11
<b>Thailand</b>	2	2	3	3	5	5	7	6	11	12
<b>Trinidad and Tobago</b>	2	1	1	1	1	1	0	0	0	0
<b>Turkey</b>	28	35	39	39	45	48	47	47	49	52
<b>Ukraine</b>	1	2	2	4	5	6	6	6	6	4
<b>United States of America</b>	56	58	59	67	78	84	87	90	93	93
<b>Uruguay</b>	0	0	0	0	0	0	0	1	1	1
<b>Venezuela</b>	4	4	4	4	4	0	0	0	0	0
<b>Viet Nam</b>	0	0	0	0	0	0	0	0	0	1

Source: Ifo Institute, data from WTO (2015)

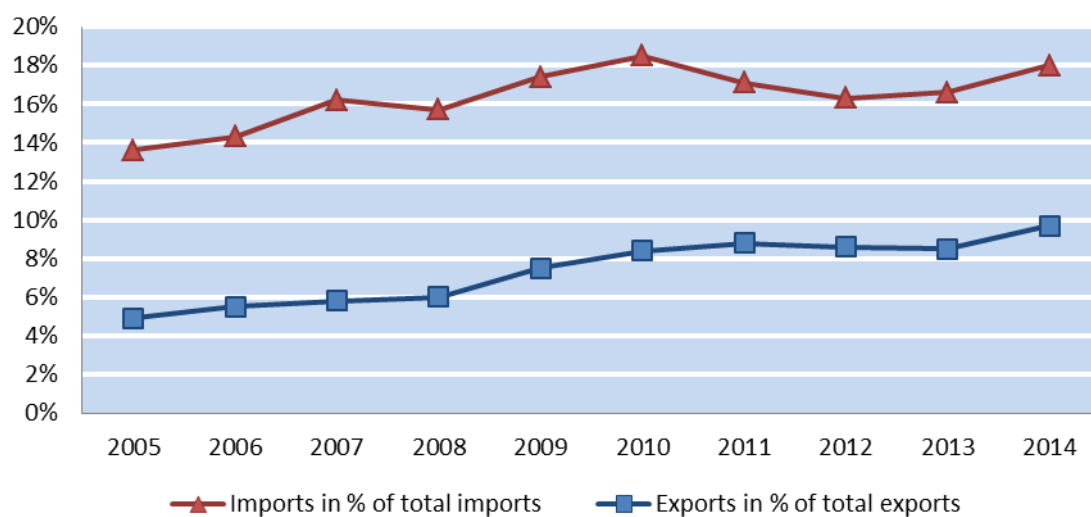
## A4 EU trade with China

**Figure A2: EU 28 trade in goods with China, in bn. EUR**



Source: Ifo Institute, data from Eurostat

**Figure A3: EU 28 trade in goods with China, in % of total trade**



Source: Ifo Institute, data from Eurostat



## A5 Revealed comparative advantage by country and industry

Table A6: Industries revealed comparative advantage by country, 2010

country	Food	Textile	Wood	Paper	Chemicals	Plastic	Minerals	Metals	Machinery	Electrical	Transport	Misc. Manuf.
Argentina	1.99	0.79	1.01	0.81	0.84	0.98	0.80	0.82	0.75	0.86	0.89	1.13
Australia	1.24	0.84	0.93	1.08	0.95	0.88	1.01	1.01	1.01	0.99	0.95	1.00
Brazil	1.53	0.81	1.36	0.81	0.85	0.96	1.21	1.11	0.87	0.85	0.91	0.96
Canada	1.07	0.88	1.21	1.07	0.85	0.90	1.14	1.03	1.00	1.00	0.95	0.98
China	0.85	1.44	1.13	1.21	0.99	0.99	1.05	1.18	1.10	1.13	1.16	NA
France	1.05	1.02	1.01	1.00	0.98	0.99	1.01	0.97	1.01	0.99	1.00	0.98
Germany	0.93	0.94	1.11	1.05	1.00	1.01	1.08	1.00	1.05	1.01	1.03	0.94
India	1.03	1.26	0.95	0.94	1.03	1.09	0.90	1.01	1.04	0.94	0.93	0.95
Indonesia	1.07	1.16	1.27	0.96	NA	0.86	1.12	1.06	0.74	0.91	0.94	0.82
Italy	0.95	1.16	1.15	0.98	0.95	0.92	1.03	1.10	1.09	0.95	1.01	0.90
Japan	0.63	0.81	NA	1.00	0.90	0.94	0.81	0.90	1.12	1.11	1.06	1.01
Korea	0.72	1.04	0.75	0.93	1.12	1.07	0.90	0.97	0.98	1.15	1.13	1.03
Mexico	1.00	0.86	0.78	1.07	0.98	1.04	0.82	0.98	0.90	1.13	1.14	1.02
Netherlands	1.19	0.88	1.02	1.01	1.19	1.08	1.06	0.97	1.00	0.99	0.96	0.89
Russia	0.97	0.72	1.20	0.89	1.24	1.29	1.18	1.10	0.86	0.86	0.87	1.10
South Africa	1.23	0.85	0.89	0.94	0.86	1.12	1.00	0.95	0.90	1.01	0.90	1.10
Spain	1.08	1.14	1.10	0.97	1.01	1.01	1.09	1.02	0.94	0.90	0.97	0.94
Turkey	1.05	1.38	1.09	0.79	0.84	0.97	0.98	1.03	1.05	0.91	1.01	0.94
UK	1.03	1.00	0.90	1.19	0.95	0.99	0.98	1.01	1.01	1.00	0.98	0.96
US	1.02	0.86	1.13	1.07	1.06	1.01	1.02	0.98	1.07	1.06	0.99	0.92

Note: Values greater than one mean that the country has a comparative advantage in that sector

Source: (Leromain & Orefice, 2013)

Table A7: AD cases in force against China by country and sector

Country	Sector	AD cases i.f. 2014
Argentina	Stone / Glass	6
Argentina	Miscellaneous	6
Argentina	Footwear / Headgear	1
Australia	Stone / Glass	1
Brazil	Stone / Glass	7
Brazil	Miscellaneous	6
Brazil	Vegetable Products	1
EU	Stone / Glass	5
EU	Raw Hides, Skins, Leather, & Furs	1
EU	Miscellaneous	1
India	Stone / Glass	5
India	Miscellaneous	1
Indonesia	Stone / Glass	3
South Korea	Stone / Glass	2
South Africa	Stone / Glass	2
South Africa	Vegetable Products	1
USA	Miscellaneous	7
USA	Stone / Glass	3
USA	Animal & Animal Products	3
USA	Vegetable Products	2

Note: Total number of AD in force by country may exceed the aggregate presented earlier because one AD case may affect several sectors, leading to double counting.

Source: Ifo Institute, AD Data from Bown (2015)

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