

China's Joining the WTO: Opportunities for the Australian Agribusiness Sector [1]

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1. Introduction

China first applied to join the GATT (now the WTO) in July 1986. After almost 16 years of painstaking negotiations, China is very close to joining the WTO. When China gets accepted into the WTO, a market with 1.3 billion consumers will be more widely open to the rest of the world. This market represents enormous opportunities for exporters and investors of many other countries. Undoubtedly, it will also bring opportunities to the agribusiness sectors of both China and other countries.

What might be in it for the Australian agribusiness sector? What opportunities may Australia expect? What are the likely challenges Australia may encounter? In this paper, after briefly describing China's preparation for joining the WTO, we highlight the changes that are likely to take place in markets in China after it joins the WTO. We then attempt to identify areas where opportunities may exist for the Australian agribusiness sector to gain increased access to the Chinese market and where cooperation may be possible between the Australian and Chinese agribusiness sectors. We will also point out possible challenges and competition facing the Australian agribusiness sector in the Chinese market. We conclude this paper by addressing some issues that need to be taken into account for the Australian agribusiness sector to be successful in the Chinese market.

2. China's Preparation for Joining the WTO

As early as 1986 when the Uruguay Round (UR) started, China submitted a request to restore its GATT membership (China was a signatory of the GATT in 1948 but the Taiwan Kuomintang government withdrew from the Agreement in 1950). Since then, China has been fully involved in the UR negotiations. Unfortunately, China was unable to reach agreement with its major trading partners before the

Uruguay Agreements were signed. The Chinese leaders believed some developed countries attempted to impose obligations on China that were inconsistent with its status as a developing country and set obstacles to the conclusion of the negotiations.

The failure to restore GATT membership and thus to become a founding member of the WTO affected China's attitudes towards GATT/WTO affairs. Thereafter, the Chinese leaders stated that China had no intention of compromising further on opening its market in exchange for GATT/WTO membership. Joining the GATT/WTO was no longer a hot topic in the media. The negotiation was resumed in 1994 after China's major trading partners expressed their support for an early accession of China to the WTO. However, progress was slow (People's Daily 2000).

When Premier Zhu Rongji visited the USA in April 1999, the Chinese government was ready to give a push to the negotiations by making certain concessions about opening markets. To some extent, it intended to sacrifice agriculture in exchange for greater and longer protection of other sensitive sectors such as banking and communication services. China's commitments on opening the agricultural market were wide and substantial, especially in commodities of interest to the USA (USTR 1999). However, the USA government missed this opportunity under the political pressures of domestic opponents. The Chinese government halted WTO negotiation after USA missiles destroyed the Chinese Embassy in Belgrade in May 1999, which triggered off anti-US feeling. With efforts from both sides, talks were resumed in September 1999, which resulted eventually in reaching China-USA WTO Accession Agreement in November 1999.

The China-US WTO Accession Agreement was a milestone in China's long journey to the WTO. The bilateral negotiations with other concerned parties have been accelerated since then. To date, Mexico is the only WTO member with whom China needs to reach a bilateral agreement. While progress is being made continuously in Geneva to finalise China's accession protocols, uncertainties remain with regard to when China can complete all the procedures and enter the WTO (Yangzi Evening Daily 2001).

One of the key issues under dispute between China and its major trade partners concerns the status with which China should enter the WTO. China insists on joining the WTO as a developing country, which would allow the Chinese government greater flexibility in managing the process of transition as well as reduced urgency to remove policy distortions. In contrast, the USA and some other parties intend to impose stringent disciplines on China's trade behavior, with a concern being whether the accession of China would disturb the order of world trade, given the already big and still rapidly growing size of the Chinese economy and its particular socio-economic system.

Disagreements exist about the level, speed and sector focus of tariff reduction, elimination of various non-tariff barriers of border protection, opening market of services and binding arrangements for implementation of the commitments. The last of these becomes a major issue for the Working Party on the Accession of China in Geneva, whose members will draft the Protocol of Accession. The Chinese leaders and officers in charge have reiterated on various occasions that China will fulfil all the commitments it made, but China will not accept any additional obligations (Zhu, R.J. 24 October, 2000; Long, Y.T. 27 October, 2000).

It should be noted that no matter how the GATT/WTO negotiation was going on, the Chinese government pushed forward the market-oriented reforms of its economic system in a gradual way to prepare China for entering the WTO. In fact, China has initiated a number of steps to reduce trade barriers. For instance, China's average tariff was reduced from over 40 per cent in the early 1990s to 15.3 per cent by January 2001 (see Table 1). The extent of reduction was much greater than what was required by UR agreements for both developing and developed countries. Similar to tariff cuts, China has autonomously implemented a wide range of reform measures in removing non-tariff barriers (NTBs). For example, China has reduced coverage of licence controls substantially since 1992. Trading rights have been granted to foreign and joint venture firms first and then to domestic non-state firms. These measures have made China's trade regime much more liberal than that which prevailed in the 1980s. In the meantime, the Chinese government has also taken steps to improve its domestic regulatory framework covering legal system, firm system, and government institutions.

Table 1. China's Tariff Reduction over Time

Time	Simple average tariff after reduction %	Tariff lines subject to cut	Share as total tariff lines %
January, 1992	43.2	225	3.6
December, 1992	39.9	3371	53.8
December, 1993	36.4	2898	45.6
July, 1995	35.6	23	0.36
April, 1996	23.0	4971	75.9
October, 1997	17.0	4874	69.8

January, 1999	16.5	1014	14.6
January, 2000	16.4	819	11.8
January, 2001	15.3	3462	49

Note: While the nominal rate of protection is high in China as shown by the simple average of tariff, the level of real tariff protection is substantially lower due to legal tariff exemptions and illegal smuggling. Based on official data, the rate of actually collected tariff was as low as 3 per cent in the late 1990s.

Sources: Compiled from various government documents and publications.

China's experience in its journey to the WTO shows that China intends to participate in the multilateral trade system and reform its policies accordingly, provided it can exercise sufficient control over the process and the speed of transition. On the other hand, China's major trading partners wish to gain the benefits from China's market opening up but, in the meantime, are concerned about China entering their own markets with privileges as a WTO member. Thus, while both sides have common interests regarding China's joining the WTO, as in the past there are conflicts and there certainly will also be conflicts in the future. This explains why the process of China's acceptance to the WTO has been so slow.

While the Chinese leaders perceive that accession to the WTO will bring about economic benefits (e.g., improved access to foreign markets, foreign investments and technologies into China which may help China to accelerate economic growth), as well as political benefits (e.g., improving China's reputation and obtaining influence on world affairs, pressure on Taiwan to establish a closer link with China), they recognize the costs, such as expected hardship in structural adjustment, constraints on policy options, and influence on the Chinese society by western culture. Nonetheless, it seems that the Chinese government intends to adhere to some baselines/principles.

China's academia in general is supportive of entering the WTO, although there exist different views on benefits and costs for China and on policy suggestions to the government. In fact, many think that joining the WTO will bring in external pressure to push forward China's ongoing reforms. The public in China is not well informed about the WTO issues and has almost no involvement in policy discussions. So, although China is close to the gate of the WTO, Chinese society has not been well prepared to deal with the complex situation after accession. Some chaos are likely to occur which may disturb the economy and cause irregular policy responses.

3. Changes in the Market Environment Resulting from China's Joining the WTO

No matter what may happen, one thing that seems to be fairly certain is that after China's accession to the WTO, China's market environment will change fundamentally. Major changes include external and internal market conditions, and the framework of regulatory policies. Here we emphasise several specific areas such as improved market access, enhancement of competition, improved environment for foreign direct investment (FDI), and related intellectual property protection.

3.1. Market Opening Up

Although the Protocol of China's accession has not been worked out yet and the Chinese government has not released any details of bilateral agreements, substantial reduction of border protection is widely expected. Agriculture was once regarded as the basis of the national economy and for the achievement of food security. However, China has made substantial compromises in its negotiation with the USA and some other parties in trade of agricultural products. As reported by USDA (2000), upon accession to the WTO, China will:

- establish a 'tariff-only' import regime and eliminate all non-tariff barriers;
- reduce tariff on agricultural products from 22 per cent to 17.5 per cent with the average duty on agricultural products of USA priority interest falling from 31 per cent to 14 per cent;
- use a tariff-rate quota (TRQ) system for certain sensitive commodities under additional requirements to allocate a certain proportion of quotas to non-state trading entities and to redistribute unused quotas by state-trading enterprises to other end users who have an interest in importing;
- permit any entity, including foreign enterprises, to import most agricultural products into any part of China and to engage in the full range of distribution services within a three-year period;
- stop subsidising export of agricultural products;
- cap and reduce trade-distorting domestic subsidies; and
- abide by the terms of the WTO Agreement on Sanitary and Phytosanitary Measures.

As these commitments will be included in China's accession protocol, they will be applied equally to all other WTO members. Thus, China's agricultural market will be more widely opened up, presenting opportunities for exporters of agribusiness products world-wide. In the meantime, the Chinese suppliers will have to face great challenges after reduction of trade barriers.

3.2. Enhanced Market Competition

The accession to the WTO means that the Chinese government accepts all rules and disciplines as mandated in UR Agreements. As a result, China's trade regulatory system must comply with the principles of national treatment and most-favored-nation treatment. Thus, the Chinese government is likely to allow business decisions to be made without much government interference. This is important for agribusiness firms since trade of agribusiness products has been subject for a long time to planned management via state-trading regimes, under which trade decisions are often made on the basis of non-economic considerations and may favour or discriminate certain trade partners or between domestic and foreign firms.

Without politically chosen winners and losers, both the Chinese and foreign firms must compete for market shares by developing and exploiting their own competitive advantages. For this purpose, it is important for Chinese firms to obtain knowledge of foreign markets and for foreign firms to understand the Chinese market. However, the smooth operation of a free market system requires an effective legal system. This cannot be established easily and quickly. Thus, conflicts may be expected during the transition process. Problems may also arise when the national government fails to enforce regional governments to follow national laws and regulations. However, in the long term, China's accession to the WTO will help to foster a competitive market environment in China.

3.3. Improved Environment for FDI

Attracting more foreign direct investment (FDI) is one of the considerations for China to join the WTO. To attract more FDI with advanced technologies into China, China must provide effective protection of intellectual properties as mandated by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). China has committed to fully implement WTO's Agreements on Trade-Related Investment Measures (TRIMS) and TRIPS after its accession to the WTO. As a result, China may revise its regulations over FDI and grant sufficient protection to intellectual properties.

An improved environment for FDI will offer opportunities for both Chinese and foreign firms through the marriage of foreign capital, advanced technologies and managerial skills with China's low labour and raw material costs and large market potential. However, the exploitation of such opportunities will be increasingly based on direct business negotiations between the Chinese firms and foreign firms rather than through government departments as before.

3.4. Challenges Facing China's Agribusiness Sector and its Likely Responses

Several studies (e.g., Arndt et al. 1997; Wang 1997; CEM 1999; Letour 2000; DRC 1998; Zhai 2000) have shown that China entering the WTO is likely to induce a notable increase in demand for agribusiness products, especially those of income-elastic products. China lacks comparative advantages in land-intensive crops (mainly cereals, oilseeds, cotton and sugar crops) and production of such commodities is likely to shrink after opening the market (CEM 1999; Zhang 2000). Consequently, it is expected that China will have to increase imports of major bulk commodities in the long run.

Small farmers involved in the production of bulk commodities may suffer from slow income growth due to competition from imported goods. Agro-processing industries are likely to improve their competitiveness in both domestic and international markets as a result of relatively cheap supplies of raw materials and improved access to external markets. The impacts may vary across different regions within China. The major agricultural regions, such as the Northeast, Northwest, Central China and Southwest, may face greater difficulties while the coastal provinces, which are already economically better-off, may gain from easier access to overseas markets for import and export.

Clearly, the implementation of the commitments by China will lead to substantial structural adjustments and redistribution of benefit among sectors and regions in China. To facilitate the agribusiness sector's ability to face the challenges and in the meantime to capitalize on any opportunities, the government and agribusiness firms are likely to be proactive in dealing with the new situations and to respond to the new situations by taking the following measures:

- to foster domestic agribusiness firms who can compete with foreign competitors both in the Chinese market and overseas market and in the meantime who can involve small farmers in their business operations as suppliers;
- to improve market infrastructure and legal and social services to both agribusiness firms and small farmers;
- to install WTO-consistent instruments to prevent external disturbances in case of need; and
- to assist rural adjustment in line with long-term trend of changing comparative advantages so as to ensure rural people can also benefit from China's joining the WTO.

4. Areas of Opportunity and Cooperation for the Australian Agribusiness Sector

The discussion above suggests that China joining the WTO will bring about increased market access and cooperation opportunities for the agribusiness sector of other countries in the Chinese market. There are three broad areas where increased efforts need to be made by the Australian agribusiness sector in order to secure such emerging opportunities following China's joining the WTO. These areas are:

- capitalising on the improved market access to increase export to the Chinese market
- making use of Australia's technology and expertise to produce in China for the Chinese market
- making use of Australia's technology and expertise to produce in China for other overseas markets.

4.1. Increased Exports to Chinese markets

4.1.1. Wool

Australian fine wool faces few competitors in the international market. Although the Chinese government has taken measures to encourage domestic fine-wool production, Australian wool is better quality and enjoys a good reputation. After China joins the WTO, restrictions on the import of Australian wool to China will be significantly (but gradually) eased. While China's demand for imported wool is significantly affected by China's domestic demand for and export of textiles, it is certain that China will remain a major wool user. Continued reinforcement of the reputation of Australian wool in China and internationally and offering of technical support to the Chinese enterprises in wool processing are likely to enhance Australia's comparative advantage in raw wool production in the long run.

4.1.2. Wheat

In total quantity terms, China's wheat supply has been sufficient to meet demand in recent years. However, under China's present marketing arrangements, high quality wheat cannot be collected and marketed separately to meet the demand of food processing industries, and imports are sought (Tian, Zhou and Cao 2000). After joining the WTO, NTBs to wheat import will be removed. TRQs will be used with a very low tariff for imports within quotas (3 per cent). The above-quota tariff rate will be reduced from the present 114 per cent to 65 per cent by 2004. The quota for the first year after China's acceptance to the WTO is reported to be 7.3 million tonnes and this will be increased to 9.64 million tonnes by 2004. It is thus expected that China's wheat import will be increased from the present low level (Tang and Zheng 2000, p. 206). The USA, Canada and Argentina are the likely major competitors for Australia. The USA has been watching the Chinese wheat market for a long time. With its improved competitiveness following its successful negotiation in its bilateral agreement on China's WTO accession, the USA is likely to increase its wheat export to China (Amponsah, Qin and Wang 1999). How much Australia can gain from China's increased wheat import critically depends on the export subsidies of other major wheat exporters. Australia produces high quality wheat but is yet to do more to project the image of Australian wheat in the China market.

4.1.3. Barley

China's demand for barley has increased notably in the past years, primarily due to the rapid expansion of the beer industry (Tian and Chudleigh 1999). In order to ensure stable high quality beer, major brewers in China resort to using almost 100 per cent imported barley for their beer production. Major sources of supply include Australia, Canada and France. After China joins the WTO, barley imports will be free of any restrictions and there will only be a single 9 per cent tariff rate. The tariff rate for malt will also be significantly reduced from 30 per cent to 10 per cent. Thus, barley and malt import is expected to increase. However, further increases in market share of Australia's barley in the Chinese market requires Australian producers to maintain their competitiveness in price and quality.

4.1.4. Dairy

Present per capita consumption of milk in China is about 6 kg per year, much lower than that in many other countries. The Chinese government has started to encourage its residents to increase their consumption of dairy products (see, for example, Ministry of Agriculture 2000). The consumption of dairy products by wealthier people, especially in the urban areas, has been on the increase in recent years (Li 1999, Wei and Viney 1999). Chinese consumption of dairy products at present is largely confined to milk, milk powder, ice cream and yoghurt due to taste preference. However, in view of the Japanese and Korean experience (Song and Sumner 1999), with further increased disposable income by the Chinese and with overseas influence, it is expected that change in taste and thus the consumption of butter and cheese will take place, especially among the younger generations. China agreed to a substantial reduction of tariff rates for dairy products after WTO accession. For instance, the tariff rate for cheese will be reduced from the present 50 per cent to 12 per cent and yoghurt from 50 per cent to 10 per cent. This is certainly helpful for stimulating consumption of dairy products by reducing costs and increasing diversity. Although a change in tastes is likely to be a slow process, early preparation for entry into the market is necessary. Some EU countries started to work on this market in China some ten years ago. The Australian dairy industry needs to take action soon. The EU, the USA and New Zealand are likely to be the major competitors for Australia in this market.

4.1.5. Beef

Beef consumption started to become popular among the Han majority people from the early 1980s. Since then per capita consumption of beef has increased by about 100 per cent but the absolute quantity is still very small (less than 3 kg in urban areas and less than 1 kg in rural areas in 1999). Beef is only about 1/5 of pork consumption in urban area and about 1/12 in rural areas. In the near future, a large volume of beef export to China is unlikely. However, in the longer term, with further changes in tastes and increased demand for higher quality beef, a niche market for imported beef will be developed.

China's commitment to tariff reduction from 45 per cent to 12 per cent by 2004 and implementation of WTO consistent SPS measures will be helpful for a growth of beef imports. Major beef producers in the world include Brazil, China, the EU and the USA. Due to the Mad Cow Disease problem, the EU is unlikely to be competitive in the Chinese market. However, the USA will be the major competitor for Australia. Australia needs to project a high quality image of Australian beef in China's markets. When selling Australian beef to Chinese markets, it is

necessary to take Chinese cooking methods into consideration.

4.1.6. Animal skins

China is a major user of animal skins for producing leather products for exports. Domestic supply is constrained by capacity to expand animal production. China's import of raw hides and leather in 1999 was over 2.3 billion USA dollars (SSB 2000, p. 591). Australia, as a major supplier of raw hides, is likely to export more to the Chinese market. China's demand for raw hides in future will be affected by its export of leather products and its consciousness about environment protection – raw hide processing is highly environment polluting. Improvement of technologies in both leather processing and pollution control is urgently needed by Chinese enterprises. It is an area where Australian firms may be able to help.

4.1.7. Cooking oils

In China, priority cannot be given to the production of oilseeds due to the pressure to produce grains. As a result of increased demand by rural residents and food processing industries, a large quantity of oilseeds and vegetable oils has been imported in recent years and China has now become the largest vegetable oil importer. China agrees to use a tariff-only system for all vegetable oils except for soybean oil, which is subject to TRQ before 2006. Vegetable oil imports are expected to grow, and demand for high quality vegetable oils will be on the increase. This provides potential for Australia's canola oil export to China. There is a need to promote canola oil's cholesterol-free feature, targeting the wealthier groups of consumers.

Some other products may not be able to be exported to the Chinese market in a large volume. However, it may be possible to find a niche market for them. These include, for example, some fruits (e.g., cherry, plum, mango), some aquatic products (e.g., lobster), sugar and cotton.

4.2. Produce in China for the China market

China itself is a huge market. A middle class population is taking shape and there are some consumers who are extremely rich. Given the 1.3 billion population base, the number of consumers with strong purchasing power in China is impressive. Even if one per cent of the population has a strong purchasing power, this translates to a total of 13 million. With the increase in consumers' income, their health awareness is also increasing. Those wealthier consumers look for better quality and healthy agricultural products. However, China's current production methods and marketing arrangements are not capable of producing and marketing such products of high quality and high health standard. Given the presence of such a demand and low labour cost in China, opportunities exist for Australian agribusiness firms to cooperate with China's local entrepreneurs by making use of Australia's technology and expertise to produce in China for the Chinese market. Using product branding and their own marketing channels, the potential gains from such a venture can be enormous when the brands get accepted in the Chinese market.

4.3. Produce in China for other markets

A similar venture that Australian agribusiness firms may find worth exploring is to produce in China for overseas markets by making use of Australia's technology and expertise. Given the low labor cost, some of the agribusiness products produced in China are very competitive in the international market. However, due to low health standards and quality, the exportability of such products is very limited. In addition, China's firms also suffer from limited intelligence about overseas markets and less effective marketing strategies. It is possible for Australia's expertise and China's low labour cost advantage to be combined to produce high quality of those exportable products. After establishing a good reputation for their products in international markets, Australian agribusiness firms will be able to reap the benefits for years to come from such a venture.

4.4. Some qualifications on the above three approaches

Each of the above three approaches have their own advantages and disadvantages. Export of commodities to China requires relatively less knowledge of the Chinese markets and is easier to manage. However, the competition is likely to be strong. Australian agribusiness firms must be well prepared to compete with many suppliers that may have better positions, such as the USA and EU, whose agricultural products are often subsidized. The profit margin is likely to be thin. Thus, apart from ensuring quality reputation, Australian firms need to work hard to keep the cost and hence the price low.

It is expected that the Chinese government will gradually relax its compulsory grain procurement system and reform the land tenure policies. These changes will have important implications for foreign firms who want to establish agribusiness enterprises in China. When producing in China, foreign agribusiness firms have better control over the raw material production process, which is essential to ensure quality of final outputs. For foreign food processing firms, contract production may be used to collect raw materials from small producers; this allows quality assurance. Such firms that produce or process in China for the Chinese market could sell their higher quality products through designated chain-stores and supermarkets to establish their product brands and product reputation in the market.

Producing in China for exporting is likely to get strong support from the Chinese government. At present, Chinese firms have very limited knowledge of overseas markets and their products virtually have no reputation to overseas consumers. Thus, China's ability to take

advantage of easier access to overseas markets is quite limited. Australian agribusiness firms in general have advantages in this area and their efforts to co-operate with Chinese agribusiness firms to export Chinese products will be supported by governments at the central and regional levels. China has initiated a program to establish a number of 'exporting processing zones' in major cities. This offers great opportunities for foreign firms that want to establish their export-oriented businesses in China.

5. Concluding Comments

China, as a big market, is of relevance mainly if the Australian agribusiness sector can secure business opportunities in that market and make a profit out of it. China's joining the WTO will make the access to that market much easier and thus offers businesses in the Australian agribusiness sector an exciting historical opportunity that it must not miss.

It must be noted, however, China's opening-up to increased trade will be gradual and not an over-night event. On the other hand, preparation for doing business in the market is a continual process. For firms in the Australian agribusiness sector to be successful in the Chinese market, it needs to pay attention to the following areas.

- **Get prepared:** First, prepare the right products for the Chinese market. Research on the Chinese market for the product of interest is essential. A personal business trip to the market can be most beneficial. In addition, there is a need to monitor changes in tastes and preference by the Chinese for some products in which Australia has an interest so that timely market operations can be undertaken. Second, get familiar with business practice in China. The value of getting familiar with business practice in China by the Australian agribusiness firms cannot be overemphasised. In the future, business dealings will be mainly with individual private companies rather than with government trading companies. In addition, understanding Chinese culture in general is also very important. Quite often, business failure is due to cultural misunderstanding.
- **Longer-term planning:** In most cases establishing a market in China is a painful process. The pain is attributable to a number of factors, but mainly political influence and differences in social and business culture. To establish a market in China takes time. Thus, long-term vision is essential. If a firm expects to go to China today and bring profits back tomorrow, then it should stay home. Sometimes a firm can expect to have profitable returns in two to three years time. Investment in training staff who understand the Chinese market and in establishing goodwill with business contacts in China will be most rewarding in the long run.
- **Sufficient funds for initial market establishment** It is essential to have sufficient funds at the outset to tap the Chinese market. If a firm does not have a good sum of money to start with, it will most probably run out of money before making any profit. In this sense, it is often better to embark on a joint effort or an industry effort in order to establish a product in the Chinese market. The more capital a firm has at its disposal for tapping the Chinese market, the greater will be its chances of success.
- **Industry or group effort :** To promote products such as meats, dairy products, and canola oil to the Chinese market, an industry effort is necessary. For other products, such as cherry and plum, a group effort may be sufficient.
- **Be innovative:** When China's market becomes open to the world, the competition will be tough. To succeed in the Chinese market, Australian agribusiness firms must be creative and innovative in their business operations and in promoting their products. In China, returns from well-designed advertisements are very high. Efforts by firms in the Australian agribusiness sector to promote the image of their products in the Chinese market are essential.

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