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A Comparative Analysis of the United States' Trade Frictions with China, Japan and South Korea, 1985-2016

Murat BAYAR* & Tuğba BAYAR**

Abstract
This article investigates the interplay between interstate economic and security relations by conducting a comparative analysis of United States' (U.S.) trade frictions with China, Japan and South Korea. The data demonstrate that the U.S. responded to its East Asian allies during the Cold War with retaliatory measures when they started to make trade surpluses against the U.S. Thus, it could be expected that the U.S. would respond to its mounting trade deficit against China after 2001 even more decisively, since it has had territorial disputes with this country. However, our analysis indicates that the U.S. followed a more docile approach with China until its 2008 economic crisis. This puzzle is explained by a number of economic and political factors. Our analysis concludes with insights for the coordination of trade and security policies at the governmental level and for the World Trade Organization's dispute settlement mechanism.
Key words: *Trade, security, retaliation, United States, Japan, South Korea, WTO.*

A.B.D.'nin Çin, Japonya ve Güney Kore ile Ticari Sürtüşmelerinin Karşılaştırmalı Bir Analizi, 1985-2016

Özet
Bu makale, A.B.D.'nin Çin, Japonya ve Güney Kore ile yaşadığı ticari sürtüşmelerin karşılaştırmalı bir analizini yaparak ülkelerin ekonomik ve güvenlik ilişkileri arasındaki etkileşimi incelemektedir. Veriler göstermektedir ki, A.B.D., Soğuk Savaş döneminde Doğu Asyalı müttefikleri kendisine karşı ticaret fazlası vermeye başladığında bu ülkelere misilleme kabilinde tedbirlerle karşılık vermiştir. Bu nedenle, A.B.D.'nin toprak anlaşmazlığı yaşadığı Çin'e karşı 2001'den beri vermekte olduğu devasa ticaret açığına çok daha kararlı tepki vermesi beklenebilir. Ancak, analizimiz gösteriyor ki 2008 ekonomik krizine değin ABD Çin'e karşı daha pasif bir yaklaşım göstermiştir. Bu muamma çesitli ekonomik ve siyasi sebeplerle açıklanmaktadır. Analizimiz, ticaret ve güvenlik politikalarının hükümet seviyesinde koordinasyonu ve Dünya Ticaret Örgütü ihtilafların halli mekanizması alanlarında sonuçlar çıkarmaktadır.
Anahtar Kelimeler: *Ticaret, güvenlik, misilleme, A.B.D., Japonya, Güney Kore, DTÖ.*

* Assistant Professor Dr., Department of Political Science, Social Sciences University of Ankara, Ankara.
** Instructor Dr., Department of International Relations, Bilkent University, Ankara.

1. INTRODUCTION

Trade between China and the United States (U.S.) has expanded dramatically since 1979 and reached its highest volumes after China's accession to the World Trade Organization (WTO) in 2001. During the first seven years of China's membership in the WTO, the U.S. trade deficit against this country reached an unprecedented USD 258.5 billion.[1] During the same period, the U.S. government accused China of following unfair trade practices, including currency manipulation. The central question to this article is, why did the U.S. fail to use retaliatory economic and diplomatic measures against China, as it used against Japan and South Korea under similar circumstances in previous decades? This is a puzzling relationship both from realist and neoliberal perspectives, because Japan and South Korea have been close allies of the U.S., which, on the other hand, has territorial disputes with China.[2] Thus, if anything, the U.S. could be expected to retaliate more against China, whose relative trade gains could translate into military power.

This article conducts a comparative analysis of U.S.' trade frictions with China, Japan and South Korea for the period 1985-2016 with an extensive use of descriptive statistics in order to: (1) reveal retaliation patterns of the U.S. against its allies, and (2) the degree to which these patterns apply to its relations with China. Our analysis offers insight into trade relations with allies and rivals, as well as for the limitations of the World Trade Organization's dispute settlement mechanism.

2. TRADE WITH ALLIES

2.1. Japan-U.S. trade relations

Lovett et al. noted that the Kennedy Round, as part of the General Agreement on Tariffs and Trade (GATT) negotiations, significantly decreased tariffs in 1967 especially for the American automobile market without getting reciprocal reductions from Japan and other developing countries. Since Western European countries kept their markets protected against Japanese cars, it was inevitable for Japan to focus on the American market while enjoying its most favored nation status in this country. The increasing Japanese competitiveness was attributed to its technological and managerial innovations, as well as its undervalued currency (Yen) against the U.S. dollar (USD).[3]

The U.S. had already started to make a trade deficit against Japan in 1965, and it reached USD 1 billion in 1971. While this amount was still negligible compared to the U.S. gross domestic product (GDP) at the time (USD 5.525 trillion),[4] the Nixon

1 U.S. Census Bureau, Trade in Goods (Imports, Exports and Trade Balance), 2017, http://www.census.gov/foreign-trade/balance/index.html (retrieved on: March 22, 2017).

2 Robert G. Sutter, Chinese Foreign Relations: Power and Policy since the Cold War, (Lanham, MA: Rowman & Littlefield Publishers, Inc., 2008.)

3 William A. Lovett, Alfred E. Eckes, and Richard L. Brinkman, U.S. Trade Policy: History, Theory, and the WTO, (New York: ME Sharpe, 1999.)

4 United Nations Data, 2017, data.un.org/Data.aspx?d=SNAAMA&f=grID%3A101%3BcurrID%3AUSD%3BpcFlag%3A1 (retrieved on: March 22, 2017)

administration immediately applied a 10 percent import surcharge on all Japanese exports. Langdon stressed that the Nixon administration was cautious about the worsening trade imbalance and American competitiveness, so they intended to urge the Japanese to revalue their currency as well. In 1977, the Orderly Marketing Arrangement restricted Japanese TV and steel exports to the U.S. The Nixon, Ford, and Carter administrations all pressured Japan to adopt "voluntary" export restraints and to remove Japanese trade barriers against American products.[5]

In 1978, Japan surpassed the United Kingdom (U.K.) as the primary holder of U.S. government securities. Although Japanese capital investment helped the U.S. to finance its growing budget deficit, it also prevented the U.S dollar from losing value against Yen and kept Japanese exports relatively cheap and competitive. The Japanese-U.S. trade dispute escalated by the arrests of Hitachi and Mitsubishi employees in 1982 on the charge of industrial espionage from the IBM, and by Mitsui's attempt to sell steel at artificially low prices.[6] The U.S. Congress officially condemned Japan in 1985 for its protectionist and interventionist policies that created an unfair trade and investment environment for American companies.[7]

By the early 1980s, the U.S. trade deficit against Japan had already risen sharply due to Japanese automobile exports and protectionism of the Japanese domestic market. The increase in the U.S. deficit led American manufacturers to urge their government for further retaliation that finally turned the tide down in 1987. The U.S. started to increase its pressure on Japan in 1992 after its trade deficit accelerated.[8] The Clinton administration continued to force Japan to restrain its exports, which slowed down again in the mid-1990s.[9] A major factor behind these policies is the complaints filed by American companies against unfair practices, such as currency manipulation and industrial espionage.[10] The U.S. trade numbers with Japan, as well as with South Korea, for the period 1985-2016 are presented in Table 1:

A review of the Japan-U.S. trade relations shows that the U.S. reacted to its trade deficit against this country almost immediately by pushing for voluntary export reductions and other means at the risk of destabilizing its key ally's economy during the Cold War. This is striking from both realist and neoliberal points of view, because Japan has been dependent on the U.S. military (especially nuclear) umbrella, so this country was unlikely to translate its relative trade gains into security threats against the U.S.

5 Frank Langdon, 'Japan-United States Trade Friction: The Reciprocity Issue', Asian Survey, 23(5), 1983, pp. 653-666.

6 Frank Langdon, 'Japan-United States Trade Friction: The Reciprocity Issue', Asian Survey, 23(5), 1983, pp. 653-666.

7 William A. Lovett, Alfred E. Eckes, and Richard L. Brinkman, U.S. Trade Policy: History, Theory, and the WTO, (New York: ME Sharpe, 1999.)

8 Ibid.

9 Cristina Davis, 'Japan: Trade and Security Interdependence', Foreign Policy in Focus, 2(18), 1997, pp. 1-3.

10 Gerald L. Curtis, 'U.S. Policy toward Japan from Nixon to Clinton: An Assessment' in Curtis (ed.) New Perspectives on U.S.-Japan Relations, (New York: Japan Center for International Exchange, 2001.)

Table 1: *U.S. Trade with Japan and South Korea, 1985-2016* [11] *

Year	Japan: Trade USD Billions	Japan: % Change	Japan: Deficit / U.S. GDP	South Korea: Trade USD Billions	South Korea: % Change	South Korea: Deficit / U.S. GDP
1985	-46.2		0.011	-4.1		0.001
1986	-55.0	19	0.012	-6.4	56	0.001
1987	-56.3	2	0.012	-8.9	39	0.002
1988	-51.8	-8	0.010	-8.9	0	0.002
1989	-49.1	-5	0.009	-6.3	-29	0.001
1990	-41.1	-16	0.007	-4.1	-35	0.001
1991	-43.4	6	0.007	-1.5	-63	0.000
1992	-49.6	14	0.008	-2.0	33	0.000
1993	-59.4	20	0.009	-2.3	15	0.000
1994	-65.7	11	0.009	-1.6	-30	0.000
1995	-59.1	-10	0.008	1.2	-25	0.000
1996	-47.6	-19	0.006	4.0	233	0.000
1997	-56.1	18	0.007	1.9	-53	0.000
1998	-64.0	14	0.007	-7.5	295	0.001
1999	-73.4	15	0.008	-8.2	9	0.001
2000	-81.6	11	0.008	-12.5	52	0.001
2001	-69.0	-15	0.006	-13.0	4	0.001
2002	-70.0	1	0.006	-13.0	0	0.001
2003	-66.0	-6	0.006	-13.2	2	0.001
2004	-76.2	15	0.006	-20.0	52	0.002
2005	-83.3	9	0.006	-16.2	-19	0.001
2006	-89.7	8	0.006	-13.6	-16	0.001
2007	-84.3	-6	0.006	-13.2	-3	0.001
2008	-74.1	-12	0.005	-13.4	2	0.001
2009	-44.7	-40	0.003	-10.6	-21	0.001
2010	-60.1	34	0.004	-10.1	-5	0.001
2011	-63.1	5	0.004	-13.2	31	0.001
2012	-76.5	21	0.005	-16.6	26	0.001
2013	-73.3	-4	0.004	-20.7	25	0.001
2014	-67.6	-8	0.004	-25.1	21	0.001
2015	-68.9	2	0.004	-28.3	13	0.002
2016	-68.9	0	0.004	-27.7	-2	0.001

* Negative trade (USD billions) indicates U.S. deficit against the stated country.
Sources: U.S. Census Bureau, Trade in Goods, and Bureau of Economic Analysis, 2017.

11 U.S. Census Bureau, Trade in Goods (Imports, Exports and Trade Balance), 2017, http://www.census.gov/foreign-trade/balance/index.html (retrieved on: March 22, 2017) and Bureau of Economic Analysis, National Economic Accounts (U.S. GDP in current dollars), 2017, http://www.bea.gov/national/index.htm#gdp (retrieved on: March 22, 2017)

2.2. South Korea-U.S. trade relations

Similar to the Japan-U.S. case, South Korean exports increased by 21 percent between 1975 and 1985 causing a trade imbalance against the U.S. Accordingly, American companies complained that South Korea was subsidizing its exporters and adopting protectionist policies towards its domestic market. In response, the U.S. restricted South Korean imports and pressured this country to liberalize its trade policies.[12] For instance, the Carter administration immediately sought for voluntary export restraints when South Korea almost tripled its non-rubber shoe exports to the U.S. between 1975 and 1976. Other U.S. measures included charging anti-dumping suits in 1983 and accusing South Korea for manipulating its exchange rate in 1988.[13] South Korea eventually yielded to U.S. demands.[14]

Ballo and Cunningham, and Odell noted that the U.S. retaliation was harsher and more effective on South Korea than on Japan.[15] While South Korea's relative economic weakness can partly account for this difference, the U.S. might also have benefited from its previous experience with Japan's trade practices.[16]

3. RETALIATION PATTERNS

Milner underlined that internationally-oriented companies resist the protectionist demands of domestically-oriented ones in order to keep markets open at home and abroad. As trade interdependence increases at the international level, the former group increases its economic and political influence, which in turn leads to further trade liberalization.[17]

In the Japanese and South Korean cases, however, lobbying efforts were unified for retaliation, because both internationally- and domestically-oriented American companies were put into disadvantage by the trade practices of these East Asian countries: while small- and middle-sized companies were losing market shares to Japanese and Korean exports, U.S. exporters were not gaining access to their markets. Subsequently, the electoral competition in the U.S. diverted trade policies into a protectionist direction.[18] Yet, the U.S. government obfuscated its retaliation by pushing for voluntary export restraints in Japan and South Korea, rather than increasing

12 Chung-in Moon, 'Complex Interdependence and Transnational Lobbying: South Korea in the United States', International Studies Quarterly, 32(1), 1988, pp. 67-89.

13 Ibid; and Walden Ballo and Shea Cunningham, 'Trade Warfare and Regional Integration in the Pacific: The USA, Japan and the Asian NICs', Third World Quarterly, 15(3), 1994, pp. 445-458.

14 John S. Odell, 'The Outcomes of International Trade Conflicts: The US and South Korea, 1960-1981', International Studies Quarterly, 29(3), 1985, pp. 263-286.

15 Ibid.

16 Wontack Hong, Trade and Growth: A Korean Perspective, (Seoul: Kudara International, 1994.)

17 Helen V. Milner. 'Resisting the Protectionist Temptation: Industry and the Making of Trade Policy in France and the United States during the 1970s' International Organization, 41 (4), 1987, pp. 639-665.

18 Daniel Y. Kono. 'Optimal Obfuscation: Democracy and Trade Policy Transparency', American Political Science Review, 100 (3), 2006, pp. 369-384.

its own tariffs and quotas, due to reputational concerns in the international trade regime.[19]

In 1985, the U.S. trade deficit against Japan exceeded 1 percent of the U.S. GDP which led to the market oriented sector specific (MOSS) talks.[20] As the deficit continued to rise, the U.S. reacted with the Semiconductor Agreement to prevent the dumping of Japanese semiconductors exports in 1986, economic sanctions in 1987, the Structural Impediments Initiative (SII) in 1992, and the Framework for New Economic Partnership in 1993. In 1994, the Japan-U.S. trade frictions were largely settled by the Uruguay Round, which constituted the foundation of the WTO.[21] Table 2 summarizes the U.S. retaliation patterns against Japan and South Korea in the 1980s and the 1990s.

Table 2: *U.S. Retaliation Years Against Japan and South Korea*

Retaliation Year	Japan			South Korea		
	Trade USD Billions	% Change	Deficit / U.S. GDP	Trade USD Billions	% Change	Deficit / U.S. GDP
1985	-46.2	192 (1981-1985)	0.011	-4.1	21 (1975-1985)	0.001
1986	-55.0	19 (1986)	0.012			
1987	-56.3	2 (1987)	0.012			
1989				-6.3	54 (1985-1989)	0.001
1992	-49.6	20 (1990-1992)	0.008	-2.0	33 (1992)	0.000
1993	-59.4	20 (1993)	0.009	-2.3	15 (1993)	0.000

Sources: U.S. Census Bureau, Trade in Goods, and Bureau of Economic Analysis, 2017.

Similarly, the U.S. trade deficit against South Korea increased by 39 percent over previous year in 1987 (see Table 1). Subsequently, the U.S. left this country out of the list of eligible countries for General System of Preferences in 1989. When South Korea increased its trade surplus again in 1992, the U.S. demanded voluntary restrictions on Korean imports and insisted for large-scale property rights protection in 1993. [22]

19 Beth Simmons, 'International Law and State Behavior: Commitment and Compliance' in International Monetary Affairs, American Political Science Review, 94(December, 2000), pp. 819-836; and Robert O. Keohane, After Hegemony: Cooperation and Discord in the World Political Economy, 1st ed., (Princeton and Oxford: Princeton University Press, 1984.)

20 Stephen D. Cohen, 'United States-Japan Trade Relations', Proceedings of the Academy of Political Science, 37(4), 1990, pp. 122-136.

21 Frank Langdon , 'Japan-United States Trade Friction: the Reciprocity Issue', Asian Survey, 23(5), 1983, pp. 653-666; Gerald L. Curtis, 'U.S. Policy toward Japan from Nixon to Clinton: An Assessment', in Curtis (ed.) New Perspectives on U.S.-Japan Relations, (New York: Japan Center for International Exchange, 2001); Michael Duffy, 'Trade and Politics: Mission Impossible', Time, January, 20, 1992, http://www.time.com/time/magazine/article/0,9171,974715,00.html?promoid=googlep (retrieved on January 2, 2017); and Ronald E. Dolan and Robert L. Worden (eds.), Japan: A Country Study, (Washington: GPO for the Library of Congress, 1994.)

22 Walden Ballo and Shea Cunningham, 'Trade Warfare and Regional Integration in the Pacific: The USA, Japan and the Asian NICs', Third World Quarterly, 15(3), 1994, pp. 445-458; and John S. Odell, 'The Outcomes of International Trade Conflicts: The US and South Korea, 1960-1981', International Studies Quarterly, 29(3), 1985, pp. 263-286.

Yet, trade deficit may become more problematic when parties have security disputes with each other.[23] President Nixon and his National Security Adviser Henry Kissinger "prided themselves on being realist" (p. 10) and believed that Japan would eventually channel its economic capability into military strength unless it was restrained by the U.S.[24] These remarks point out their concerns for relative losses against allies during the Cold War. Thus, in contrast to Gowa's argument, trade with an ally is not necessarily perceived as a positive security externality by policymakers.[25]

This article focuses on the 1985-2016 period due to the availability of comparable statistics for China, Japan and South Korea. Overall, the U.S. took retaliatory measures against its East Asian allies in the studied period when at least one of the following conditions was satisfied: (1) its deficit reached USD 4.1 billion (South Korea, 1985) or (2) its deficit/GDP ratio exceeded 0.011 (Japan, 1985). Based on these patterns, this article suggests that the U.S. could be expected to react against China's trade surplus at least under the same conditions (putting the bar for retaliation high), since they have not been allies but had territorial disputes with each other (e.g. on the status of Taiwan, South China Sea) and rivaled for regional hegemony.[26]

4. ANALYSIS

The thresholds for U.S. retaliation against its East Asian allies for the studied period are found to be a certain deficit amount (USD 4.1 billion) and a certain deficit/GDP ratio (0.011). Table 3 indicates that the U.S.' trade deficit against China satisfied these conditions simultaneously in 2003 with USD 124.1 billion deficit and 0.011 deficit/GDP ratio.

The China-U.S. case parallels Japanese and South Korean cases in several ways. Scott noted that the first five years of China's membership in the WTO cost the U.S. 1.8 million jobs.[27] The U.S.-China Economic and Security Review Commission's 2007 report claimed that China owed its success after 2001 largely to its unfair practices, such as export industry subsidies, counterfeiting, and lax health, safety, and environmental regulations.[28] Similarly, the Council on Foreign Relations stressed

23 Robert Powell, 'Absolute and Relative Gains in the International Relations Theory', The American Political Science Review, 85(4), 1991, pp. 1303-1320.

24 Gerald L. Curtis, 'U.S. Policy toward Japan from Nixon to Clinton: An Assessment', in Curtis (ed.) New Perspectives on U.S.-Japan Relations, (New York: Japan Center for International Exchange, 2001.)

25 Joanne Gowa, Allies, Adversaries, and International Trade, (Princeton, NJ: Princeton Univ. Press, 1994.)

26 John J. Mearsheimer, The Tragedy of Great Power Politics, (New York and London: W.W. Norton and Company, 2001.)

27 Robert E. Scott, 'Wal-Mart's Reliance on Chinese Imports Costs U.S. Jobs', Economic Policy Institute, June 26, 2007. http://www.epi.org/author_publications.cfm?author_id=292 (retrieved on: February 21, 2017.)

28 U.S.-China Economic and Security Review Commission of the Congress, '2007 Report to Congress'. Washington, DC., 2007, http://www.uscc.gov/annual_report/2007/report_to_congress.pdf (retrieved on: January 4, 2017.)

that intellectual property right violations cost U.S. companies around USD 200 billion a year, most of which took place in China. The Council argued that neither the U.S. nor the WTO could urge China to fight against piracy because of insufficient WTO-established metrics for enforcement and modest punishment mechanisms in the Chinese legal system. In other words, it is not enough to pass anti-piracy laws if they are not enforced effectively.[29]

Table 3: U.S. Trade Deficit Against China, 1985-2016 [30]

Year	Trade USD Billions	% Change	Deficit / U.S. GDP	Year	Trade USD Billions	% Change	Deficit / U.S. GDP
1985	-0.006		0.000	2001	-83.1	-1	0.008
1986	-1.7		0.000	2002	-103.1	24	0.009
1987	-2.8	65	0.001	**2003**	**-124.1**	**20**	**0.011**
1988	-3.5	25	0.001	2004	-162.3	31	0.013
1989	-6.2	77	0.001	2005	-202.3	25	0.015
1990	-10.4	68	0.002	2006	-234.1	16	0.017
1991	-12.7	22	0.002	2007	-258.5	10	0.018
1992	-18.3	44	0.003	2008	-268.0	4	0.018
1993	-22.8	25	0.003	2009	-226.9	-15	0.016
1994	-29.5	29	0.004	2010	-273.0	20	0.018
1995	-33.8	15	0.004	2011	-295.2	8	0.019
1996	-39.5	17	0.005	2012	-315.1	7	0.020
1997	-49.7	26	0.006	2013	-318.7	1	0.019
1998	-56.9	14	0.006	2014	-344.9	8	0.020
1999	-68.7	21	0.007	2015	-367.2	6	0.020
2000	-83.8	22	0.008	2016	-347.0	-6	0.019

Sources: U.S. Census Bureau, Trade in Goods, and Bureau of Economic Analysis, 2017.

Despite the satisfaction of retaliation conditions as early as 2003, the U.S. government did not take significant action against this country until its 2008 economic crisis. To illustrate, the U.S. Government Accountability Office reported that five American companies petitioned against China's market disruptions to the U.S. International Trade Commission (ITC) as of September 2005. While the ITC found disruptions in three of them, U.S. government refused to apply duties and quotas.[31]

29 Independent Task Force of the Council on Foreign Relations, U.S.-China Relations: An Affirmative Agenda, a Responsible Course, (New York: The Council on Foreign Relations Inc., 2007.)

30 U.S. Census Bureau, Trade in Goods (Imports, Exports and Trade Balance), 2017, http://www.census.gov/foreign-trade/balance/index.html (retrieved on: March 22, 2017) and Bureau of Economic Analysis, National Economic Accounts, 2017, http://www.bea.gov/national/index.htm#gdp (retrieved on: March 22, 2017)

31 U.S. Government Accountability Office, U.S.-China Trade: The United States has not Restricted Imports Under the China Safeguard, September 2005, http://www.gao.gov/new.items/d051056.pdf (retrieved on: February 7, 2017.)

A number of factors can account for this unprecedented trade deficit and lack of retaliation. First, China's cheap labor, infrastructure, high production potential, and steady demand from world markets constituted major advantages in its manufacturing and exports.[32] Despite the conventional wisdom, Branstetter and Foley underlined that American Multinational Enterprises (MNEs) primarily produced for the Chinese domestic market, rather than exporting to their home country.[33]

Second, the Clinton administration was criticized for approving China's entry to the WTO in 2000 (effective in 2001) without receiving sufficient assurances, thus losing political leverage over this country.[34] Apparently, the U.S. government expected that China's WTO membership would bring a win-win situation and decrease the U.S. deficit. Based on U.S. International Trade Commission's (USITC) analysis, the Clinton administration assumed that China would fully comply with the WTO agreements, avoid currency manipulation, and liberalize its market after its accession to the WTO. Accordingly, the USITC estimated a 10.1 percent increase in U.S. exports and only a 6.9 percent increase in China's imports after 2001.[35] Yet, Table 3 shows that the U.S. trade deficit against China increased by 318 percent between 2001 and 2016.

The U.S. government's optimism may partly be attributed to their confidence in China's potential to democratize and cooperate, as developmentalism and the democratic peace theory suggest.[36] President Clinton declared in 1992 that, "our strategic interests and moral values both are rooted in this goal [democratic peace]. As we help democracy expand, we make ourselves and our allies safer."[37] In parallel, President Bush underlined in his National Security Strategy statement in 2006 that, "as economic growth continues, China will face a growing demand from its own people to follow the path of East Asia's many modern democracies, adding political freedom to economic freedom. Continuing along this path will contribute to regional and international security".[38]

32 Kevin H. Zhang, 'China's Foreign Trade and Export Boom', in Zhang (ed.) China as the World Factory, (London and New York: Routledge, 2007), pp. 9-26.

33 Lee Branstetter and C. Fritz Foley, 'Facts and Fallacies about U.S. FDI in China', National Bureau of Economic Research (NBER) Working Paper Series 13470, Issues in October 2007, http://www.nber.org/papers/w13470 (retrieved on: February 22, 2017.)

34 Carlo Pelanda, The Grand Alliance: The Global Integration of Democracies, (Milan: Franco Angeli, 2007.)

35 Robert E. Scott, 'The High Cost of the China-WTO Deal', Economic Policy Institute, February 1, 2000, http://www.epi.org/publication/issuebriefs_ib137/ (retrieved on February 27, 2017)

36 Howard J. Wiarda, Political Development in Emerging Nations: Is there still a Third World, (Belmont, CA: Wadsworth, 2004); Christopher Layne, 'Kant or Cant: The Myth of the Democratic Peace', International Security, 19(2), 1994, pp.5-49; and Joanne Gowa, Ballots and Bullets: The Elusive Democratic Peace, (Princeton, New Jersey: Princeton University Press, 1999.)

37 Piki Ish Shalom, 'For a Democratic Peace of Mind: Politicization of the Democratic Peace Theory', Harvard International Review, May 2, 2007, http://hir.harvard.edu/for-a-democratic-peace-of-mind (retrieved on: March 3, 2017.)

38 The White House, The National Security Strategy of the United States of America, March 2006, https://www.state.gov/documents/organization/64884.pdf (retrieved on March 6, 2017.). p. 41.

However, expectations of the Clinton and the Bush administrations for China's democratization were far from being achieved as of 2016.[39] Yet, this outcome should not come with a surprise, since China's government declared in 2006 that it aimed to use this "period of strategic opportunity" to consolidate the Communist Party rule.[40] Furthermore, China's President Hu Jintao (2003-2012) announced in October 2007 that their democracy objective was the expansion of "intra-Party democracy."[41] As a matter of fact, political experiences of China, Japan and South Korea are different from each other, since the latter two countries developed their economies and democratized under the U.S. hegemony.[42]

Third, internationally- and domestically-oriented American companies have diverged in their interests and lobbying efforts, unlike in Japanese and South Korean cases. A U.S. Congressional report underlined that several American companies lost their motivation to lobby against China's unfair practices as they invested more and more in this country, although those practices threatened overall U.S. economic interests.[43]

Bivens and Scott compared China's currency manipulations with the policies of South Korea and Taiwan in the 1980s and 1990s, and stressed that China's malpractices surpassed all others.[44] The report underlined several, yet futile, attempts of the U.S. Congress and president to pressure China for abandoning its unfair practices.[45] The European Union (EU) also increasingly discussed retaliating against China due to this country's poor performance in fulfilling its WTO commitments.[46]

39 Arch Puddington and Tyler Roylance, Populists and Autocrats: The Dual Threat to Global Democracy, Freeedom in the World, The Freedom House, 2017, https://freedomhouse.org/report/freedom-world/freedom-world-2017 (Retrieved on February 18, 2017.)

40 Federation of American Scientists, China's National Defense in 2006, Information Office of the State Council – People's Republic of China, December 29, 2006, www.fas.org/nuke/guide/china/doctrine/wp2006.html (Retrieved on March 2, 2017.)

41 The 17th National Congress of the Communist Party of China 2007, 'Hu Jintao Charts Roadmap for China: Sustainable Growth, Greater Democracy', http://english.cpcnews.cn/92243/6283199.html (Retrieved on January 7, 2017.)

42 Kellee S. Tsai, Capitalism without Democracy, (Ithaca and London: Cornell University Press, 2007.)

43 U.S.-China Economic and Security Review Commission of the Congress, '2007 Report to Congress'. Washington, DC., 2007, http://www.uscc.gov/annual_report/2007/report_to_congress.pdf (retrieved on: January 4, 2017.)

44 Robert E. Scott and L. Josh Bivens, 'China Manipulates Its Currency? A Response is Needed', September 25, 2006, http://www.epi.org/publication/pm116/ (retrieved on February 19, 2017.)

45 Thomas Lum and Dick K. Nanto, 'China's Trade with the United States and the World'. Washington, DC: Congressional Research Service (CRS) Report for Congress, November 2004, http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1017&context=key_workplace (retrieved on February 19, 2017.)

46 Paolo D. Farah, 'Five Years of Chinas WTO Membership: EU and US Perspectives on China's Compliance with Transparency Commitments and the Transitional Review Mechanism', Legal Issues of Economic Integration, 33(3), 2006, pp. 263-304.

5. AFTERMATH

Right before the 2008 economic crisis, China's foreign exchange and gold reserves reached USD 1,493 billion, almost twice as big as its closest follower Japan's USD 881 billion.[47] Furthermore, China became the second largest holder of U.S. Treasury securities (19 percent of all U.S. Treasury securities) after Japan and the primary holder of the securities of U.S. agencies and government-sponsored enterprises (23 percent of all agency/enterprise securities) among foreign investors.[48] The total value of U.S. securities held by China reached USD 699 billion in 2006,[49] whereas Chinese securities held by the U.S. was only USD 74 billion (3 percent of all Chinese securities).[50]

China invested its surplus in the U.S. government securities that can be liquidated faster than investments in fixed American assets (e.g. land and production facilities) in a future conflict.[51] Bardhan and Jaffee's analysis showed that the wholesale of U.S. government securities by China in exchange for Yuan or Euro assets would skyrocket U.S. interest rates and inflation, which would devastate the U.S. economy.[52] Whether such a scenario is likely, the Chinese government already threatened the U.S. to sell its dollar holdings unless the U.S. withdrew its demands for the revaluation of Yuan.[53] A Congressional report underlined that "various Chinese government officials are reported to have suggested that China could dump (or threaten to dump) a large share of its holdings to prevent the United States from implementing trade sanctions against China's currency policy" (p.1).[54]

On this matter, U.S. economists expressed three different views on the eve of the 2008 economic crisis: (1) Ben Bernanke, the former chairman of the U.S. Federal Reserve Board, suggested that there was no problem with having a trade deficit as long as the trade partner invested its surplus in the U.S.; (2) Paul Krugman, a Nobel prize winner economist, advocated that American financial markets were not immune to a third-world-type economic crisis, during which trade partners would not hesitate to divert their investments elsewhere; and (3) Gregory Mankiw, another foremost

47 Central Intelligence Agency, World Factbook, Rank Order, 2008, https://www.cia.gov/library/publications/download/download-2008/ (retrieved on January 10, 2017.)

48 Congressional Budget Office, Foreign Holdings of U.S. Government Securities and the U.S. Current Account, 2007, http://www.cbo.gov/ftpdocs/82xx/doc8264/06-26-ForeignHoldings.pdf (retrieved on: January 14, 2017.)

49 Wayne M. Morrison and Marc Labonte, 'China's Holdings of U.S. Securities: Implications for the U.S. Economy', Congressional Research Service, August 19, 2013, http://fas.org/sgp/crs/row/RL34314.pdf (retrieved on: March 24, 2017.)

50 Federal Reserve Bank of New York, 'Report on Foreign Portfolio Holdings of U.S. Securities', June30, 2006, http://ticdata.treasury.gov/Publish/shl2006r.pdf (retrieved on: March 24, 2017.)

51 World Trade Organization (WTO), Trade Profiles: China, http://stat.wto.org/CountryProfile/WSDBCountryPFView.aspx?Language=E&Country=CN (Retrieved on January 10, 2017.)

52 Ashok D. Bardhan and Dwight M. Jaffee, "Global Capital Flows, Foreign Financing and US Interest Rates", Fisher Center Working Papers 303, 2007.

53 'China Threatens 'Nuclear Option' of Dollar Sales', The Telegraph, August 8, 2007, http://www.telegraph.co.uk/finance/markets/2813630/China-threatens-nuclear-option-of-dollar-sales.html (Retrieved on: January 22, 2017.)

54 Wayne M. Morrison and Marc Labonte, China's Holdings of U.S. Securities: Implications for the U.S. Economy, October 2, 2008, h http://www.dtic.mil/dtic/tr/fulltext/u2/a488378.pdf (Retrieved on January 22, 2017.)

economist, argued that trade deficit was the symptom of low national saving ratio and a major financial crisis was unlikely but possible.[55] The repercussions of the 2008 crisis largely vindicated Krugman's view.

To note, China has put forward some efforts to liberalize its economy and international trade in order to comply with its obligations since its accession to the WTO in 2001. China has amended numerous municipal laws and eliminated several non-tariff barriers. However, China is still pursuing state directed policies that are not entirely compatible with WTO rulings, which have proven particularly ineffective in enforcing exchange rate regimes. Furthermore, China's authoritarian and nontransparent regime hinders the ability of the WTO and the U.S. to monitor and punish defection.[56] In the meantime, China's veto power in the United Nations Security Council has become critical after 2001 when the U.S. launched wars in Afghanistan, the Middle East and North Africa.

As a result, China added substantial relative gains in all economic indicators vis-à-vis the U.S. between its WTO membership and the 2008 economic crisis. For instance, China's annual industrial growth rate hit 23 percent in 2007, while U.S.' annual industrial growth rate remained around 4 percent (one of the nine components of national power).[57]

Similarly, the comparative national power (CNP) index, which has been developed by the Chinese Academy of Social Sciences (CASS) to examine the international balance of power, points out that China's CNP score was 37 in 1989, 53 in 2000, and 65.2 in 2006, compared to a benchmark U.S. score of 100.[58] These results show that China achieved a 16-unit increase in eleven years between 1989 and 2000 and a 12.2-unit further increase in the following six years. In other words, China gained significant momentum in expanding its national power, including military power, after its WTO membership.

55 Greg Mankiw, 'Is the U.S. Trade Deficit a Problem?', March 31, 2006, http://gregmankiw.blogspot.com.tr/2006/03/is-us-trade-deficit-problem.html (retrieved on February 21, 2017.)

56 Morris Goldstein, Currency Manipulation and Enforcing the Rules of the International Monetary System, Presented at the Conference on IMF Reform Institute for International Economics, Washington, DC. September 23, 2005, https://piie.com/commentary/speeches-papers/currency-manipulation-and-enforcing-rules-international-monetary-system (retrieved on: February 20, 2017.)

57 Hans J. Morgenthau, Kenneth W. Thompson and W. David Clinton, Politics among Nations: The Struggle for Power and Peace, 7th edition, revised by Kenneth W. Thompson and W. David Clinton (1st edition in 1948 by Hans J. Morgenthau), (New York: McGraw Hill, 2006.)

58 Michael Pillsbury, China Debates the New Security Environment, National Defense University Press, 2000, https://www.files.ethz.ch/isn/104682/2000-01_China_Debates_Future.pdf (Retrieved on January 24, 2016); and Chinese Academy of Social Sciences, 2007, www.fas.org/nuke/guide/china/doctrine/pills2/part08.htm (Retrieved on January 24, 2016)

Table 4: Annual Economic İndicators of China and the U.S., 2001-2007 [59]

	United States of America		People's Republic of China	
	2001	**2007**	**2001**	**2007**
Industrial production growth	-3.7%	4.2%	10%	22.9%
GDP (PPP)	$10,128 billion	$13,843 billion	$4,500 billion	$10,210 billion
GDP per capita (PPP)	$36,300	$43,800	$3,600	$7,800
GDP real growth rate	0.3%	2.9%	8%	11.1%
Unemployment rate	4%	4.8%	10% (urban)	4.2% (urban)
Current acct. balance	-$541.8 billion	-$811.5 billion	$31.17 billion	$249.9 billion
Forex/gold reserves	$85.94 billion	$65.89 billion	$412.7 billion	$1,493 billion

Source: The World Factbook, 2017.

As a matter of fact, the U.S.-China Economic and Security Review Commission pointed out that China's use of anti-satellite weapons revealed its increasing military capabilities. Taiwan's defense capability against a potential Chinese attack has also diminished as the latter party is eagerly investing in the blue-water technology (e.g. new class submarines with longer ranges and greater strike capabilities). The Congressional report also warned against the outsourcing of U.S. defense components to China-based manufacturers, as this process increased import-dependency of U.S. army-procurement. The report concluded that the modernization of Chinese armed forces, military doctrine, and integrated operation capabilities were creating an ever-increasing challenge for the U.S. and its East Asian allies.[60]

6. CONCLUSION & DISCUSSION

This paper develops variables and measurements from previous U.S. trade frictions and applies them to China-U.S. trade relations. Our comparative analysis shows that the U.S. did not react to its trade deficit against China as effectively and decisively as it did against its East Asian allies. Subsequently, China has utilized its WTO membership to accumulate unprecedented relative gains and to increase its military power at the expense of its trade partners.

This paper attributes the ineffectiveness of U.S. retaliation primarily to three factors. First, the false expectations of the Clinton administration for China's will to democratize and cooperate put security concerns into a secondary place. Once China was allowed in the WTO without establishing strong monitoring mechanisms and assurances, the U.S. lost a critical leverage over this country. Second, the WTO did

59 The World Factbook, 2017, https://www.cia.gov/library/publications/resources/the-world-factbook/index.html (Retrieved on: March 4, 2017.)

60 U.S.-China Economic and Security Review Commission of the Congress, 2007 Report to Congress. Washington, DC, https://www.uscc.gov/sites/default/files/annual_reports/2007-Report-to-Congress.pdf (Retrieved on: January 22, 2016.)

not have authority on financial matters, including currency manipulation, which allowed a critical loophole in its trade regime. Third, the interests and lobbying power of big U.S. corporations, many of which outsourced to or produced in China, have marginalized the complaints of small- and medium-sized companies against China's unfair trade practices. A final reason may be that the priority of the U.S. after the 9/11 was its wars abroad, during which it needed China's support, at least neutrality, at the United Nations Security Council.

Despite its limitations, the WTO has constituted a major platform for retaliation. Increasingly since 2008, the U.S. authorities have filed violations of China to the WTO dispute settlement system.[61] Recent cases indicate that Chinese disputes are mainly gathering around issues like subsidiaries given to certain companies or sectors, price comparison measures (DS516), control over foreign exchange rate, tariff rate quotas (DS492 or DS517), and renewable energy (DS452). As of March 2017, China had become subject of 39 complaint cases within the WTO. Twenty-one of these complaints were made by the U.S. followed by eight E.U. cases.[62] Fourteen out of 21 U.S. complaint cases were launched by the Obama administration.

As a result of the joint complaints by the E.U. and the U.S., as well as Japan, the WTO dispute settlement system has found Chinese practices in violation of international trade law and finalized all cases at the expense of China.[63] Although China came up with counterarguments to defend its policies, it abided by and implemented the rulings of the dispute settlement body.[64]

In conclusion, this paper argues that a state may fail to respond to its mounting trade deficit effectively if its domestic constituencies are divided and economic and security bureaucracies are not aligned. Trade deficit may become particularly problematic if it is given against a rival country, which can translate its gains in the economic arena into military power. As the overarching trade institution, the World Trade Organization has proven effective in addressing unfair trade practices when joint complaints are filed by major members, whereas its lack of authority on financial matters (e.g. currency manipulation) remains a hurdle. Overall, this paper suggests that economic and security policies need to be coordinated especially when security disputes exist with trade partners.

61 World Trade Organization, Dispute Settlement, DS252.

62 World Trade Organization, Disputes by country, https://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm (Retrieved on March 2, 2017.)

63 World Trade Organization, Dispute Settlement, DS511.

64 World Trade Organization, Dispute Settlement, DS394.

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